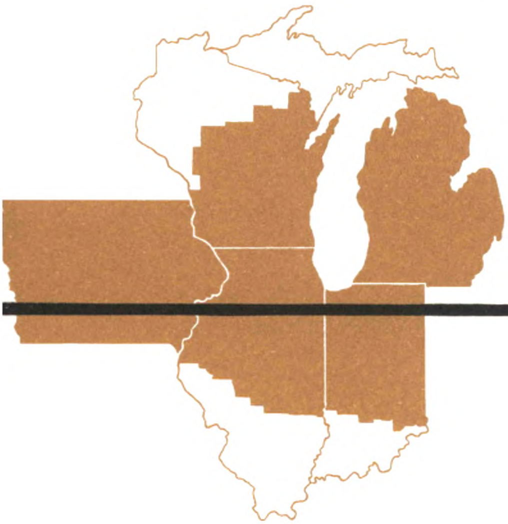
A review by the **Federal Reserve Bank of Chicago**

Business Conditions



1962 May

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THE Trend OF BUSINESS

Business activity continued to rise in the first quarter of 1962, but at a substantially slower pace than prevailed during most of last year. Gross national product—the total spending on goods and services—was at an annual rate of nearly 550 billion dollars in the January-March period, slightly more than 1 per cent greater than in the fourth quarter of 1961 and 10 per cent above the first quarter low. This 10 per cent increase slightly exceeds the gains in the first year of business expansion beginning in 1949, 1954 and 1958.

Total spending probably will rise less rapidly in the future than in the past year. Clearly, successive annual gains in spending approaching 10 per cent would probably reflect substantial price inflation.

About 11 billion dollars, or one-fifth, of the rise in activity between the first quarter of 1961 and the first quarter of 1962 was attributable to a switch from inventory liquidation at a 4 billion dollar annual rate to accumulation at a rate of about 7 billion dollars. In earlier postwar upswings the inventory factor had accounted for one-third or more of the first year rise in activity.

The passing of the steel strike threat largely removes the danger of an excessive build-up of steel inventories which would have been liquidated in the second half of 1962 whether or not a work stoppage occurred. At the end of February total business inventories were 3.3 billion, or 3.6 per cent, higher than a year earlier. Much emphasis has been placed upon higher steel and auto inventories. Nevertheless, only one-third of the rise in inventories during the past year has been in durable goods including the manufacturing, wholesale and retail levels, despite the fact that total inventories of durable goods are larger than those of soft goods.

Sales of virtually all types of goods have risen and inventories have been increased to accommodate this larger volume of business. Over-all sales rose more than inventories, as is typical during the first year of business recoveries, with the result that the ratio of stocks to sales for all business declined to 1.5, about the same as in the spring of 1955 and 1959.

Steel output starts to slide

Among major steel users, it is believed that the auto, machinery and appliance makers made substantial efforts to increase inventories as a hedge against a possible steel strike. In November 1961, before the rush of orders developed, steel was being produced at a rate of 106 million tons per year. As production and orders increased, it was commonly anticipated that steel production would rise to a near record rate of about 140 million tons in March, a level well within the industry's potential.

Actually, the peak steel rate was reached in mid-February at 127 million tons. In April, after the strike threat had passed, output was declining toward 120 million tons and was expected to fall appreciably further.

According to *Iron Age,* steel inventories in the hands of consumers and warehouses reached a level of about 17 million tons in April, only 3.5 million more than last fall. In the first half of 1959, preceding a strike, it is estimated that steel stocks were increased by 12 million tons.

Consumer buying strengthens

Retail sales in the first quarter were at a record annual rate of over 228 billion dollars. This was 6.5 per cent above the same period of 1961 and was about the same as the increase in personal income.

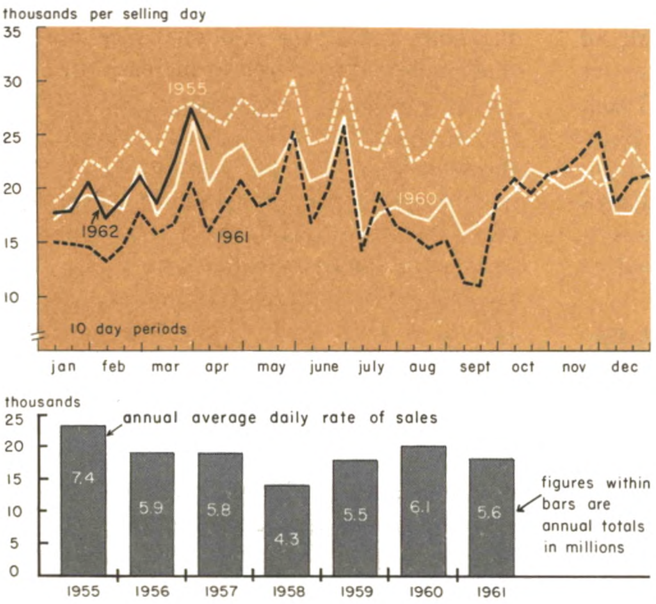
In March retail sales were boosted by a rise in deliveries of new cars. Including imports, deliveries were at a seasonally adjusted annual rate of about 6.9 million, the best performance since last November when the new models were introduced. The excellent level of sales during March caused a number of producers to step up production by adding overtime, second shifts or Saturday work. As a result, the daily rate of production rose in March for the first time this year. Despite the rise in output, inventories declined somewhat during the month for the first time since the model changeover period last fall. Inventories of domestically produced cars totaled almost 1 million on April 1, but based on March deliveries, dealers had only a 43-day supply in stock, the lowest in five years.

Total sales of automotive retailers (including new and used cars, parts, accessories and other items) were at an annual rate of almost 42 billion dollars in the first quarter. This was a new high, 19 per cent above the same period of 1961 and 16 per cent above the first quarter of 1955 when unit sales were at a substantially higher rate.

All categories of retailing have been doing appreciably better than last year. For nondurable goods, which had declined very little during the recession, sales increases have been more modest than in the case of durables—first quarter sales being only 4 per cent higher than in the same period of last year.

March and April sales of various types of merchandise, especially items handled by department stores and clothing stores, must be interpreted against the later date of Easter. In 1961 Easter Sunday was on April 2. This year it came three weeks later, on April 22. In view of this shift, the fact that Seventh District department store sales in the four weeks ending March 31 were 3 per cent higher than the comparable period of last

Spring sales of domestically produced autos highest since 1955 record



year was a remarkably strong showing.

For the nation there was a year-to-year decline of 2 per cent in department store sales in the four weeks ending March 31. However, after adjustment for seasonal trends, including the later date of Easter, sales of the nation's department stores were at a record level for the month of March, slightly above the previous high set in December and 8 per cent higher than in March 1961.

Construction contracts higher

Last fall a Government estimate pointed to an increase of about 5 per cent in construction outlays in 1962. Construction contract information so far this year suggests that any revision in that projection will be up rather than down. For the first two months of the year, contracts reported by F. W. Dodge for the nation were 14 per cent above the high level of the same period of 1961 while in the Midwest contracts were up 17 per cent.

Public works, particularly highways and sewerage systems, and large "high-rise" apartment buildings have shown the greatest gains in construction contract awards thus far. Contracts for new manufacturing plants also are running well ahead of last year.

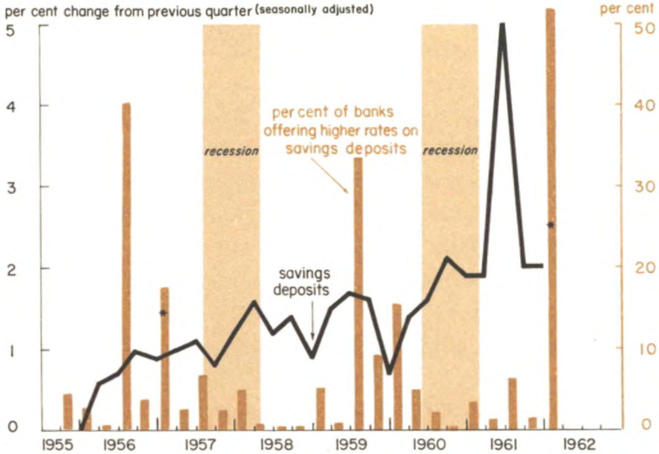
In contrast, builders' plans for construction of single-family homes suggests little, if any, gain from last year, despite somewhat lower interest rates and increased availability of mortgage loans. This situation could change as the year moves on, but at present it appears that new home building, exclusive of apartments, will not exceed the 1961 total.

Time deposits rise at Midwest banks

Time deposits, after rising rapidly at Midwest banks during 1961, registered especially large increases in the early months of 1962. The gain last year repeats the pattern of earlier years when economic activity was in the early stage of recovery following mild recession. At the end of 1961, total time deposits of member banks in the Seventh Federal Reserve District had reached 11.2 billion dollars, an increase of 12 per cent from the year-earlier figure. In 1954 and 1958, similar years of recovery from recession, time deposits rose 5 and 9 per cent, respectively.

The particularly vigorous rise in the early months of 1962 was associated with announcements by many banks of increases in interest rates paid on savings and other types of time deposits. At all member banks in the District, time deposits increased 3 per cent in January and an additional 2 per cent in February. Based on evidence from a group of large banks in major metropolitan areas for which information is available weekly, the rise has continued in March and April (see chart). For all member banks in the United States the results were very similar although the gains varied by region. Would the faster growth of time deposits turn out to be a temporary spurt or was it the beginning of a new era of bank expansion in the investing of savings? Past experience, while not providing a specific answer, may shed some light on

Savings deposits have grown faster during recessions and following increases in interest rates paid by banks



*Date of revision of regulation permitting higher rates to be paid on time deposits. Based on data for member and nonmember banks in District metropolitan areas.

this intriguing question.

Effective January 1, the Federal Reserve Board and the Federal Deposit Insurance Corporation permitted commercial banks to raise interest rates on time deposits above the previous maximum of 3 per cent, if they desired to do so, and state regulations did not specify lower limits. The new maximums are 4 per cent on deposits of one year or longer and 3½ per cent on deposits of from six months to one year.

The rate ceiling had last been raised on January 1, 1957, from 2½ to 3 per cent. Prior to this, relatively few banks were paying the maximum permissible rate on time deposits. At the beginning of 1956, for example, the most frequent rate offered by banks in metropolitan areas in the Seventh District was 1 per cent. About midyear, however, many banks raised rates and by the beginning of the fourth quarter, over one-half of the banks were paying 2 per cent, but only about 1 in 20 was paying the existing ceiling rate of 2½ per cent.

This situation contrasts sharply with the autumn of 1961, when 86 per cent of banks in District metropolitan areas were offering the maximum of 3 per cent for savings deposits and nearly all were offering 3 per cent on other types of time deposits.

Although the demand for bank credit has not been especially strong in the early months of 1962, a substantial number of member banks boosted rates on time deposits in January. Of all member banks in the District, 39 per cent raised rates on savings deposits, while two-thirds posted higher rates on other time deposits.

Such increases were more common among the larger than the smaller banks. Nearly 60 per cent of the banks with total deposits of 50 million dollars or more boosted rates, often to the new maximum of 4 per cent on both savings and other time deposits maintained for one year or more. In the 10-50 million dollar size class, about one-half of the banks raised rates and among banks having less than 10 million of total deposits, about one-third instituted higher rates, but relatively few of these banks boosted them to 4 per cent, except on time certificates.

Rate increases on savings deposits were especially widespread in Illinois and Michigan. In Iowa and Wisconsin relatively few banks raised rates on savings deposits but about two-thirds increased rates on other time deposits to the new maximum of 4 per cent.

In Indiana, where state regulatory authorities maintained the maximum permissible rate at 3 per cent, relatively few banks increased rates on time deposits. Some banks which had been paying less than 3 per cent raised rates to that level, but the number was not large.

The effect of interest rates

The volume of personal savings—the major source of time deposits—is affected by many factors, including the level of personal income and spending and expectations about the future. The share of the personal savings held in the form of time deposits is, in turn, influenced by many additional factors, including the rate of interest paid by banks.

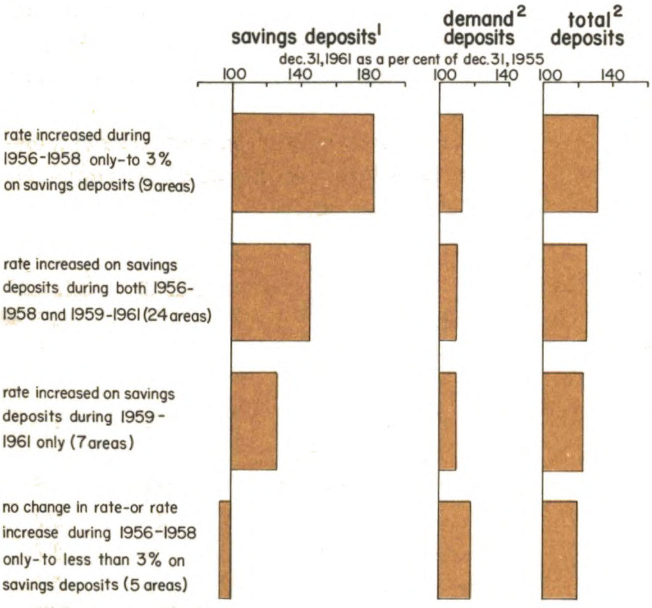
Some impression of the factors affecting growth of time deposits may be gained from data available for savings deposits of both member and nonmember banks in metropolitan areas of the Seventh District (see chart). In early 1956, savings deposits in these banks began to rise rapidly. This was a period of high business activity and strong credit demand, during which a large proportion of the banks raised rates paid on savings deposits. Other thrift institutions also boosted their rates during this period.

Effective January 1, 1957, the rate ceiling on time deposits was raised from 2½ to 3 per cent. In subsequent months, some banks posted higher rates and toward year-end business activity declined. Both of these developments appear to have stimulated further gains in the growth of savings deposits in the fourth quarter of 1957 and the early months of 1958.

With business activity rising rapidly in 1959, the rate of growth of savings deposits declined slightly in the third quarter and then dipped sharply in the fourth quarter even though a significant proportion of the banks had begun to offer higher rates in the third quarter. The slowdown in the growth of savings deposits may be traceable largely to the effects of the nationwide steel strike and, to a lesser extent, the sharp rise in yields on other debt securities.

The increase in savings deposit growth during the second quarter of 1961 reflects in part the transfer of funds from time certificates to savings accounts in Detroit after

Deposit gains have been greatest in areas where banks raised rates on savings deposits



[1] Includes both member and nonmember banks. Member banks in metropolitan areas hold over 85 per cent of savings deposits at all District member banks.

[2] Includes only member banks. Demand deposits are for individuals, partnerships and corporations.

several banks there began to offer 3 per cent on savings as well as on time certificates.

A clearer indication of the effect of changes in interest rate on the growth of time deposits is obtained by comparing areas where the "prevailing rates" were different. Between the end of 1955 and the end of 1961, the largest over-all gains in savings deposits were generally reported by banks in areas where the prevailing interest rates were increased to the maximum of 3 per cent during 1956-58 (see chart on page 6). Moreover, in areas where

Seventh District member bank time deposits

Savings deposits account for more than four-fifths of Seventh District member bank time deposits. They consist of funds deposited to the credit of one or more individuals, or of a corporation, association or other organization operated primarily for religious, philanthropic, charitable, educational, fraternal or other similar purposes and not operated for profit. Subsequent to January 1, 1962, the maximum permissible interest rate (except in states having more restrictive laws or regulations) is 4 per cent on deposits held for one year or more and $3\frac{1}{2}$ per cent for less than one year. Depositors may be required to give not less than 30 days' notice of intended withdrawal.

Certificates of deposit are for specified amounts of funds and generally are issued with specified maturities. They are payable at expiration of the specified time, not less than 30 days from date of deposit, or upon the expiration of the specified time or upon notice in writing given not less than 30 days before the date of repayment. Ownership is evidenced by a negotiable or nonnegotiable certificate. Corporations are substantial holders of CD's because maturities can be tailored to meet their needs. Negotiability enhances their attractiveness as a liquid short-term investment. Maximum permissible rates (except in states having more restrictive laws or regulations) are: less than 90 days, 1 per cent; 90 days to 6 months, $2\frac{1}{2}$ per cent; 6 months to 1 year, $3\frac{1}{2}$ per cent; and 1 year or more, 4 per cent.

Open accounts include time deposits pledged for repayment of personal loans, time deposits of a bank's own trust department, Christmas Club funds and similar deposits. They are evidenced by a written contract subject to terms somewhat similar to those for certificates of deposit but are unlike certificates in that funds may be added or withdrawn from time to time. Maximum permissible interest rates are the same as for certificates of deposit of comparable maturities.

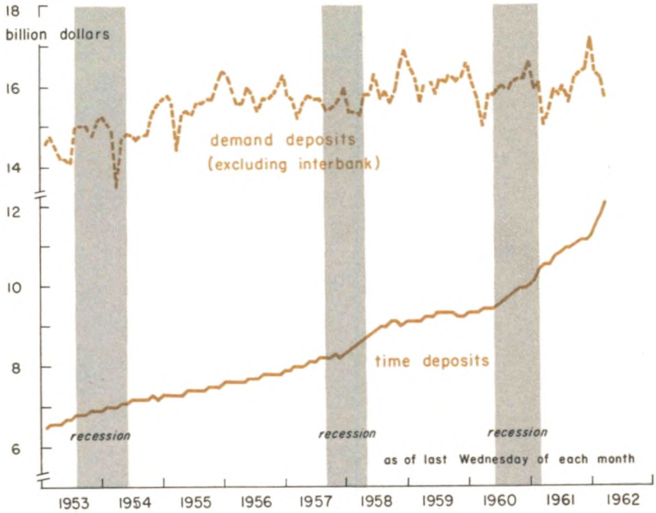
The distribution of Seventh District member bank time deposits as of December 31, 1961 is shown below:

	Million dollars	Per cent
Savings	9,458	84.3
Other time*	1,213	10.8
State and local governments	408	3.6
Foreign governments, central banks, etc.	99	0.9
U. S. Government	20	0.2
Domestic banks	10	0.1
Foreign banks	9	0.1
TOTAL	11,217	100.0

*Includes certificates of deposit and open accounts held by individuals, partnerships and corporations.

interest rates on savings deposits were increased twice, that is, during 1956-58 and again in 1959-61, the gains in savings balances exceeded those in areas where rates were boosted only during the latter period. Declines in savings balances were confined largely to areas where the prevailing interest rate on savings deposits remained unchanged or was below 3 per cent at the end of 1961.

Time deposits have risen faster than demand deposits at District member banks since 1955



Other time deposits, held mostly by corporations and state and local governments, while a small part of total time deposits, have fluctuated much more than savings deposits. This reflects in part the greater sensitivity of these funds to yields obtainable on Treasury bills, commercial paper, bankers' acceptances and similar investments. During 1956-61, for example, the amount of corporate time deposits at large Seventh District banks declined when yields on Treasury bills rose above the rate on time certificates and fell when bill yields dropped below that rate. In the second half of 1960, Treasury bill yields dropped below maximum permissible rates on time certificates of comparable maturity and remained below these rates throughout 1961.

This situation, together with increased commercial bank promotion of negotiable time certificates of deposit figured importantly in a nearly tenfold rise in corporate time deposits, from about 40 million to 400 million dollars, at large banks in Chicago, Detroit, Milwaukee, Indianapolis and Des Moines during 1961. (This increase excludes the issuance and subsequent redemption of a substantial amount of non-interest bearing time certificates to one large corporation.) In contrast, savings deposits rose 14 per cent. As a result, at the end of the year, corporate time deposits comprised about 8 per cent of the total time deposits at these banks compared with less than 1 per cent at the beginning of 1961, while the proportion in savings deposits declined from 86 to 83 per cent.

Since the first of this year, corporate time deposits at large Seventh District banks have continued to rise. They increased 11 per cent in January, 13 per cent in February and 17 per cent in March.

Time deposits and bank growth

From the end of 1955 to the end of 1961, time deposits at member banks in the District rose 48 per cent, from 7.6 billion to 11.2 billion dollars while demand deposits at these banks, exclusive of interbank deposits, increased from 16.4 billion to 17.2 billion dollars, or less than 5 per cent (see chart). The corresponding increases for all member banks in the United States were 70 per cent for time deposits and 12 per cent for demand deposits, exclusive of interbank deposits.

The experience of recent years contrasts sharply with that of the early postwar period when demand deposits grew more rapidly than time deposits. During 1947-51, for example, time deposits accounted for only 24 per cent of the increase in total deposits at Seventh District member banks and 45 per cent during 1952-56. Since 1957, however, time deposits have accounted for nearly 78 per cent of over-all deposit growth. Bank growth in recent years, therefore, has reflected to a considerable extent their ability to attract time deposits. In addition to offering higher interest returns and advertising their services, many banks have vigorously promoted additional types of time accounts.

Most notable has been the increased promotion of time certificates of deposit. The option of negotiability has made this type of time deposit especially attractive to corporations and other large investors seeking high quality short-term investments. This is reflected in developments at large District banks for which information is available weekly. Between the last Wednesday in December 1961 and the last Wednesday in March 1962, savings deposits at these banks grew 5 per cent but other types of time deposits, including time certificates, rose 41 per cent. Also, numerous banks have added "fringe benefits" to savings accounts such as crediting interest monthly, instead of quarterly or semiannually, as well as for the full month on deposits received shortly after the first of the month.

Trade barriers coming down?

Early in March the major trading nations of the West concluded one of the most successful rounds of tariff bargaining since the war. Conducted under the provisions of the General Agreement on Tariffs and Trade (GATT), the talks marked the European Common Market's initial participation in international tariff negotiations.

Prior to the opening of the tariff conference in September 1960, the Common Market nations had offered to reduce by 20 per cent their proposed common external tariff on industrial products provided the other GATT participants would also lower their tariff barriers. United States Government officials applauded the move and offered to negotiate roughly similar cuts in American tariffs. In 1958 Congress had approved a four-year extension of the Trade Agreements Act authorizing the President during that period to reduce United States duties up to 20 per cent of the rates existing on July 1, 1958.

Results encouraging

Major interest has focused on the new trade concessions drawn up between the United States, the European Common Market and Britain—the leading industrial areas of the West. In essence, the three agreed to cut tariffs on many industrial products by as much as a fifth over the next several years. Most of the new concessions, moreover, are expected to be extended to the other GATT nations under the long-standing *most favored nation* principle which assures equal tariff treatment to imports of similar goods from all countries.

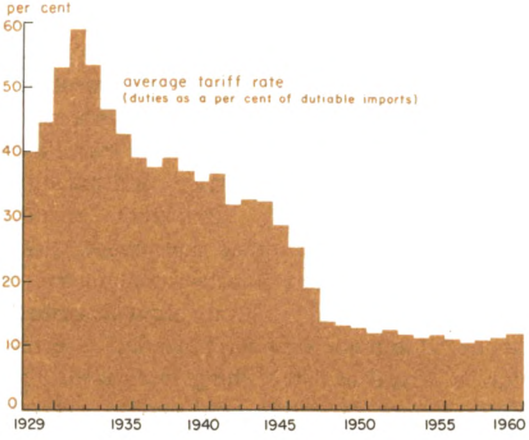
The United States agreed to lower its import duty on automobiles from 8½ to 6½ per cent in two equal steps. The European Common Market will reduce its proposed external automobile tariffs from 29 to 22 per cent, while Britain will lower its import duty on cars from 30 to 22 per cent. Significant rate reductions also were made on electrical machinery and equipment, business machines and office equipment, machine tools, textile machinery and materials handling equipment.

Chemicals were the only major industrial category where bargaining failed to produce any important concessions. Little progress was made in the agricultural sector, but this had been expected mainly because of the difficulties and delays encountered by the Common Market nations in drawing up their common agricultural policy.

In agreements signed thus far, the United States has obtained new concessions on about 1.1 billion dollars of annual exports in exchange for lowering tariffs on about 0.9 billion dollars of imports. Furthermore, the President announced that in order to avert possible collapse of the negotiations, he had agreed to lower American tariffs below the "peril point" recommendations of the United States Tariff Commission on a list of imports totaling roughly 80 million dollars in 1958.[1]

The United States tariff on industrial goods (as measured by the ratio of duties collected to the value of dutiable imports) averaged about 12 per cent in 1960, and the next few years should see a decline to nearly 10 per cent as the cuts resulting from the recent GATT meeting become effective. By comparison, in the Twenties and early Thirties,

The American tariff wall has declined markedly since passage of the Trade Agreements Act in 1934



SOURCE: Department of Commerce.

[1]The "peril point" amendment to the Trade Agreements Act is one of several measures designed to avoid serious injury to domestic industries as a result of trade agreements negotiated with other countries. Other measures include the "escape clause" and national security amendments.

First adopted in 1948 the "peril point" amendment requires the President to submit to the Tariff Commission a list of items on which tariff concessions are being considered. The commission then advises the President as to how far he can go on each item "without causing or threatening serious injury" to the domestic industry. If a concession is granted which goes beyond the "peril point," the action must be explained to Congress.

An "escape clause" was first included in a trade agreement negotiated with Mexico in 1942 and in all agreements thereafter. It permitted the President to modify or withdraw tariff concessions extended to other countries if increased imports threatened "serious injury to domestic industries producing like or directly competitive goods." In 1951 the Trade Agreements Act was amended to make the "escape clause" a permanent part of the program.

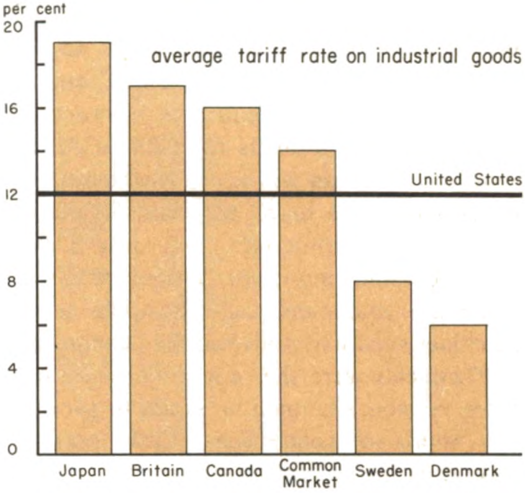
The national security amendments of 1954 and 1955 authorized the President to impose import controls in order to prevent injury to domestic industries deemed essential to national defense.

effective United States tariff rates on many industrial imports ranged from 50-100 per cent and in some instances as high as 400 per cent. These duties, the highest in our history, were prescribed by the Fordney-McCumber and Hawley-Smoot Tariff Acts of 1922 and 1930, respectively.

In 1960, the Common Market tariff on manufactured goods averaged about 14 per cent and the British tariff, about 17 per cent. Their future industrial tariffs, reflecting the recent GATT concessions, will average slightly more than 11 and 13 per cent, respectively.

As a result of this working down of tariffs, large sectors of the economies of all three areas have become more exposed to foreign competition. But there are important exceptions. In the United States, for example, the watch industry and woolen textile manufacturers continue to operate behind tariffs averaging roughly 50 per cent, while sporting goods and many chemicals are protected by tariffs averaging more than 18 per cent. Examples of European tariff protection include the relatively high Common Market and British duties on automobiles—22 per cent—and rates of 15 per cent and more on certain chemicals and pharmaceuticals. In addition, the Common Market nations and Britain employ quotas to restrict imports of manufactured goods to a much greater extent than the United States. These apply mainly to motor vehicles, textiles, aircraft and chemicals.

In 1960 many manufacturing countries had higher tariffs than the United States



SOURCE: Department of Commerce and U. S. Tariff Commission.

Tariffs down to zero?

There is a growing feeling on both sides of the Atlantic that tariffs on industrial products traded in large volume between the major manufacturing countries are obsolete and should be removed entirely. One indication of this is the President's request, embodied in the Trade Expansion bill now undergoing congressional review, for special authority to bargain down to *zero* tariffs on those groups of products for which the United States and the Common Market account for 80 per cent or more of "free" world exports.

In February the Department of Commerce submitted a list of 26 commodity groups that might be included in the final "zero" list. Alphabetically, the list runs from aircraft to tobacco products. Among the more important groups, in terms of estimated 1960 trade, are aircraft, motor vehicles, agricultural machinery, power-generating equipment, metalworking machinery, office equipment, electrical machinery and industrial machinery.

The President's proposal, often described as the "dominant supplier formula," is principally aimed at establishing freer trade for those groups of goods produced by capital intensive industries and for which world demand is expected to continue rising rapidly in the future.

There are, however, other large segments of international trade where little if any progress has been made toward freer trade. In 1960, the total export value of the 26 commodity groups included in the "zero" list amounted to 19.2 billion dollars, or only 17 per cent of the estimated value of total "free" world exports (Soviet bloc excluded).

The list embraces only a small part of the industrial products—textiles, sporting goods, toys and other light manufactures—exported in large volume by the low-wage countries of Asia. And it excludes agricultural foodstuffs and most industrial raw materials such as mineral ores and petroleum. For many low-income countries, one or a few items in these broad product classes represent their most important source of foreign exchange earnings.

Motor vehicles and machinery dominate "zero" list exports in 1960

Commodity group	"Free" world exports from Common Market* and U. S.	Exports to "free" world: U. S.	Exports to "free" world: Common Market*	Exports to "free" world: Common Market* and U. S.
	(per cent)	(million dollars)		
Motor vehicles	91	1,237	2,671	3,908
Industrial machinery	81	1,817	1,966	3,783
Electrical machinery	80	1,066	1,535	2,601
Aircraft	97	1,227	259	1,486
Agricultural machinery	85	520	414	934
Power-generating machinery	82	280	649	929
Office machinery	81	207	211	418
19 other groups	80 or over	2,449	2,690	5,139
Total		8,803	10,395	19,198

* Includes five other possible member countries: Britain, Denmark, Greece, Ireland and Norway.

SOURCE: Department of Commerce.

Key problem areas

Trade restrictions on *agricultural commodities,* which account for about 18 per cent of total "free" world exports, are doubtless the most difficult to reduce or remove. These include quotas, health and purity requirements and effective tariffs averaging as high as 54 per cent in Japan and 42 per cent in Austria.

In every GATT tariff bargaining session since the war the leading industrial nations, including the United States, have insisted upon retaining strict controls on agricultural imports. Each country argues that its agricultural problems are unique and too complicated to permit exposure to the competitive forces of the world market. But to a considerable extent controls are necessary only because domestic agricultural support programs have raised agricultural prices in these countries substantially above world levels.

The United States experience is a case in point. The web of Government controls over agricultural imports has tightened materially since inception of the reciprocal trade agreements program in 1934. This may seem strange since at the outset agricultural interests, especially in the South, were among the most vigorous supporters of the program.

They felt that the rigorous protective tariff acts of 1922 and 1930 had hurt important sectors of American agriculture which depended heavily on export markets, notably cotton, wheat and tobacco.

But as the trade agreements program got under way, the Government's depression-born domestic agricultural support programs began to raise the prices of many farm commodities above world levels. It was recognized that increased imports of agricultural products would tend to reduce the effectiveness of the domestic support programs and increase their cost to the Treasury. To guard against this possibility, Congress in 1935 added Section 22 to the Agricultural Adjustment Act. This authorized the President to restrain by means of additional tariff duties or quotas the import of any agricultural commodity whenever it was determined that such imports tended to interfere with any domestic agricultural program operated by the Department of Agriculture.

Quotas were applied to imports of cotton and wheat in 1940 and 1941, respectively; but then the disruptions of the war obviated the need to take any additional action under this authority for at least another decade, despite the fact that domestic agricultural support prices were raised substantially during the war to encourage increased production and were maintained at relatively high levels in subsequent years.

In the early postwar period large exports of foodstuffs to Europe and the Far East, financed to a large extent by Marshall plan and other foreign aid programs, absorbed most of the increased domestic production at prices generally above the Government support levels. However, with the recovery of European agriculture by the late 1940's, world prices declined and in 1950 American agricultural exports dropped almost 20 per cent from the level of the previous year to 2.9 billion dollars.

This placed the domestic agricultural support program in a difficult position. Domestic prices of some farm commodities now stood substantially above prevailing world market prices and foreign agricultural exporters were beginning to seek markets in this country. In the circumstances it was necessary to impose import controls on a much broader scale. In 1953 quotas were imposed on butter, cheese and other dairy products; flaxseed and linseed oil; peanuts and peanut oil; and in the following year on rye and rye flour and meal.

Meanwhile, the domestic support programs continued to funnel massive stocks of surplus agricultural commodities into the warehouses of the Commodity Credit Corporation. In an

High tariffs still exist on some U. S. imports

Commodity	1960 effective tariff rate* (per cent)
Clocks, watches and parts	51
Finished woolens and worsteds	49
Jewelry	44
Synthetic fabrics and wearing apparel	40
Asbestos	32
Coal-tar products	31
Toys and sporting goods	31
All dutiable imports	12

* Ratio of duties collected to value of dutiable imports.
SOURCE: Department of Commerce.

effort to reduce these surpluses, the Government has adopted a number of "special" export programs—involving barter arrangements, sales for foreign currencies, sales below cost, credits, grants and other arrangements—collectively referred to as the "Food for Peace" program. Although these "special" export devices have provoked complaints on the part of several other leading agricultural exporting nations, they are indicative of the many kinds of special trading arrangements that have grown up, largely as a result of efforts to aid agriculture in various countries.

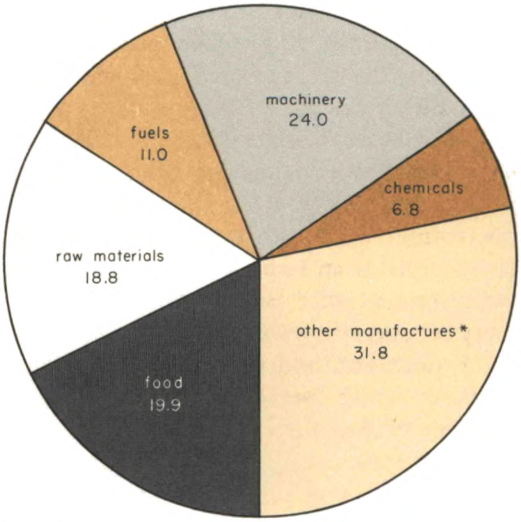
The European Common Market's common agricultural policy, the broad outlines of which were approved last January, represents a continuation of this trend. By far the most important feature of the new policy is an external tariff consisting of a sliding scale of duties that will serve to boost the cost of imported farm commodities to a level equal to the generally higher prices prevailing in the Common Market.

In substance, this is not unlike the authority to adjust tariffs "to equalize differences in the cost of production in the United States and the principal competing foreign countries" contained in the tariff acts of 1922 and 1930. A possible objective, and certainly a probable result of such a tariff policy, would be to make the Common Market largely self-sufficient in many important agricultural products.

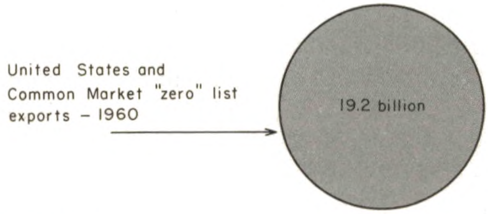
A second problem concerns trade between industrial nations and the *primary producing countries* which export large quantities of industrial raw materials and agricultural foodstuffs. The industrial countries maintain controls over large segments of this trade; in many instances, to shield certain domestic industries from lower-cost foreign competition and, to a lesser extent, to preserve long-standing trade relationships with former colonial possessions.

Exports from "free" world countries—1960

total: 112.3 billion dollars f.o.b.



* includes about 1 billion dollars of unclassified commodities



SOURCE: Department of Commerce and United Nations.

The United States, for example, has long imposed quotas on imports of sugar to encourage domestic production of cane and beet sugar even though tropical producers could supply our requirements at substantially lower cost. Imports of cotton and peanuts also are restricted by quotas to prevent interference with domestic agricultural support programs. Imports of rice and meat, on the other hand, are limited by rigorous health and purity requirements.

In 1958 the President utilized the "escape clause" amendment to the Trade Agreements Act to impose quotas on imports of unmanufactured lead and zinc in order to prevent injury to domestic producers. The quotas limited subsequent lead and zinc imports to 80 per cent of the average annual volume during the five-year period 1953-57.

For many years Britain has granted preferential treatment to imports from the Commonwealth nations in exchange for similar concessions on British exports. Raw cotton, rice and tea from India, Ceylon and Malaya, for example, enter Britain duty free, as do dairy products from New Zealand and Australia. Raw cotton and tea imports from non-Commonwealth members are subject to an effective tariff of 6 per cent; rice, 13 per cent; and dairy products, 10 per cent. France accords similar preferential treatment to raw material and tropical food imports from her former African territories.

Controls such as these, despite their justification on grounds of hardship or long-standing commercial and political associations, are serious obstacles to the attainment of freer international trade. Indeed, the search for a satisfactory alternative to the elaborate system of Commonwealth preferences is proving to be one of the major obstacles to Britain's bid to join the Common Market.

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Under the Trade Expansion bill, the President has requested special authority to reduce or eliminate all restrictions on imports of tropical agricultural products supplied by underdeveloped countries. His action would be conditional on similar steps by the Common Market and would be limited to those commodities not produced "in any significant quantity" in this country. In the circumstances present restrictions on imports of sugar, cotton, rice and certain vegetable oils presumably would be continued, as would the export subsidies which enable United States farmers to compete effectively with tropical producers of these commodities.

A third problem concerns the restrictions of major industrial countries against imports from the *low-cost manufacturing countries* of Asia, notably Japan and Hong Kong. Frequently, such controls are invoked on the grounds that wage rates in these countries are so low as to create "unfair competition." About a dozen European countries and Australia maintain quantitative import restrictions against Japanese goods. In addition, the United States has an informal understanding with Japan under which that country voluntarily limits exports of certain items, including textiles, stainless steel flatware, electrical appliances and canned tuna to the United States.

In recent years, exports of cotton textiles from Asian countries have expanded rapidly. This is an industry in which developing nations appear to have a decided comparative cost advantage over the advanced industrial countries. In fact, the textile industry was one of the mainsprings in the rapid industrialization of Europe and North America more than 150 years ago.

Last July the United States and other major textile importers obtained, within the framework of GATT, a temporary agreement with the leading exporting countries to stabilize cotton textile exports for a period of twelve months, starting October 1, 1961. In the interim a special GATT committee was to develop a long-term plan for "orderly expansion" of international trade in cotton textiles that would assure an increase in export opportunities for underdeveloped countries and at the same time would avoid disruption of markets in importing countries. In February the exporting and importing nations approved a five-year agreement proposed by the committee which will go into effect when the temporary arrangement expires next October.

However, the new pact contains "escape clauses" permitting textile importing countries to invoke embargoes and other restrictions which will be binding even if the exporting nations feel they are unjustified.

If countries like Japan are to remain oriented toward the West, they must find markets for their textiles and other light manufactures in that part of the world in order to pay for imports of food, raw materials and capital equipment vital to their long-range economic development.

Another problem is the continuation of rigid controls on international trade in *energy resources.* In 1959 the President, under the national security amendments to the Trade Agreements Act, imposed quotas on imports of crude oil and petroleum products. These quotas have limited crude oil imports to about 10 per cent of total domestic demand. European countries, on the other hand, have long restricted coal imports from this country to protect their higher-cost producers.

It is possible that the web of controls on energy resources may broaden further, inasmuch as France has strongly insisted that the Common Market maintain tight controls over "noncommunity" fuels. Presumably, this would give France's newly developed Saharan crude oil fields a preferred position in supplying the petroleum requirements of the Common Market.

No easy solution is available for any of the foregoing problems. It is encouraging, however, that the major manufacturing countries are continuing to make headway in their efforts to lower trade restrictions on industrial goods. As the benefits of progress in this area become increasingly evident, what now appears as at best a gloomy prospect in other important sectors could brighten considerably.

Substantial compromises will be required from all countries and adjustments doubtless will have to be made by many firms in many areas if freer international trade is to continue to play an important role in helping men to wring more and "better" products from the resources available to them.