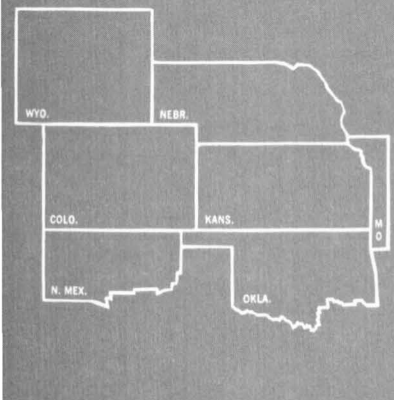
monthly review

DECEMBER 1968



FEDERAL RESERVE BANK OF KANSAS CITY

The Rapid Growth in U. S. Merchandise Imports

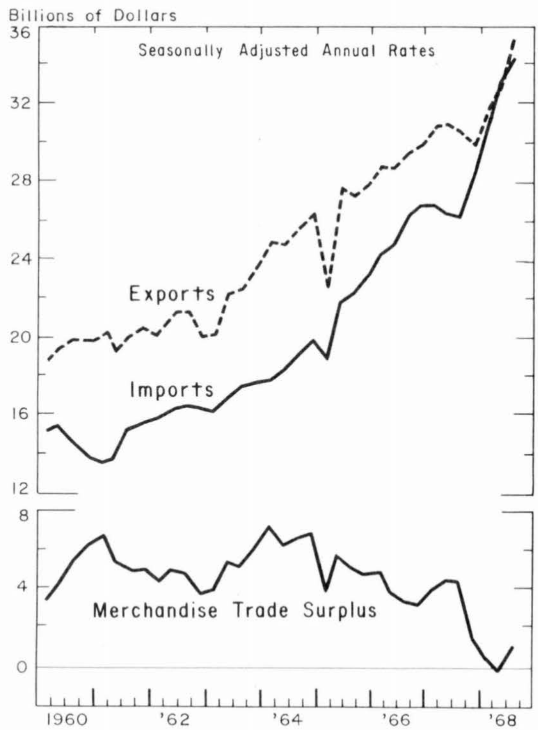
By Thomas E. Davis

AMONG THE many significant changes and developments in international trade and finance during the past few years, one of the most disturbing has been the progressive deterioration in the U. S. merchandise trade surplus. Concern over this deterioration has been prompted by the fact that the U. S. merchandise trade surplus has long been considered a key element of strength in the U. S. balance of international payments. Indeed, the United States has traditionally relied upon a substantial surplus in its merchandise trade account to offset in large part deficits occurring in many of its other international accounts, such as the U. S. private capital and Government accounts. A good example of this reliance occurred in the early 1960's when the merchandise trade surplus increased gradually due to an expansion in U. S. exports and only a moderate rise in U. S. imports (Chart 1). As a consequence, the United States was able to make some progress during this period in reducing its large balance of payments deficit, even though there was a sizable rise in U. S. net capital outflows.

Since 1964, however, when the U. S. trade surplus reached \$6.6 billion—the highest level recorded since 1947—the U. S. position on merchandise trade account has deteriorated very rapidly. In 1965, the U. S. trade surplus dropped nearly \$2 billion, and in the next two years it fell again by close to \$1 billion. Moreover, in the first three quarters of 1968 the trade surplus declined sharply to an annual rate of less than one half billion dollars. As a result of this progressive deterioration in the U. S. trade surplus, official efforts to eliminate the deficit in the U. S. balance of payments have been seriously hampered. Although significant progress has been made in curtailing the net outflow of U. S. capital since the mid-

Chart 1

U. S. MERCHANDISE IMPORTS, EXPORTS, AND TRADE SURPLUS, 1960-68



SOURCE: U. S. Department of Commerce.

Table 1

U. S. GROSS NATIONAL PRODUCT, MERCHANDISE EXPORTS, AND IMPORTS, 1960-68

	Gross National Product		Exports*		Imports*		
Year	Billions of Current Dollars	Per Cent Change Over Previous Year	Billions of Current Dollars	Per Cent Change Over Previous Year	Billions of Current Dollars	Per Cent Change Over Previous Year	Imports as Per Cent of GNP
1960	503.7	4.1	19.487	19.6	14.744	—3.7	2.9
1961	520.1	3.3	19.944	2.3	14.522	—1.5	2.8
1962	560.3	7.7	20.606	3.3	16.219	11.7	2.9
1963	590.5	5.4	22.071	7.1	17.014	4.9	2.9
1964	632.4	7.1	25.297	14.6	18.648	9.6	3.0
Average Annual Per Cent Change 1960-64		5.5		9.4		4.2	2.9
1965	684.9	8.3	26.244	3.7	21.516	15.4	3.1
1966	747.6	9.2	29.176	11.2	25.541	18.7	3.4
1967	789.7	5.6	30.468	4.4	26.991	5.7	3.4
1968†	851.6	8.8	33.428	9.1	33.019	24.9	3.9
Average Annual Per Cent Change 1965-68		8.0		7.1		16.2	3.5

*U. S. balance of payments basis.
†Seasonally adjusted annual rates through the first three quarters of 1968. Since fourth quarter data for 1968 were not available, the per cent changes for 1968 were computed relative to the first three quarters of 1967 on an annual basis.
SOURCE: U. S. Department of Commerce.

1960's—on both private and Government accounts—through various restraint programs, the shrinkage in the U. S. trade surplus has offset much of this progress. Thus, most observers today point to the deterioration in the U. S. trade surplus as one of the principal factors accounting for the persistent deficit in the U. S. balance of payments since 1964.

The dominant factor underlying the shrinkage in the U. S. trade position since 1964 has clearly been the rapid growth in U. S. merchandise imports. Starting from a level of \$18.6 billion in 1964, U. S. imports have jumped sharply to an annual rate of \$33.0 billion during the first three quarters of 1968 (Table 1). Thus, within the last 3¾ years, U. S. imports have increased \$14.4 billion, or by 77 per cent over the 1964 level. U. S. merchandise exports, on the other hand, advanced only \$8.1 billion over this same period to an annual rate of \$33.4 billion. In comparison, the gain in U. S. exports represented an increase of only 32 per cent relative to 1964.

In view of the important role that the rapid growth of imports has played in the deterioration of the U. S. trade position—and the serious implications this growth has had on the overall U. S. balance of payments position—this article examines the growth and the commodity composition of U. S. imports since 1964 and comments on some of the factors associated with this growth.

THE GROWTH IN U. S. MERCHANDISE IMPORTS SINCE 1964

In the early 1960's—during the 1960-64 period—total U. S. merchandise imports grew at an average annual rate of 4.2 per cent (Table 1). This relatively moderate rate of growth in imports generally reflected the state of the business activity in the United States. Over this period, the U. S. economy was expanding at a stable and noninflationary rate and was marked by the availability of a certain margin of unutilized productive resources and capacity. Against this background, there was no particular pressure for the United States to increase significantly its purchases of goods from abroad.

In 1965, however, the expansion in the U. S. economy suddenly became excessive and prices began to rise sharply. The two factors primarily responsible for the acceleration in total spending and prices were a rapid buildup in defense expenditures connected with the Vietnam war and a marked increase in business fixed investment spending. In response to this inflationary burst, as well as the simultaneous rapid absorption of unutilized productive resources, the U. S. demand for imported goods increased appreciably. In 1965, total U. S. merchandise imports jumped $2.9 billion, or 15 per cent over the previous year—their highest growth rate in over six years.

The upward trend in imports that began in 1965 accelerated throughout the first three quarters of 1966. Propelling the upward movement in imports was the continued pressure of excess demand in the United States which emanated mainly from increased domestic outlays for defense and for business investment. In the latter part of the year, however, the expansion in U. S. business activity moderated somewhat in response to official policies of monetary and fiscal restraint. In turn, the growth in imports from the third to the fourth quarter was reduced to an annual rate of 7 per cent. However, for 1966 as a whole, U. S. imports were up nearly 19 per cent over 1965, the largest year-to-year percentage gain in imports recorded since the exceptional rise stimulated by the Korean war in 1950-51.

In 1967, the growth rate in U. S. imports was slowed substantially by the sluggish pace of business activity in the United States. During most of that year, industrial production in the United States leveled off, consumer spending and business investment rose only moderately, and business inventory accumulation was cut quite sharply. In response to this easing of excessive domestic demand and the subsiding of upward pressures on domestic prices, U. S. purchases of goods from abroad rose only slightly in the first quarter of 1967, and then declined marginally in the second and third quarters. In the fourth quarter, however, as U. S. business activity and inventory accumulation again began to expand, U. S. imports increased sharply. Contributing to the fourth quarter increase were sizable imports of copper due to the prolonged strike in the U. S. copper industry, as well as stepped up purchases of iron and steel products from abroad in anticipation of a possible strike in the U. S. steel industry. Despite the large rise in the final quarter, U. S. imports for the year were up only about 6 per cent over 1966.

During the first three quarters of 1968, U. S. merchandise imports advanced substantially, increasing sharply in the first quarter and then growing at a less vigorous pace in the second and third quarters. As a result, imports over the first nine months of the year were up to a seasonally adjusted annual rate of $33 billion, or 22 per cent above the 1967 total. Stimulating this year's surge in imports was the renewed expansion in domestic business activity, a marked increase in consumer expenditures, and a resurgence in the upward movement of domestic prices. Also contributing to the rise in imports early in the year was the continuation of strike-related purchases of copper, and iron and steel mill products from abroad. However, since the settlement of labor disputes in the U. S. copper and steel industries, purchases of metals from abroad have slowed somewhat, accounting for much of the less vigorous pace in total imports during the two most recent quarters.

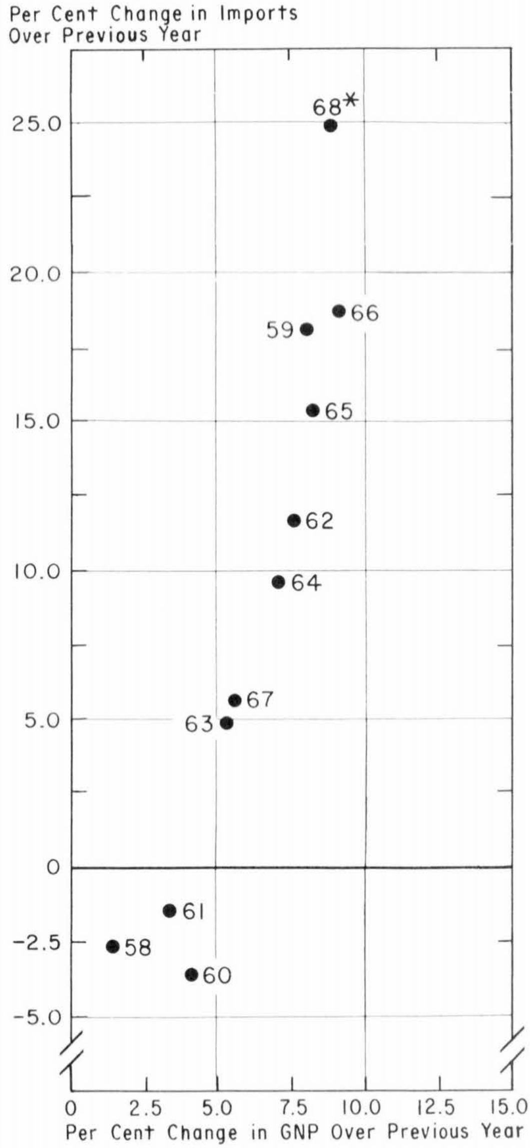
As a consequence of the sharp rise in imports over the first three quarters of 1968 and the gains posted over the previous three years, total U. S. imports during the 3¾ years since 1964 have grown at an average annual rate of 16 per cent. This average growth rate, it should be emphasized, constitutes not only an extremely rapid rate of growth but also one that is close to four times that (4.2 per cent) recorded for the 1960-64 period. A further indication of the exceptional rise in imports in recent years compared to the early 1960's is seen in the relatively large increase in the ratio of imports to gross national product (GNP). This ratio rose from an average of 2.9 per cent during the 1960-64 period to 3.9 per cent in the first three quarters of 1968, an all-time high for the postwar period.

The major factors accounting for the rapid growth in U. S. imports since 1964 are generally considered to be (1) the vigorous pace of economic expansion in the United States over this period, (2) the concomitant emergence of inflationary price pressures in this country and (3) the occurrence of certain extraordinary or special factors that affected U. S. imports. One of these special factors, of course, was the strike-related step-up in imports of metals that occurred in late 1967 and early 1968, and to a lesser extent in 1965. A more pervasive special factor, though, has been the import stimulating effect of the U. S.-Canadian automotive agreement in 1965. As a result of the duty-free provisions of this agreement, imports of autos and parts from Canada have jumped from a low of $70 million in 1964 to an annual rate of $2.3 billion in the first nine months of 1968. Omitting this substantial gain in imports of Canadian automotive goods, U. S. imports of all other goods still have posted a spectacular rate of increase, rising at a 13 per cent average annual rate in the 3¾ years since 1964.

The extent to which the import rise in recent years has been influenced by the rapid ex-

Chart 2

U. S. MERCHANDISE IMPORTS IN RELATION TO U. S. GROSS NATIONAL PRODUCT, 1958-68



*Seasonally adjusted annual rates through the first three quarters of the year. Also see footnote, Table 1.

SOURCE: U. S. Department of Commerce.

Table 2
WHOLESALE PRICE INDEX FOR MANUFACTURED GOODS IN SELECTED COUNTRIES, 1960-68
(1958 = 100)

	United States	United Kingdom	Japan	Germany	Italy	France	Canada	Belgium	Netherlands	Switzerland
1960	100	102	102	100	98	107	101 (96)	101	99	99
1961	100	104	103	102 (107)	98	110	102 (92)	101	98 (103)	99
1962	100	107	102	103 (108)	101	113	105 (91)	101	99 (104)	102
1963	100	108	103	103 (108)	106	117	107 (93)	103	101 (106)	107
1964	100	112	104	105 (110)	110	119	108 (93)	109	107 (112)	108
Average Annual Per Cent Change										
1960-64	0	2.3	.6	1.2 (2.2)	2.6	2.5	1.4 (—1.6)	1.8	1.2 (2.1)	2.0
1965	102	117	104	107 (112)	112	120	110 (95)	110	111 (117)	109
1966	105	120	107	109 (114)	113	123	114 (99)	112	116 (122)	111
1967	106	122 (118)	109	108 (113)	113	122	116 (100)	111	116 (122)	111
1968 (1st half)	108	126 (107)	110	103 (108)	114	123	117 (101)	110	116 (122)	111
Average Annual Per Cent Change										
1965-68	2.0	3.0 (—1.0)	1.4	—.5 (—.4)	.9	.8	2.0 (2.1)	.2	2.1 (2.2)	.7

NOTE: Data in parentheses reflect adjustments made for currency revaluations.
SOURCE: International Monetary Fund, **International Financial Statistics.** The series have been taken from several issues and converted to 1958 = 100.

pansion of economic activity in the United States can be seen in Chart 2. This chart shows the relationship of annual percentage changes in U. S. gross national product and U. S. merchandise imports over the past 10 years, measured in current prices. Whenever GNP has increased at about 5 per cent, imports have risen at approximately the same rate; below this rate imports have risen relatively less; and—most importantly—whenever GNP has increased above the 5 per cent rate, imports have risen at a relatively faster pace. In 1963 and 1967, for example, when the rate of increase in GNP ranged near 5 per cent, imports registered advances between 5 and 6 per cent. However, in 1965, 1966, and 1968, as GNP advanced at about 8 to 9 per cent, imports rose between 15 and 25 per cent. In short, changes in U. S. imports not only have proven to be very sensitive to changes in GNP but they have been particularly sensitive on the upward side whenever GNP has advanced substantially.

An indication that the import rise in recent years also may have been due partly to price inflation in the United States can be seen in Table 2. This table shows developments in the wholesale price index for manufactured goods in the United States and nine other selected countries over the period 1960-68.[1] As seen in this table, the U. S. price performance during the early 1960's—a period when U. S. imports rose only moderately—was on the average considerably better than every other country listed except Canada, after taking account of changes in foreign exchange rates.

[1]Although a case might be made for using another type of price index for international comparison, the wholesale price index of manufactured goods was used on the basis that manufactured goods, i. e., semimanufactures, finished manufactures, and manufactured foodstuffs, have constituted about 75 per cent of total U. S. imports in recent years.

Indeed, the United States achieved a perfect record in terms of stability in its wholesale price index over this period. Since 1964, however, the United States has experienced a rise in its wholesale price index which—at an average annual rate—has been in excess of that posted by all other countries in this group except Canada and the Netherlands, again taking account of changes in exchange rates. Thus, to the extent that changes in wholesale prices of manufactured goods provide a relevant comparison for international trade purposes, it would appear that the inflationary conditions in the United States since 1964 have been instrumental in lessening the competitiveness of goods produced in the U. S. vis-a-vis goods produced and imported from abroad.

THE COMMODITY COMPOSITION OF U. S. MERCHANDISE IMPORTS SINCE 1964

The rapid growth of U. S. imports since 1964 has occurred throughout a broad range of commodity classifications. Of the five major commodity groupings tabulated on an end-use basis, the largest absolute gain has been registered by imports of industrial supplies—a category that constitutes nearly one half of total U. S. imports—followed in turn by imports of automobiles, consumer goods, capital equipment, and food. In terms of overall percentage gains since 1964, imports of automobiles and capital equipment have posted the largest advances, followed by imports of consumer goods, industrial supplies, and food, in that order, as shown in Table 3.

Industrial Supplies

U. S. merchandise imports of industrial supplies and materials rose from \$9.5 billion in 1964 to an annual rate of \$14.1 billion in the first three quarters of 1968, a gain of 48 per cent. Purchases of these imports advanced strongly in 1965 and most of 1966 in response to a sharp expansion in U. S. industrial production, but declined slightly in 1967 as a consequence of a cyclical downturn in U. S. industrial activity and inventory investment. During the first nine months of 1968, imports of industrial supplies rebounded vigorously as a result of large strike-related imports of metals and a resumption in the upward trend in U. S. industrial production. Over the past 3¾-year period as a whole, imports of industrial supplies have advanced at an average rate of 11 per cent a year, more than twice that recorded during the previous four-year period.

Nearly two fifths of the 48 per cent expansion in industrial supply imports has been in purchases of copper, and iron and steel mill products. The value of copper imports has risen \$.5 billion since 1964 due partly to higher prices in 1966, but most importantly, due to the nine-month strike in the U. S. copper industry that began in mid-1967. Iron and steel imports have increased \$1.3 billion since 1964—to an annual rate of \$2.1 billion in the first three quarters of 1968—largely as a result of hedge buying in anticipation of strikes in the U. S. steel industry in both 1965 and 1968. The rapid gain in steel imports since 1964 has brought the average rate of growth in these imports up to 30 per cent a year, up from 15 per cent in the 1961-64 period. Reflecting this rise in steel imports, purchases of steel from abroad now account for nearly 14 per cent of apparent U. S. steel consumption, compared to only 7 per cent in the early 1960's.

Imports of industrial supplies for the production of nondurable goods also have increased substantially in recent years. Showing particularly strong advances have been imports of industrial chemicals, and fertilizers and other farm materials. Textile imports for the production of nondurable goods—being somewhat depressed by the general downturn in the domestic textile market in 1967—have grown at a more moderate pace since 1964. Other

Table 3
U. S. MERCHANDISE IMPORTS BY SELECTED END-USE CATEGORIES

	1964	1968*	Per Cent Change 1964-68	Average Annual Per Cent Change 1961-64†	Average Annual Per Cent Change 1965-68‡
	(In millions)				
Industrial supplies and materials	$ 9,498	$14,096	48.4	5.1	11.2
Fuels and lubricants	2,015	2,477	22.9	6.3	5.5
Paper and paper base stocks	1,227	1,401	14.2	2.9	3.6
Materials for nondurable goods production	2,084	2,791	33.9	4.9	8.1
Textiles, yarns, and fabrics	1,009	1,208	19.7	4.9	5.6
Tobacco	142	153	7.7	6.4	2.4
Industrial chemicals	234	500	113.7	8.2	21.5
Fertilizers, seed, and other farm materials	159	223	40.3	2.9	8.8
Materials for durable goods production	3,469	6,413	84.9	5.1	18.3
Iron and steel	825	2,117	156.6	14.6	30.1
Iron ore, scrap, and ferro-alloys	602	677	12.5	4.5	4.3
Nonferrous ores, metal, and scrap	1,236	2,347	89.9	6.0	19.3
Copper	345	817	136.8	2.2	30.2
Aluminum	343	596	73.8	17.8	16.3
Nickel	181	273	50.8	13.1	12.7
Capital goods other than automotive	1,039	2,777	167.3	16.9	28.8
Machinery	1,020	2,604	155.3	17.7	26.8
Electrical machinery other than consumer type	203	675	232.5	13.5	36.9
Metalworking machine tools	53	240	352.8	9.9	50.3
Other industrial machinery and components	191	512	168.1	14.9	26.9
Farm tractors and machinery	191	355	85.9	22.0	16.3
Business machines and computers	84	217	158.3	11.0	27.5
Civilian aircraft and all aircraft parts	20	173	765.0	56.2	128.0
Automotive vehicles and parts	767	3,926	411.9	10.0	55.9
From Canada	67	2,305	3,340.3	81.7	167.4
Passenger cars	19	1,177	6,094.7	450.0	217.1
Trucks and special vehicles	8	368	4,500.0	100.0	217.2
Automotive parts and engines	40	760	1,800.0	57.9	129.6
From other countries	700	1,621	131.6	7.8	28.2
Passenger cars	574	1,405	144.8	6.5	30.6
Trucks and special vehicles	16	32	100.0	−6.2	23.6
Automotive parts and engines	111	184	65.8	24.0	16.3
Consumer goods: nonfood and nonautomotive	2,694	5,168	91.8	9.4	18.8
Apparel	506	883	74.5	10.5	15.3
Leather footwear, gloves, and luggage	134	349	153.7	8.2	28.8
Rubber footwear and other rubber goods	74	156	110.8	−4.4	22.1
Household appliances, radios, TV's, etc.	290	756	160.7	19.5	30.4
Bicycles, motorcycles, and boats	121	225	86.0	18.9	17.6
Photographic and optical goods	91	165	81.3	4.3	18.0
Toys and sporting goods	141	287	103.5	15.4	21.1
Diamonds and other gem stones	303	527	73.9	12.1	15.9
Foods, feeds, and beverages	3,915	5,235	33.7	4.5	8.4
Coffee	1,197	1,176	−1.8	5.2	.2
Sugar	458	639	39.5	−1.1	8.7
Meat products and poultry	424	760	79.2	8.7	17.2
Fish and shellfish	425	611	43.8	9.1	10.4
Fruits, nuts, and preparations	309	461	49.2	8.2	11.8
Whiskey and other alcoholic beverages	387	608	57.1	9.2	16.3

NOTE: Data shown do not necessarily add to totals.

*Annual rates based on first three quarters of 1968.

†Average annual per cent change was computed for the 1961-64 period because of the nonavailability of 1959 data to compute the per cent change for 1960.

‡Averages include the per cent change for 1968 computed relative to the first three quarters of 1967 on an annual basis.

SOURCE: U. S. Department of Commerce.

types of industrial supplies, such as fuels and lubricants, and paper and paper base stocks, have increased at a slower rate than the industrial supply category as a whole.

Capital Goods

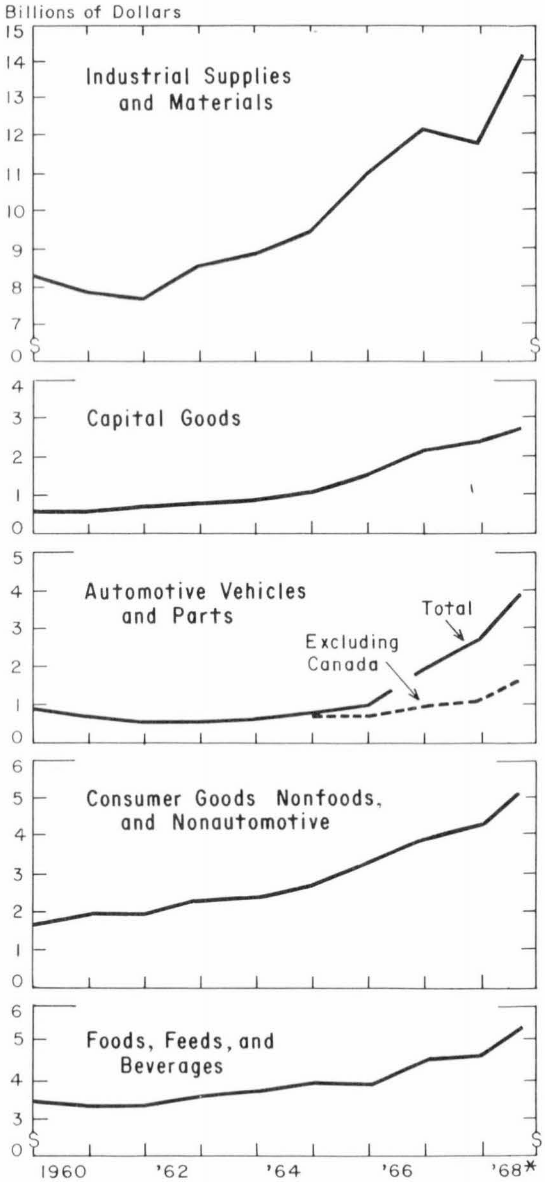
Imports of capital equipment increased to an annual rate of $2.8 billion during the first nine months of 1968, a gain of $1.7 billion since 1964. This gain amounted to a spectacular 167 per cent increase over the 1964 level. A large portion of this rise occurred in 1965 and 1966 when the rapid expansion in the U. S. economy pressed heavily on domestic manufacturing capacities and created large order backlogs and extended delivery periods for capital goods. In turn, the U. S. demand for capital goods spread increasingly to foreign suppliers. Since 1966, the easing of pressures on domestic manufacturing capacity has served to moderate the growth in these imports. Nevertheless, arrivals of capital equipment from abroad now account for as much as 4.6 per cent of domestic expenditures on producers' durable equipment, up from 2.6 per cent in 1964 and 2.0 per cent in 1960.

Particularly expansive components within capital goods imports in recent years have been electrical machinery, metalworking machine tools, and other industrial machinery. Purchases of these types of machinery have constituted almost $1 billion of the total $1.7 billion gain posted for imports of capital goods since 1964. Also registering large gains in the capital goods category have been imports of business machines—mostly of the conventional type—and imports of agricultural machinery. Purchases of civilian aircraft and parts have fluctuated erratically from year to year, but are up substantially from their 1964 level.

Automotive Vehicles and Parts

Total U. S. imports of automotive vehicles and parts amounted to $3.9 billion at an annual rate during the first three quarters of 1968,

Chart 3
MAJOR END-USE CATEGORIES OF U. S. MERCHANDISE IMPORTS
1960-68



*First three quarters shown at annual rate.
SOURCE: U. S. Department of Commerce.

a jump of \$3.2 billion since 1964. Nearly three fourths of this gain, or \$2.3 billion, represented purchases of vehicles and parts from Canada. As mentioned earlier, these imports from Canada have grown at a spectacular pace since 1964—by 167 per cent on an average annual basis—mainly because of the U. S.- Canadian automotive agreement of 1965. (Under this agreement, there also has been a large but not quite offsetting expansion in U. S. automotive exports to Canada.) Purchases of non-Canadian vehicles and parts have risen at a slower but still substantial pace since the end of 1964, reaching an annual rate of \$1.6 billion during the first nine months of 1968. The extent of the rapid rise in imported vehicles from countries other than Canada is underscored by the fact that "foreign" cars now account for 9.9 per cent of total new car registrations in the United States, compared with only 6.0 per cent in 1964.

Consumer Goods

Purchases of foreign consumer goods (excluding food and automotive goods) reached an annual rate of \$5.2 billion in the first three quarters of 1968, up \$2.5 billion, or 92 per cent, over their 1964 level. Imports of these goods rose markedly in 1965 and 1966, and again in late 1967 and during 1968, in response to the strong surge in domestic personal consumption expenditures in both of these periods. For the 3¾ years since 1964, consumer goods imports have risen at an average rate of 19 per cent a year, up significantly from the average rate of 9 per cent registered during the previous four-year period.

The rise in imported consumer goods has occurred throughout a wide variety of nondurable and durable goods. Within the nondurable category, purchases of apparel and footwear—both leather and rubber—have posted strong advances. Imports of durable consumer goods, such as diamonds, toys and sporting goods, and photographic and optical goods, also have increased rapidly. Arrivals of household appliances, radios, and TV's have grown at an exceptionally rapid pace since 1964, continuing the rapid expansion in these imports that began in the early 1960's.

Foods, Feeds, and Beverages

Imports of food and related items have risen only moderately since 1964, increasing \$1.3 billion to an annual rate of \$5.2 billion during the first three quarters of 1968. Purchases of meat products and poultry—stimulated by high prices of similar U. S. products—paced the moderate expansion in food imports, followed by imports of whiskey and other alcoholic beverages, and imports of fish and shellfish. Sugar imports, which are controlled largely by U. S. quotas, advanced at a 9 per cent average annual rate since the end of 1964, while coffee imports experienced a slight absolute decline. Total U. S. imports of foods, feeds, and beverages increased at an average rate of only 8.4 per cent a year over the past 3¾ years, the lowest growth rate of any major category.

CONCLUSION

The U. S. surplus on merchandise trade, long considered a traditional source of strength in this country's balance of payments, has progressively deteriorated since 1964, mainly because of a massive increase in U. S. merchandise imports. Some portion of this increase can be attributed to special factors, but most of the increase has been due to excessive demand conditions in the U. S. economy combined with inflationary domestic price pressures. As a result, there has been a marked acceleration in the rate of growth in practically every major commodity classification of U. S. imports since 1964.

If the needed restoration in the U. S. merchandise trade surplus is to be achieved, it is vitally necessary to reduce the rapid growth rate in U. S. merchandise imports that has occurred in recent years. Toward that end, the successful implementation of economic policies designed to slow the inflation of prices and costs in this country clearly would be helpful. However, in view of the magnitude of the deterioration in our trade surplus and the likely inroads foreign goods have made in U. S. markets in the past 3¾ years, it seems unrealistic to assume that just a temporary cessation of price pressures in the United States would be sufficient. Only if the United States pursues policies designed to achieve relative stability in prices and a stable rate of economic growth over the long run is it likely that any significant progress will be made toward the desired improvement in our international trade position.

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