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INTERNATIONAL ECONOMIC COMPARISONS

Summary of U.S. Economic Conditions

The U.S. economy continues its moderate expansion driven by a rise in consumer confidence and spending, and prospects of stronger export demand. The U.S. Department of Commerce reported that a 5.8-percent surge in consumer spending in the third quarter of 1989 compensated for a drop in exports and manufactures output, causing the GNP to grow by 2.5 percent at an annual rate. The rate of increase in the GNP price index, a broader indicator of inflation than the Consumer Price Index, dropped sharply in the third quarter, to 2.9 percent from 5.0 percent in the second quarter.

In October 1989, industrial output fell due to a decline in sales of domestic cars, a labor strike in the aircraft industry, and production disruptions due to the California earthquake. This also caused a softening in manufacturing employment. Nevertheless, the unemployment rate on a total labor force basis (including military) remained virtually unchanged from the month before at 5.2 percent.

Although exports declined overall in the third quarter, prospects for growth in exports appears good. A survey by the National Association of Purchasing Management (NAPM) shows that new orders for exports started to rebound in September after four months of decline. In addition, the monthly U.S. merchandise trade deficit declined by 21.4 percent to its lowest level in 5 years, from $10.1 billion in August to $7.9 billion in September. The improvement in the September trade deficit was largely due to higher U.S. exports.

Economic Growth

The annualized rate of real economic growth in the United States during both the second and third quarters of 1989 was 2.5 percent. The annualized rate of real economic growth during the second quarter of 1989 was -1.0 percent in the United Kingdom, 0.6 percent in Canada, 2.0 percent in West Germany, 3.2 percent in France, and -3.1 percent in Japan. The latest available data indicate that the annualized rate of real growth for the first quarter of 1989 was 3.0 percent in Italy.

Industrial Production

U.S. industrial production fell 0.7 percent in October 1989 after remaining flat in September, but it was 1.4 percent higher than it was in October 1988. The October decline in industrial output was attributed to a labor strike in the aircraft and parts industry and to production disruptions in computers and related parts resulting from California earthquake.

Capacity utilization in manufacturing, mining, and utilities stood at 82.8 percent in October 1989, down from 83.6 percent in September due to the fall in aircraft production and other manufacturing disruptions mentioned above. The operating rate for aerospace and miscellaneous transportation equipment dropped from 86.6 percent in September to a low of 77.9 percent in October.

Other major industrial countries reported the following annual growth rates of industrial production: during the year ending September 1989, Japan reported an increase of 3.8 percent, and West Germany reported an increase of 3.3 percent; during the year ending August 1989, France reported an increase of 4.8 percent, the United Kingdom reported an increase of 0.9 percent, Canada reported a decrease of 0.4 percent and Italy reported an increase of 2.1 percent.

Prices

The seasonally adjusted U.S. Consumer Price Index rose by 0.5 percent from September to October 1989, and increased by 4.5 percent during the year ending October 1989.

During the 1-year period ending October 1989, consumer prices increased 3.3 percent in West Germany, and 6.6 percent in Italy. During the year ending September 1989, consumer prices increased 7.6 percent in the United Kingdom, 3.4 percent in France, 5.2 percent in Canada and 2.6 percent in Japan.

Employment

The seasonally adjusted rate of unemployment in the United States (on a total labor force basis, including military personnel) remained unchanged at 5.2 percent in October from September 1989. The Government of West Germany reported a 7.8 percent unemployment rate in October 1989. For September, Italy reported 16.6 percent unemployment; Canada, 7.3 percent; the United Kingdom, 6.0 percent; France, 9.5 percent; and Japan, 2.2 percent. For foreign unemployment rates adjusted to U.S. statistical concepts, see the tables at the end of this issue.

Forecasts

Table 1 shows macroeconomic projections for the U.S. economy for October 1989 to December 1990, by four major forecasters, and the simple average of these forecasts. Forecasts of all

Table 1
Projected quarterly percentage changes of selected U.S. economic indicators, 1989-90

Quarter	Data Resources Inc.	Merrill Lynch Economics Inc.	Wharton F.A. Inc.	UCLA Business Forecasting Project	Mean of 4 indicators and forecasts
GNP:[1]					
1989:					
September—October	3.8	4.6	6.8	6.9	5.5
1990:					
January-March	5.5	5.8	6.8	4.5	5.6
April-June	5.7	6.9	6.4	6.6	6.4
July-September	5.5	6.7	6.8	7.3	6.6
October-December	6.0	7.5	6.8	7.2	6.9
GNP:[2]					
1989:					
October-December	0.8	1.4	1.7	1.8	1.4
1990:					
January-March	1.4	1.4	1.6	-0.8	0.9
April-June	1.6	2.4	1.7	2.1	1.9
July-September	1.7	2.6	2.9	3.5	2.7
October-December	2.4	2.4	2.7	3.3	2.7
GNP deflator index:					
1989:					
October-December	3.0	3.2	5.0	5.0	4.0
1990:					
January-March	4.1	4.4	5.0	5.3	4.7
April-June	4.1	4.4	4.5	4.4	4.3
July-September	3.8	4.0	3.8	3.7	3.8
October-December	3.6	5.0	4.0	3.8	4.1
Unemployment, average rate:					
1989:					
October-December	5.4	5.4	5.3	5.3	5.3
1990:					
January-March	5.4	5.5	5.5	5.6	5.5
April-June	5.5	5.6	5.6	5.8	5.6
July-September	5.5	5.5	5.6	5.8	5.6
October-December	5.6	5.5	5.5	5.7	5.6

[1] Current dollars.
[2] Constant (1982) dollars.

Note.—Percentage changes in the forecast represent compounded annual rates of change from the preceding period. Quarterly data are seasonally adjusted.

Source: Compiled from data received by telephone from the Conference Board, *Statistical Bulletin*. Used with permission.

the economic indicators, except unemployment, are presented as percentage changes over the preceding quarter, on an annualized basis. The forecasts of the unemployment rate are averages for the quarter. All the forecasts, except UCLA's, project a rise in the nominal growth of GNP throughout the period. The average of the forecasts predicts a slight increase in the unemployment rate in 1990. The causes of the predicted economic growth are (1) a projected rebound in export growth due to the higher growth rates in Western Europe and the opening of the EC market to U.S. exports, and (2) a boost in U.S. domestic investment due to the decline in U.S. interest rates. Inflation (measured by the GNP deflator index) is expected to rise in the first quarter of 1990, and then to moderate during the remainder of the year.

National Savings

A recent study by the Organization for Economic Cooperation and Development (OECD) found that net national savings rates have trended downward in most OECD countries over the 1971–87 period. (The net national savings rate is the sum of government, household, and business savings, net depreciation, as a percent of Net National Product (NNP).) Table 2 shows the average net national savings of the G–7 countries as a percent of Net National Product for three periods spanning 1960–87. The OECD study indicated that a drop in government savings (or increasing fiscal deficits) was the largest component of the decline in national savings in these countries. In contrast, total private savings (households plus businesses) have been more stable. Household savings are affected by the level of corporate savings, the rate of inflation, and the rise in household net wealth. The OECD study found that in the 1970s, households saved more to make up for the erosion in the real value of their financial assets due to high rates of inflation. In the 1980s, households saved less because of a decline in inflation rates, and a sharp rise in household net wealth due to a rise in real estate and equity prices. The OECD also found that the expansion in public pensions in recent years, and the liberalization of financial markets

Table 2
Average net national saving rates as a percent of Net National Product, 1960-70, 1971-80, and 1981-87

Country	*1960-70*	*1971-80*	*1981-87*
United States	10.6	8.9	3.9
Japan	25.6	24.6	20.2
West Germany	19.9	14.3	10.7
France[1]	26.3	25.4	19.6
United Kingdom	11.2	8.2	6.2
Italy	15.0	12.1	7.5
Canada	11.3	13.3	9.4

[1] Gross savings rate.

Source: OECD Working Paper No. 67, Saving Trends & Behavior in OECD countries.

(which made borrowing much easier) have reduced household savings. Net national savings in the G-7 countries averaged around 17.1 percent of Net National Product in the 1960s and only 11.1 percent in the 1980s. During the 1981-87 period, the United States had the lowest average savings rate of the G-7 countries (3.9 percent), while Japan had the highest (20.2 percent).

U.S. Direct Foreign Investment Position

Table 3 shows cumulative U.S. direct investment abroad and foreign direct investment in the United States by area and country from 1986 to 1988. At the end of 1986, the cumulative value of U.S. direct investment abroad amounted to $39.4 billion more than total foreign direct investment in the United States. However, between 1986 and 1988, the cumulative value of foreign direct investment in the United States increased by 49.2 percent compared with an increase of only 25.8 percent in U.S. direct investment abroad. As a result, by the end of 1988, U.S. direct investment abroad was slightly lower (by 0.6 percent) than foreign direct investment in the United States.

U.S. direct investment abroad between 1986 and 1988 was heaviest in the European Community (EC), where it grew by 28.3 percent. In 1988, U.S. direct investment in the EC was concentrated in the following sectors: petroleum (12.4 percent); chemicals and allied products (11.4 percent); machinery except electrical (12.5 percent); transportation equipment (5.9 percent); other manufacturing (11.8 percent); finance (except banking), insurance, real estate (17.1 percent); wholesale (10.1 percent); and banking (4.6 percent). Developing countries as a whole ranked second in terms of U.S. direct investment, followed by Canada. Total U.S. direct investment in developing countries grew by 24.1 percent from 1986 to 1988. In 1988 it was concentrated in manufacturing (32.5 percent); petroleum (20.8 percent); finance (except banking), insurance, and real estate (22.6 percent); wholesale trade (7.8 percent); and banking (8.8 percent). Latin America accounted for 64.1 percent of total U.S. direct investment in developing countries in 1988. U.S. direct investment in Canada grew during 1986-88 by 21.0 percent and in 1988 was concentrated in manufactures (45.9 percent); petroleum (19.1 percent); finance (except banking), insurance, real estate (16.9 percent); wholesale trade (6.2 percent); and other (8.4 percent).

Total foreign direct investment in the United States increased dramatically (by 49.2 percent) from 1986 to 1988 due to pronounced increases from the EC(12) (52.0 percent) and Japan (99.0 percent). Japanese investment in the United States has grown faster in percentage terms than that of the EC. But in absolute terms investment from the EC, and in particular from the United Kingdom (U.K.), significantly outpaced that of Japan during the period. The Netherlands ranked second to the U.K. in 1986-87, but fell to third, behind Japan, in 1988. Canada's direct investment in the United States grew by 35.0 percent over the period.

Table 4 shows the percentage distribution by major sectors of foreign direct investment of the U.K., the Netherlands, Canada, Japan, and OPEC in the United States through the end of 1988. Investments of the U.K., the Netherlands, and Canada in the United States were widely distributed among industries, but Japan's direct investment tended to be concentrated in wholesale trade (34.5 percent), banking (7.3 percent), real estate (18.8 percent) and other manufacturing (11.1 percent). As of the end of 1988, OPEC direct investment was mainly in these same industries.

Balance-of-payments flows accruing from U.S. direct investment abroad (income, royalties, license fees, and charges for other services), grew from $47.0 billion in 1986 to $59.4 billion in 1988. Part of the increase was due to the dollar depreciation that started in 1985. Profits earned abroad in appreciating foreign currencies bought more dollars than before. Income and royalties on foreign direct investment in the United States increased from $4.7 billion in 1986 to $17.0 billion in 1988. Several factors account for the large difference between U.S. income earned on foreign investment abroad and income generated by foreign investment in the United States, including currency fluctuations, the generally higher yields earned on U.S. investments abroad because of the higher risk associated with these investments,

and the payment by foreigners of "goodwill" when acquiring U.S. companies, a practice uncommon when purchasing foreign assets. Also, the relative levels of U.S. direct investment abroad and of foreign direct investment in the United States are somewhat misleading in terms of expected investment income because the asset values that comprise these figures were calculated at different times using different methods.

Table 3
U.S. direct investment abroad and foreign direct investment in the United States, by areas and countries, 1986-88

(In billions of dollars)

Area or country	U.S. direct investment abroad			Foreign direct investment in the United States		
	1986	1987	1988	1986	1987	1988
Total	259.8	308.0	326.9	220.4	271.8	328.8
Canada	50.6	58.4	61.2	20.3	24.0	27.4
EC (12), total	98.6	120.1	126.5	127.2	165.4	193.3
United Kingdom	35.4	42.0	48.0	55.9	79.7	101.9
Netherlands	11.6	14.4	15.4	40.7	49.1	49.0
West Germany	20.9	24.8	21.7	17.2	20.3	23.8
France	8.9	11.8	12.5	7.7	10.1	11.4
Other EC	21.4	27.1	29.0	5.3	6.2	7.2
Other Europe	23.7	26.2	25.7	17.3	20.6	22.5
Sweden	0.9	1.1	1.1	4.0	4.9	5.3
Switzerland	16.4	19.5	18.7	12.1	14.7	15.9
Other Europe	6.4	5.6	5.9	1.3	1.5	2.0
Japan	11.3	14.7	16.9	26.8	35.1	53.3
Australia, New Zealand and South Africa	11.2	13.4	15.1	5.6	6.5	5.6
Latin America & other Western Hemisphere	34.8	44.9	49.3	16.8	12.7	17.0
Middle East	4.6	4.6	4.1	4.9	5.0	5.8
Other Africa, Asia & Pacific	16.6	21.2	23.5	1.8	2.3	3.2
International[1]	4.6	4.6	4.6	[2]	[2]	[2]
Addendum- OPEC	10.9	10.1	10.1	4.8	4.9	6.2

[1] Represents investment not within legal boundaries like international shipping and international drilling.

[2] Not available.

Source: U.S. Department of Commerce, Survey of Current Business, August 1989.

Table 4:
Share by sector of foreign direct investment, from selected countries, in the United States, 1988

Industry	United Kingdom	Netherlands	Canada	Japan	OPEC
	Percent of total				
Petroleum and mining	19.0	[2]	9.2	[2]	12.0
Food and kindred products	5.1	11.9	1.9	[1]	[2]
Chemicals and allied products	10.3	10.1	2.3	2.1	[1]
Primary and fabricated metals	1.7	1.9	12.5	4.3	[2]
Machinery	5.3	4.0	8.6	4.8	[1]
Other manufacturing	14.0	7.0	9.0	11.1	[1]
Wholesale	9.9	6.7	9.3	34.5	[2]
Retail trade	8.4	3.8	3.5	[3]	[3]
Banking	3.6	5.6	5.3	7.3	5.8
Finance except banking	[3]	6.5	2.2	5.4	[3]
Insurance	6.7	9.6	10.9	[2]	[3]
Real estate	5.2	6.8	15.2	18.8	14.1
Other industries	10.0	[2]	10.0	10.0	[2]

[1] Less than $500,000.

[2] Suppressed to avoid disclosure of data of individual companies.

[3] Less than one percent.

Note: Percentages might not add to 100 because of rounding and missing data.

Source: U.S. Department of Commerce, Survey of Current Business, vol. 69, August 1989.

U.S. TRADE DEVELOPMENTS

The seasonally adjusted U.S. merchandise trade deficit declined by 21.8 percent in September 1989, from $10.1 billion in August to $7.9 billion. The September deficit was 15.1 percent lower than the $9.3 billion average monthly deficit registered during the previous 12-month period, and 14.1 percent lower than the $9.2 billion deficit registered in September 1988.

U.S. exports increased 1.9 percent in September, to $31.1 billion from $30.6 billion in August. Imports declined by 3.9 percent, to $39.1 billion in September from $40.7 billion in August.

Export gains in September were concentrated in airplanes, up 72.8 percent for the month and 23.6 percent on a year-to-date basis. Other sectors experiencing monthly gains included automatic data processing equipment and office machinery (up 8.5 percent), vehicle parts (up 12.5 percent), new passenger cars (up 25.0 percent), telecommunications equipment (up 12.8 percent), trucks (up 32.8 percent), and specialized industrial machinery (up 3.7 percent).

Import decreases were concentrated in clothing and footwear (down 16.9 percent), specialized industrial machinery (down 16.4 percent), electrical machinery (down 6.0 percent), general industrial machinery (down 13.1 percent), metal working machinery (down 27.9 percent), airplane parts (down 27.7 percent), and iron and steel mill products (down 7.4 percent).

Meanwhile, the U.S. agricultural trade surplus increased in September to $1.4 billion from $911 million in August. In addition, the U.S. oil import bill declined from $4.4 billion in August to $4.0 billion in September due to the decline in the volume of imports.

The United States experienced improvements from August to September in its merchandise trade deficits with almost every country except Japan. The deficit with Canada declined (from $1.2 billion to $666 million), and also with the newly industrialized countries (from $2.7 billion to $2.3 billion). The deficit with the EC of $773 million turned into a surplus of $1.25 billion, and the deficit with all of Western Europe of $717 million turned into a surplus of $1.2 billion. The deficit with OPEC declined from $1.9 billion to $1.5 billion. In contrast the deficit with Japan increased from $4.0 billion to $4.1 billion and with China from $580 million to $727 million.

U.S.-Japan Structural Impediments Initiative Talks Stall

The United States and Japan concluded the second round of the Structural Impediments Initiative (SII) talks, held on November 6 and 7 in Washington D.C., without reaching a consensus on the nature of the structural features of each country's economy that contribute to the $50 billion bilateral trade imbalance. During the first round of SII consultations that took place on September 4 and 5 in Tokyo, U.S. negotiators identified six characteristics of Japan's economy that they considered institutional barriers to its markets. Japanese negotiators in turn raised seven aspects of the U.S. economy for discussion. (See *IER*, November 1989). During the most recent round of talks, U.S. negotiators added restrictions to direct foreign investment in Japan to its list of issues to discuss. The United States pointed out that the ratio of inward to outward direct foreign investment in the United States is 85 percent compared to only 11 percent in Japan.

At the first SII talks, the United States and Japan agreed to jointly conduct a survey of prices in their markets. The survey was a major topic of discussion at the second round of talks. U.S. negotiators argued that the results of the price survey, which was conducted by Japan's Ministry of International Trade and Industry (MITI) in conjunction with the U.S. Department of Commerce, demonstrated that the Japanese market is not freely accessible. The survey revealed that of the 122 products studied, 84 were priced higher in Japan than in the United States. In addition, of the products priced higher in Japan, 40 were priced 50-percent higher than in the United States. Products in this group include sparkplugs, bed linens, golf clubs, and wine. Only four items—ketchup, perfume, china, and household batteries—were priced 50-percent higher in the United States than in Japan.

The U.S. side held a press conference at the end of the latest round of talks. According to J. Michael Farren, Commerce Undersecretary for International Trade, although the Japanese negotiators acknowledged the price differentials found in the survey, they demonstrated a general reluctance to draw broad conclusions on overall price levels in each country based on the survey sample. Instead, the Japanese argued on an item-by-item basis that the price differentials resulted from unique circumstances. S. Linn Williams, Deputy U.S. Trade Representative, was optimistic that the results of the price survey would lead to movement on four of the issues raised by the United States. He also suggested that the formation of a committee by Japan's ruling Liberal Democratic Party (LDP) to study the SII issues will facilitate the SII process.

Charles Dallara, Assistant Secretary of Treasury for International Affairs, expressed disappointment that the two sides did not make

progress toward reaching a common understanding. According to Dallara, although the United States gained an appreciation of current Japanese practices, there was very little flexibility in the Japanese Government positions. He went on to note that although the United States recognizes that the SII issues are complex and will take time to address, the Japanese need to develop precise plans for structural adjustments so that it is clear that progress is being made.

Richard McCormack, Under Secretary of State for Economic and Business Affairs, characterized the first two rounds of talks as a "discovery phase." McCormack said the U.S. team hopes that at the third round of talks, to be held in mid-January in Tokyo, the two countries can reach agreement on the structrual impediments in their domestic economies. After the Japanese elections in late January or early February, the U.S. team expects the negotiations to proceed at a brisk pace. The fourth round of talks are anticipated to take place in March and a midterm assessment is due in April.

While the second round of SII consultations was taking place at the U.S. State Department, the Senate Finance Committee's International Trade Subcommittee held hearings to solicit public views on the SII talks. Subcommittee Chairman Max Baucus (D-MT) and Senator John Rockefeller (D-WV) expressed skepticism about the prospects for SII producing real results. Earlier, Senator Baucus had warned he would introduce legislation that would mandate a Super 301 case against Japan based on the SII issues if the talks do not make substantial progress by next spring. The subcommittee heard testimony from trade groups, business representatives, and scholars.

Korea Relinquishes Its Right to Use GATT Balance-of-Payments Exemption

Since acceding to the GATT in 1967, Korea has restricted imports to protect its balance-of-payments position. This is permitted, in certain circumstances, under GATT Article XVIII(b). GATT allows developing countries with massive debt or unstable currencies to restrict imports until their economies reach a competitive level. Such measures are reviewed annually by the GATT Balance of Payments (BOP) Committee. Following a review by the BOP Committee in early October, reportedly, the prevailing view of its members was that Korea could no longer justify invoking preferential BOP treatment because of its consistent rapid economic growth. According to International Monetary Fund figures, Korea's current account surplus should reach $6 billion this year, compared with a $11.5 billion surplus in 1988 and a $7.7 billion surplus in 1987. Some members of the Committee called for Korea's graduation from the exemption and suggested that a schedule be established for phasing out the restrictive measures. Korea has maintained restrictions on a wide variety of agricultural products, such as beef and shellfish, ostensibly for balance-of-payments reasons. (On November 7, Korea finally agreed to phase out its beef import quotas and will no longer block adoption of a GATT panel report ruling that its restrictions on beef imports from Australia, New Zealand, and the United States are contrary to GATT rules and should be eliminated. For additional information, see *IER*, June 1989.)

At the October 27 BOP Committee meeting, Korea agreed to renounce its right to impose restrictions on imports for BOP reasons. After a week of negotiations with the Committee, Korea agreed to a three-stage timetable that allows it to phase out its import restrictions over 7 and one-half years. In the first stage, beginning in January 1990, restrictions will be removed on 190 items; the next two stages will cover an additional 270 products. The process is scheduled to be completed by July 1, 1997. Korea can unilaterally reimpose the import restrictions if its balance-of-payments position worsens.

News accounts of an October 31 speech given before the American Stock Exchange by United States Trade Representative Carla Hills, reported that Ambassador Hills praised Korea's actions and called for other developing countries, particularly those with "outward-looking policies aimed at capturing additional market share through export," to follow Korea's lead.

U.S. Investigation of Brazil's Reserved Computer Market Ends

On October 6, the Office of the United States Trade Representative (USTR) announced that it would close its investigation of Brazil's import restraints on small computers and software, and of Brazilian violations of patent rights in this product area. In making its decision, the USTR determined that Brazil had made sufficient progress in opening its market to U.S. computer products. On September 13, Brazil agreed to allow payments for imported computer operating programs to be made at flexible exchange rates. (Disagreement over the correct level for exchange rates had caused delays in payments to U.S. vendors.) Earlier, Brazil had agreed to provide copyright protection for software. Also, Brazil has expressed a willingness to open part of its informatics market to foreign investment.

In Brazil, small computers and software are part of a broad category called "informatics." Informatics includes all telecommunications and data-processing equipment with a digital component, as well as related services. Brazil's efforts to establish a domestic computer industry under a protectionist umbrella are now more than a decade old. More recently, the controversial Informatics law, which formalized preexisting protective regulations, became effective in 1984 and is due to expire in 1992.

Brazil's computer and software market grew into what is probably the largest of the Third World as a result of the heavy protection it has enjoyed. Computers have been one of the few Brazilian growth industries in a decade marked by serious economic problems. However, much of the equipment produced behind Brazil's protective walls is now considered expensive and dated.

Heated disputes between the U.S. and Brazilian Governments have centered on the reserved character of Brazil's small computer market, restrictions on foreign investment in the industry, and the Brazil's lack of protection for computer software. Brazil's "Law of Similars," which prohibits imports of products similar to those already made in Brazil, has proven to be the major problem in the informatics conflict because of the arbitrary, protectionist interpretation of "similarity" by Brazilian authorities.

The informatics trade dispute between the United States and Brazil first reached critical proportions in September 1985. At that time, the United States instituted an investigation under section 301 of the Trade Act of 1984. The conflict came to a head in November 1987, when U.S. authorities targeted 45 Brazilian export products for possible 100-percent duty increases in retaliation for Brazil's denial of Microsoft Corporation's right to sell its software to Brazilian users. In response, many U.S. buyers postponed or suspended their orders of Brazilian products until details of the proposed U.S. retaliation were made clear. The situation cast a long shadow on U.S.-Brazilian relations in trade areas unrelated to computers, such as footwear and civilian aircraft.

In an effort to avert U.S. retaliation and the potentially serious effects on its exports, in December 1987, Brazil enacted a new copyright protection law. The new legislation was meant to strengthen Brazil's protection of intellectual property and was expected to diminish the arbitrary application of the "Law of Similars" in the software area. Nonetheless, access to the Brazilian computer and software market remained limited (*IER*, March 1988.)

Although U.S. authorities did not remove the threat of trade sanctions, the sanctions announced in November 1987 were never imposed. Negotiations continued, leading eventually to the recent closing of the 4-year-old section 301 investigation. This event is being hailed by the Bush administration as an important step toward improving trade relations with Brazil. At the same time, the American Electronic Association has emphasized that close monitoring of developments in Brazil is still necessary to ensure that the country lives up to its commitments, and the Software Publishers Association claims that software piracy continues to plague foreign sellers in Brazil.

With the October 6 announcment that the investigation was closed, the United States and Brazil agreed that they would consult at least four times a year on computers and related issues. during bilateral talks on a wide range of trade issues held later in October, the United States raised problems that had not been resolved prior to the closing of the section 301 case. These included difficulties encountered by U.S. companies in Brazil when trying to register operating systems (specifically AT&T's UNIX system) for sale. Under Brazil's Informatics law, a program must be registered with the Special Informatics Secretariat (SEI) before it can be sold in Brazil to ensure that there is no functionally equivalent local product under the "Law of Similars."

United States Presents Agriculture Proposal in Uruguay Talks

On October 25, the United States offered its recommendation for farm reform in the Uruguay Round Negotiating Group on Agriculture. The proposal incorporated a call for the gradual phaseout of export subsidies and certain internal support programs with a tariffication plan presented earlier by the United States (*IER*, September 1989). Secretary of Agriculture Clayton Yeutter asserted that the plan "is designed to level the playing field for farmers, so they [can] compete fairly against one another instead of against governmental treasuries, in order to feed this growing population with a rational set of international trade rules."

The new U.S. proposal covers four major areas of agricultural trade: market access, export-based subsidies, internal support, and sanitary and phytosanitary standards. Point one, which addresses the issue of market access, proposes liberalization of agricultural markets through the conversion of nontariff barriers, such as quotas, to tariffs. Quota levels would gradually be increased, as an interim mechanism, prior to their conversion to tariffs. The tariffs would then be eliminated through negotiations. "Snapback" language is included in the proposal to allow reimposition of barriers for temporary protection from unfairly traded imports. (This concept is similar to the "escape clause" contained in section 201 of the 1974 Trade Act).

The second component of the U.S. proposal is a 5-year phaseout of export subsidies. Secretary Yeutter has cited data that revealed that agricultural supports in developed countries alone amounted to $165 billion annually, $130 billion which was borne by taxpayers. In addition, he stated that a "correction" on the use of farm supports could conceivably augment farmers' overall income by as much as $20 billion.

The U.S. plan also calls for subjecting government policies (such as municipal transportation subsidies, tax incentives, or price support programs) that create surpluses, deny access to in-

coming products, or distort trade to a "traffic light" classification system. Under this approach, Uruguay Round negotiators would identify those internal supports that are trade distorting and then categorize them as "red-light," "yellow-light," or "green-light" measures. Policies designated as "red-light" would have to be phased out in 10 years. Those labeled "yellow-light" would be subject to monitoring by an appropriate international body with the authority to take disciplinary action. Supports classified as "green-light" would be those permissible under GATT.

Finally, in an effort to make it more difficult for trade barriers to be erected under the guise of consumer health and safety, the U.S. proposal calls for the harmonization of sanitary and phytosanitary regulations among GATT members. The United States suggested that the Codex Alimentarius Commission, the health and safety regulating arm of the United Nations World Health Organization, would be an appropriate body to provide the scientific evidence to be used by dispute panels.

After the U.S. proposal was presented in October, Secretary Yeutter characterized it as "more comprehensive, specific, and cohesive" than the earlier U.S. plan. In reference to the proposal, United States Trade Representative (USTR) Carla Hills emphasized that the U.S. goal in agriculture is to reform the sector "so that farmers can grow *what* they want *when* they want, and earn a decent income without government interference."

However, international response to the proposal has been mixed. Not surprisingly, opposition was voiced by the European Community (EC), which completely rejected the proposal on the grounds that it contradicted an agreement reached at the Uruguay Round midterm review in April. During the midterm review, the United States endorsed the total elimination of trade-distorting farm supports over time. The EC, however, preferred a gradual reduction—not elimination—of certain supports. In a compromise, the parties agreed to work toward "substantial progressive reductions" in agricultural supports. Since the current U.S. proposal would require the EC to totally dismantle its Common Agricultural Policy (CAP), the EC considers the proposal a breach of the mid-term compromise. The EC CAP has been an issue of contention with the United States since its inception in the early 1960's.

In Brussels, EC Commissioner for Agriculture Ray MacSharry expressed his "deep disappointment" with the U.S. paper. In Geneva, EC Delegate Rolf Mueller claimed that "the United States risks stopping the clock in the agriculture negotiations." Mueller was not optimistic about the future of the negotiations since he sees the U.S. proposal as a "retrograde step." However, the EC has not presented its own proposal for agriculrural reform.

Although Japan welcomed the American paper as going further than the positions taken in the April midterm review, it labeled the recommendation impractical and drastic. Japan opposes the part of the U.S. plan that would eliminate subsidies and has vowed to maintain heavy government supports for its rice producers. Since rice is the food staple of Japan, government officials use national security grounds to justify the subsidies that have enabled it to maintain self-sufficiency in rice production. Japan's Minister of Agriculture, Forestry, and Fisheries declared that "Japan will maintain its current stand" of protecting the staple food.

Support for the plan came from most of the members of the Cairns Group, a coalition of 14 agricultural exporting nations. New Zealand hailed the U.S. plan as a "major breakthrough," while Brazil noted that the proposal "puts agriculture back on the right track in the GATT." Australian Trade Minister Michael Duffy claimed that it would be difficult for other countries to reject the plan if they were truly committed to cutting subsidies and other trade distorting practices in agriculture. Duffy labeled the plan "radical," in that it is very detailed and addresses short-term measures, not just long-term goals. However, Canada expressed reservations about the abolition of article XI(2)(c), which covers production controls, that would be required under the U.S. plan. Canada uses the article in its supply management and quota schemes for agricultural products.

Joint Ventures Accelerate in the U.S.S.R.

Western interest in doing business with local partners in the Soviet Union increased sharply during 1989. According to Soviet sources, foreign firms concluded 749 new joint ventures (JVs) in the U.S.S.R. during January–September 1989, compared with only 23 during the full year of 1987 and 168 during the full year of 1988. Of the total 940 JVs in existence on October 1, 1989, Soviet firms concluded 748 such agreements with Western firms, 60 with firms from the developing countries, and 105 with those from the nonmarket economy countries (NMEs). (The remaining 27 JVs are comprised of various combinations of firms from the 3 categories.) With 97 JVs, U.S. firms ranked third after West German (153) and Finnish firms (110). Among the developing countries, India led with 15 JVs, and among the NMEs Bulgaria topped the list with 28 JVs, followed by Poland (26) and Hungary (22). The distribution of JVs by major categories of activity was as follows: computer hardware and software production 13.0 percent; construction, 6.4 percent; production of consumer goods and domestic trade 6.2 percent each; transportation and tourism 5.6 percent; and chemical industry and forestry products combined 5.0 percent. If JVs expand during the clos-

ing quarter of 1989 at a rate approaching that of the first three quarters of 1989, their number will surely exceed 1,000 by yearend.

As of October 1, 1989, one in three of the registered JVs was operational. U.S. partners in JVs that became operational during 1989 include the following companies: Combustion Engineering, Inc. (provides instruments for the petrochemical industry); Honeywell, Inc. (provides instruments for fertilizer production); Foster Wheeler Corp. (provides equipment for construction, oil production); Polaroid Corp. (assists in the assembly of cameras); Management Partnership International, Inc. (assists in the assembly of personal computers, software development, and marketing), Dresser Industries, Inc., (provides engineering services and products for the chemical industry), and Tambrands, Inc., (assists in the production of feminine hygiene products). The largest U.S.-Soviet JV, which is not yet operational, involves Occidental Petroleum Corp. with a capital commitment of $200 million.

The main factors behind the heightened interest in JV agreements this year are the liberal January 1989 JV law (see *IER* February 1989, pp. 4–5) and a much greater flexibility in both negotiating and operating JVs on the Soviet side than previuosly assumed by Western companies. For example, after Western businessmen complained to the authorities, restrictions introduced during the spring of 1989 on using JV ruble profits to purchase products for exports were eased. Western businessmen are also satisfied with the growing possibilities for managerial influence in the jointly operated companies.

"Using joint ventures to bring Western capital and management methods into the Soviet Union is one of the top priorities of the country's leadership," explains Mr. Jeffrey Burt, attorney at the Washington-based law firm Arnold and Porter. "The presence of these firms in the Soviet Union serves as a catalyst in the reform process, because contact with Western firms helps in achieving independence and efficiency." More than 1 year ago, a consulting subsidiary of Arnold and Porter and a Soviet consulting firm established a joint venture in Moscow to provide professional assistance, including legal services, to Western firms wanting to do business in the U.S.S.R.

Nevertheless, the business environment in the Soviet Union is far from what most Western firms would consider ideal. The lack of market prices hampers rational decision making, and supply shortages and inadequacies of infrastructure (problems with transportation, communications, storage, etc.) increase unit costs, limiting chances for profitable exports. In addition, the inconvertibility of the ruble makes profit repatriation slow. Although senior Soviet officials promise gradual improvement in the country's financial situation, they do not expect the ruble to become fully convertible before the year 2000.

But the Soviets have their concerns too. They consider the $1.49 billion hard currency capital brought into the country in connection with JV operations too small and badly distributed. At the end of the third quarter of 1989, capital committed by Western firms amounted to $1.44 billion and that by developing countries to $52.8 million. Of the total 940 JVs, 546 (or 58.1 percent) had capitalization of less than one million rubles ($628,000 at current exchange rates) and the capitalization of only 72 (or 7.7 percent) of the JVs exceeded 10 million rubles ($6.28 million). Most of the investment by Western partners is in the service sector rather than in manufacturing; the Soviets would like to have it the other way around. The territorial distribution of JVs is uneven, with a concentration in the Russian Socialist Federated Soviet Republic. There are 706 JVs in the Russian republic—478 of these in Moscow alone. With 92 JVs the Baltic states cannot complain, but the areas most in need of Western capital—including the Soviet Far East—remain largely ignored by investors.

Last but not least, Soviet policymakers are concerned that demands by Western partners to allow them to repatriate their profits in hard currency will force the Soviet Union to increase its primary product exports, deepening the country's "colonial" pattern of trade. Minerals, fuels, and crude materials averaged 74.8 percent of Soviet exports to the West during 1987 and 1988. In trade of machinery and transportation equipment with the West, Soviet imports averaged 9.2 times higher than Soviet exports during the same period. Economists generally regard as harmful the excessive reliance on exports of raw materials as a growth stimulus. Efforts to boost output becomes increasingly slow and expensive over time. Primary product prices fluctuate more than manufactured goods prices and tend to decline relative to them over the long haul, worsening the terms of trade for countries excessively reliant on primary-product exports.

Hungary Meets Requirements for "Permanent" Most-Favored-Nation Status

In 1978, Hungary became the second nonmarket economy (NME) country (following Romania in 1975) to be granted most-favored-nation (MFN) tariff status under the waiver provision of section 402 of the Trade Act of 1974. Section 402 states that MFN status may not be extended to an NME country that engages in emigration-restricting practices (the Jackson-Vanik amendment). It includes, however, a procedure that gives the President the authority to waive the freedom-of-emigration requirement. The waiver is subject to annual renewal. Both the general waiver authority of the President and any waivers in effect automatically expire on July 3 of each year unless extended by a Presidential determination not less than 30 days before that

date. This year, as in all previous years since 1978, the MFN tariff status of Hungary was continued under the renewal of its waiver. The waiver remained in effect until late October when, after passing a new emigration law, Hungary became the first NME country to receive "permanent" nonwaiver MFN status.

For several years, business groups had contended that the annual renewal requirement was detrimental in carrying out commercial transactions. They cited Hungary in particular as a candidate for an extension of the renewal period, inasmuch as its emigration practices (unlike those of Romania) were in general continuing to improve. It was not until this year, however, following a series of economic and political reforms in Hungary, that sufficient support could be found in the Congress for the passage of legislation to provide such an extension. On March 23, a bill was introduced in the House (H.R. 1594) that would suspend the application of the emigration provisions of the Trade Act of 1974 to Hungary for a period of 5 years. To ensure its passage, the bill was amended to reduce the duration of the extended MFN treatment for Hungary from 5 to 3 years, and the measure was passed by the House as amended. This legislation, which would extend the suspension until July 3, 1992, when Hungary would again be subject to the waiver procedure, was received in the Senate on September 12.

Meanwhile, Hungary proposed new legislation to meet the freedom-of-emigration requirement of section 402. Following a review of this legislation by U.S. officials, President Bush informed the Hungarian Government—during a speech he made in Budapest on July 12—that if the proposed law were passed by its Parliament, he would inform the U.S. Congress that Hungary was in full compliance with the Jackson-Vanik amendment. This law was passed on September 26 and will go into effect on January 1, 1990.

Having promised to act once the law had been passed, President Bush reported to the Congress on October 26 that Hungary was no longer in violation of the freedom-of-emigration requirement. This determination released Hungary from the waiver procedure and gave it nonwaiver status. The nonwaiver procedure of section 402 requires, however, that the President report semiannually to the Congress that Hungary's emigration policies and practices have remained in full compliance with the act. In this sense, but in this sense only, an NME country is never completely free of the restrictions of the Jackson-Vanik amendment. Since Poland's MFN status was restored in 1960, prior to the passage of the Trade Act of 1974, it is the only NME country that has the so-called unconditional MFN tariff status that applies to non-NME countries.

STATISTICAL TABLES

Industrial production, by selected countries and by specified periods, January 1986-September 1989

(Percentage change from previous period, seasonally adjusted at annual rate)

Country	1986	1987	1988	1989 I	II	III	Apr.	May	June	July	Aug.	Sept.
United States	1.1	3.8	5.7	2.2	3.2	1.3	8.0	-0.8	2.6	0	3.4	-.8
Canada	.8	2.7	4.2	4.1	1.2	([1])	-0.9	0	0.9	-1.8	-.9	([1])
Japan	-.3	3.4	9.4	13.2	0	.7	-37.4	6.3	27.1	-26.7	40.6	-20.5
West Germany	2.2	.2	3.1	9.8	2.6	([1])	22.8	-22.9	42.8	-6.2	-18.7	([1])
United Kingdom	2.3	3.4	3.8	-2.0	-4.4	([1])	0	-14.4	3.4	19.3	19.0	([1])
France	.9	2.2	4.3	5.0	7.4	([1])	53.5	-19.1	11.3	23.4	0	([1])
Italy	3.8	2.6	5.9	-3.9	.2	([1])	4.2	-8.0	21.7	3.1	40.9	([1])

[1] Not available.

Source: *Economic and Energy Indicators*, U.S.Central Intelligence Agency, November 3, 1989.

Consumer prices, by selected countries and by specified periods, January 1986-September 1989

(Percentage change from previous period, seasonally adjusted at annual rate)

Country	1986	1987	1988	1989 I	II	III	May	June	July	Aug.	Sept.
United States	1.9	3.7	4.1	5.4	6.4	2.4	7.0	2.0	2.9	0	1.9
Canada	4.2	4.4	4.0	5.2	6.3	5.4	9.7	8.0	4.2	3.1	5.1
Japan	.6	.1	.7	-2.2	9.8	.9	7.2	-1.1	-2.3	-1.1	13.5
West Germany	-.2	.3	1.2	4.8	3.5	1.8	2.7	1.3	1.1	1.2	4.7
United Kingdom	3.4	4.1	4.9	7.5	8.6	6.3	9.2	7.5	6.6	2.9	7.5
France	2.5	3.3	2.7	3.7	3.9	2.8	4.7	1.8	3.0	2.3	3.7
Italy	6.1	4.6	5.0	7.2	7.7	5.5	6.4	6.6	5.7	3.8	4.5

Source: *Economic and Energy Indicators*, U.S.Central Intelligence Agency, November 3, 1989.

Unemployment rates,[1] by selected countries and by specified periods, January 1986-October 1989

(In percent)

Country	1986	1987	1988	1989 I	II	III	July	Aug.	Sept.	Oct.
United States	7.0	6.2	5.5	5.1	5.2	5.2	5.2	5.1	5.2	5.2
Canada	9.6	8.9	7.8	7.5	7.6	7.3	7.4	7.3	7.3	([2])
Japan	2.8	2.9	2.5	2.4	2.3	([2])	2.2	2.3	([2])	([2])
West Germany	7.0	6.9	7.1	5.8	5.7	5.6	5.6	5.6	5.6	([2])
United Kingdom	11.2	10.3	8.3	7.0	6.5	6.2	6.3	6.2	6.0	([2])
France	10.6	10.8	10.5	9.9	9.9	9.9	10.0	9.9	9.9	([2])
Italy	7.5	7.9	7.9	7.6	7.8	([2])	([2])	([2])	([2])	([2])

[1] Seasonally adjusted; rates of foreign countries adjusted to be comparable with U.S.rate.
[2] Not available.

Note.—Italian unemployment surveys are conducted only once a quarter, in the first month of the quarter.

Source: Statistics provided by Bureau of Labor Statistics, U.S.Department of Labor, November 1989.

Money-market interest rates,[1] by selected countries and by specified periods, January 1986-October 1989

(Percentage, annual rates)

Country	1986	1987	1988	1989 I	II	III	Apr.	May	June	July	Aug.	Sept.	Oct.
United States	6.5	6.8	8.0	9.7	9.7	8.8	9.9	9.6	9.2	8.9	8.8	8.9	8.6
Canada	9.2	8.4	9.6	11.7	12.3	([2])	12.4	12.3	12.3	12.2	12.3	([2])	([2])
Japan	5.0	3.9	4.4	4.9	5.1	([2])	4.2	4.3	4.5	5.2	5.3	([2])	([2])
West Germany	4.6	4.0	4.3	6.2	6.8	7.1	6.3	7.3	6.9	7.0	7.0	7.3	([2])
United Kingdom	10.9	9.6	8.9	13.0	13.5	13.9	13.1	13.1	14.2	13.9	13.8	14.0	([2])
France	7.7	8.1	7.9	9.0	8.8	9.1	8.5	8.9	8.8	9.1	9.0	9.2	([2])
Italy	12.6	11.2	11.0	12.4	12.5	12.9	12.5	12.5	12.7	12.9	12.7	12.9	([2])

[1] 90-day certificate of deposit.

[2] Not available.

Note.—The figure for a quarter is the average rate for the last week of the quarter.

Source: *Federal Reserve Statistical Release* November 13, 1989, *Economic and Energy Indicators*, Central Intelligence Agency, November 3, 1989.

Effective exchange rates of the U.S.dollar, unadjusted and adjusted for inflation differential, by specified periods, January 1986-October 1989

(Percentage change from previous period)

Item	1986	1987	1988	1989 I	II	III	May	June	July	Aug.	Sept.	Oct.
Unadjusted:												
Index[1]	106.0	94.1	88.0	88.7	92.4	92.7	92.6	94.7	92.0	92.5	93.8	91.8
Percentage change	-16.5	-11.2	-6.5	1.2	1.6	.3	2.7	2.2	-2.8	.5	1.4	-2.1
Adjusted:												
Index[1]	100.9	90.2	85.9	89.6	94.5	92.8	98.0	94.8	92.1	92.6	93.8	92.3
Percentage change	-17.1	-10.6	-4.8	1.5	1.3	-1.7	7.2	-3.2	-2.8	.5	1.2	-1.5

[1] 1980-82 average=100.

Note.—The foreign-currency value of the U.S.dollar is a trade-weighted average in terms of the currencies of 15 other major nations.The inflation-adjusted measure shows the change in the dollar's value after adjusting for the inflation rates in the United States and in other nations; thus, a decline in this measure suggests an increase in U.S.price competitiveness.

Source: Morgan Guaranty Trust Co.of New York, October 10, 1989.

Trade balances, by selected countries and by specified periods, January 1986-September 1989

(In billions of U.S.dollars, f.o.b.basis, at an annual rate)

Country	1986	1987	1988	1989							
				I	II	Apr.	May	June	July	Aug.	Sept.
United States[1]	-137.5	-152.2	-119.5	-111.2	-103.4	-99.6	-121.2	-96.0	-98.4	-121.2	-94.8
Canada	7.1	8.3	7.2	8.0	3.2	0	7.2	2.4	4.8	2.4	([3])
Japan92.5	92.5	96.2	94.6	97.6	78.8	90.0	68.4	76.8	74.4	76.8	([3])
West Germany[2]	52.6	65.6	72.8	80.8	67.2	72.0	56.4	74.4	69.6	88.8	([3])
United Kingdom	-12.6	-16.9	-36.0	-42.0	-38.4	-44.4	-33.6	-37.2	-49.2	-44.4	-37.2
France	.1	-5.2	-5.8	-2.4	-8.4	-.7	-12.0	-6.0	-14.4	([3])	([3])
Italy	-2.0	-8.7	-10.0	-16.0	-12.4	-15.6	-18.0	-7.2	-8.4	-14.4	([3])

[1] 1986, exports, f.a.s.value, adjusted; imports, c.i.f.value, adjusted.Beginning with 1987, figures were adjusted to reflect change in U.S.Department of Commerce reporting of imports at customs value, seasonally adjusted, rather than c.i.f.value.
[2] Imports, c.i.f value, adjusted.
[3] Not available.

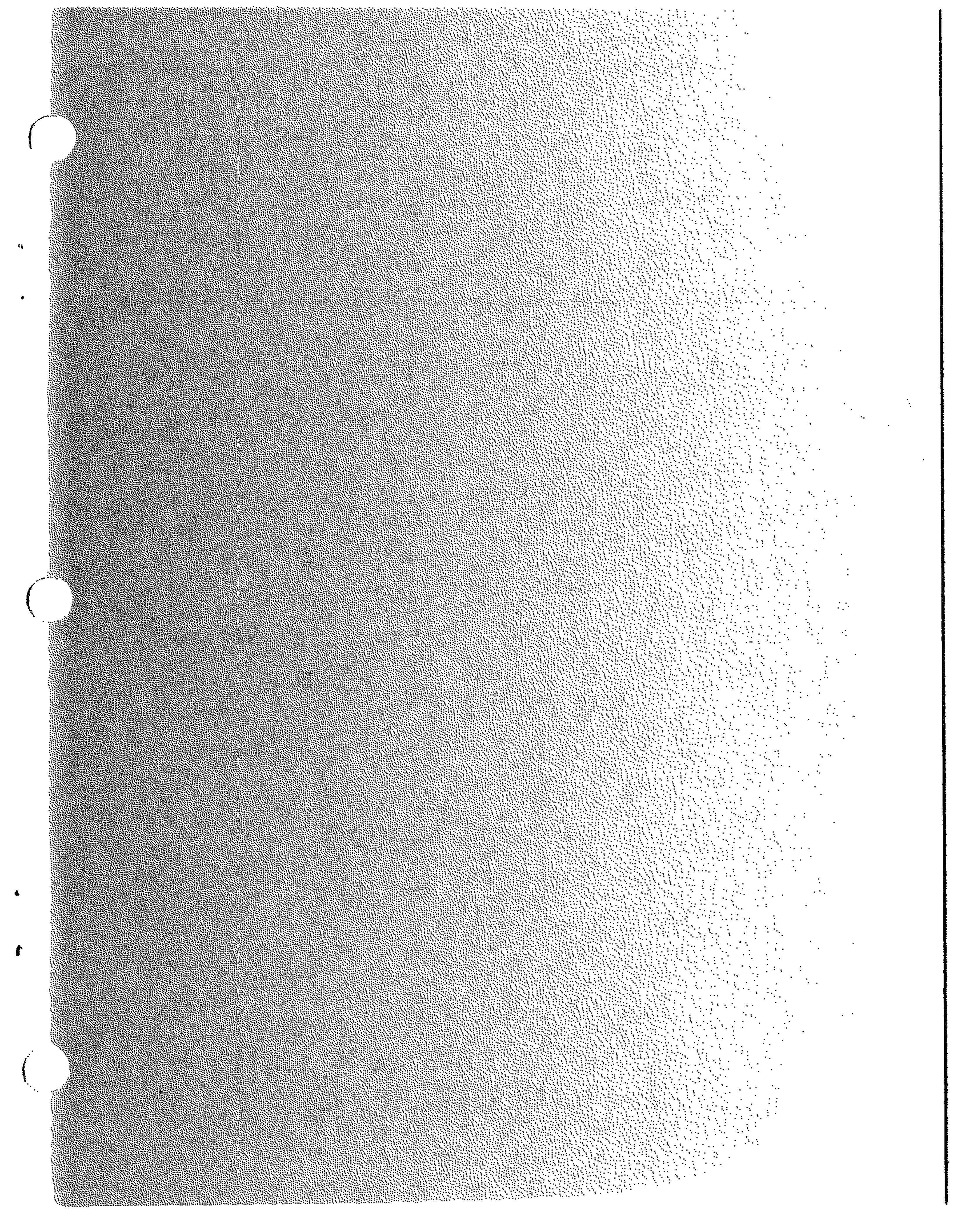
Source: *Economic and Energy Indicators*, U.S.Central Intelligence Agency, November 3, 1989, and *Advance Report on U.S.Merchandise Trade*, U.S.Department of Commerce, November 16, 1989.

U.S.trade balance, [1] by major commodity categories, by selected countries, and by specified periods, January 1986-September 1989

(In billions of U.S.dollars, customs value basis for imports)

Country	1986	1987	1988	1989								
				I	II	III	Apr.	May	June	July	Aug.	Sept.
Commodity categories:												
Agriculture	4.5	7.0	13.9	1.6	1.4	1.2	1.6	1.3	1.3	1.2	.9	1.4
Petroleum and selected products (unadjusted)	-31.8	-39.5	38.1	-3.2	-4.0	-3.8	-3.8	-4.4	-3.9	-3.9	-3.9	-3.6
Manufactured goods	-134.3	-146.1	-146.7	-8.4	-7.8	-9.0	-6.7	-8.4	-8.4	-9.3	-10.2	-7.6
Selected countries:												
Western Europe	-28.2	-27.9	-17.2	-.08	-.02	-.9	.2	-.08	-.2	-.8	-.7	1.2
Canada[3]	-23.0	-11.5	-12.6	-.9	-.5	-.7	-.4	-.7	-.5	-.4	-1.2	-.7
Japan	-55.3	-58.0	-55.5	-4.1	-4.0	-4.0	-3.9	-4.3	-3.9	-4.0	-3.9	-4.1
OPEC (unadjusted)	-8.9	-13.7	-10.7	-1.0	-1.6	-1.6	-1.3	-1.8	-1.6	-1.7	-1.8	-1.5
Unit value of U.S.imports of petroleum and selected products (unadjusted)[4]	$15.02	$18.12	$14.19	$15.17	$17.96	$16.54	$17.83	$18.40	$17.67	$17.12	$16.14	$16.38

[1] Ex ports, f.a.s.value, unadjusted.1986-88 imports, c.i.f.value, unadjusted; 1989 imports, customs value, unadjusted.
[2] Less than$50,000,000.
[3] Beginning with February 1987, figures include previously undocumented exports to Canada.
[4] Beginning with 1988, figures were adjusted to reflect change in U.S.Department of Commerce reporting of imports at customs value, seasonally unadjusted, rather than c.i.f.value.
Source: *Advance Report on U.S.Merchandise Trade*, U.S.Department of Commerce, November 16, 1989.



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