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**United States International Trade Commission
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International Trade Developments

U.S. Trade with the Beneficiaries of the Andean Trade Preference Act

New EU Agreements With African Countries Liberalize Two-way Trade

Rising U.S. Wage Inequality: Is International Trade the Cause?

U.S. Trade Developments

International Economic Comparisons



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INTERNATIONAL TRADE DEVELOPMENTS

U.S. Trade with the Beneficiaries of the Andean Trade Preference Act

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Trade with the South American beneficiaries of the Andean Trade Preference Act (ATPA) – Colombia, Peru, Ecuador, and Bolivia – accounts for a very small portion of U.S. trade. Nonetheless, its potential to create alternative income and employment opportunities to these countries' narcotics-related activities makes this trade important for the beneficiary countries.

The ATPA Program and its Effect on Beneficiaries

The South American beneficiaries of the Andean Trade Preference Act (ATPA) — Colombia, Peru, Ecuador, and Bolivia (ATPA countries) produce narcotics, trade in them, or make transit routes available for such activities. The coca plant is indigenous to the Andean mountain region, and virtually all of the world's coca production takes place in Bolivia, Colombia, and Peru. Colombia is an increasingly important supplier of heroin, too. Although Ecuador is not itself an illicit drug-producing country, it provides important transit routes for cocaine and for essential chemicals necessary to produce it.

In accordance with the U.S. objective of stemming the supply of illicit drugs at the source, ATPA goes beyond seeking to promote broad-based economic development for these beneficiaries as similar programs for other developing countries do. The U.S. program also aims specifically to provide viable economic alternatives to these countries' cultivation of crops for illicit narcotics production by offering duty-free access to the U.S. market for most of their products. In this sense, ATPA is an instrument of U.S. drug control policy.

¹ The views and conclusions expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

The cooperation of illicit drug-producing countries with the 1988 U.N. Convention on international drug control² may affect determinations by the U.S. Government on foreign assistance and multilateral banking assistance to be extended or denied to drug-producing countries. Similarly, to become or remain eligible for ATPA preferences, ATPA countries must meet certain criteria for cooperating with the United States in containing their own narcotics production and trade.

ATPA-country governments exercise containment mainly by prohibiting the cultivation of coca and opium poppy, eradicating the crops that exist, and encouraging farmers to grow other crops for alternative employment and income. The problem of the Andean governments, as well as of others trying to assist them, is that few products, if any, can viably replace coca in terms of economic return and marketability. In addition, physical and economic infrastructure, such as paved roads, storage facilities, processing plants, and financing are generally inadequate to meet the requirements of alternative legal crops and industries in the Andean coca-producing areas. By contrast, coca production requires much less infrastructure.

Under ATPA, enacted in 1991, the United States grants mostly duty-free and some duty-reduced treatment for eligible imports from the ATPA countries. The four countries became eligible at different dates in

² 1988 United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances.

1992-93, to take advantage of the program. ATPA is scheduled to expire on December 3, 2001, i.e. 10 years after the date of its enactment.³ Beneficiaries strongly advocate, however, that the termination date be extended and that the product coverage of the program be widened, especially to include apparel and footwear—product categories that do not currently qualify for duty-free entry under ATPA.

Presently, ATPA has a limited scope in the context of overall U.S. imports from ATPA countries. In 1999, some two-thirds of U.S. imports from ATPA countries were already free of duty; the bulk entered under duty-free provisions other than ATPA: general tariff rates in column-1 of the Harmonized Tariff System (HTS), the General System of Preferences (GSP), and production sharing provisions (HTS98). ATPA countries may benefit from both ATPA and GSP preferences, and sometimes have the choice of entering the same product under either one of these programs. The portion of U.S. imports entering under ATPA in 1999 accounted for 17.8 percent of all U.S. imports from the region, and the portion that qualified for duty-free treatment exclusively under ATPA (could not have entered duty-free under any other program) was 9.6 percent.

The United States International Trade Commission's (USITC) annual reports on ATPA focus on the program's impact on the United States. However, the sixth and seventh reports examined the impact of the program on the beneficiaries, specifically in promoting their export-led growth and export diversification. The sixth ATPA report contained case studies on Colombia and Ecuador, and the seventh report on Peru and Bolivia. Each report also discussed the effects of ATPA on drug-related crop eradication and crop substitution efforts in beneficiary countries. A general equilibrium analysis, which simulated the application of ATPA on the Andean region, using 1995 as the base year, was also presented in the seventh report.

The seventh report estimated that ATPA has had a small, but positive effect on the region's economy by diversifying exports to the United States, adding to the Gross Domestic Product, however slightly, and improving the terms of trade by a small amount. In addition, by providing alternative employment opportunities, ATPA may have had a small, indirect, but positive impact on the region's drug-crop eradication and crop substitution efforts in 1999. In the words of the report:

"Industries that produce ATPA-related goods provide alternative development opportunities, and although ATPA-related investment has flourished in regions where there is no presence of illicit crops, the

³ For details regarding the main provisions of ATPA, see USITC, *Andean Trade Preference Act: Seventh Report, 1999*, USITC publication No. 3358, Sept. 2000, ch. 1, and prior annual reports in this series.

program indirectly provides new sources of employment for workers that may otherwise turn to illicit crop-growing activities."⁴

Pointing out, however, that "ATPA is only one element in a multifaceted effort to combat the drug problem," the seventh report has not attempted to offer a precise estimate of the program's impact on drug-related crop eradication and crop substitution or on alternative development.

U.S. Trade with the ATPA Countries

ATPA countries account for a very small portion of U.S. trade. Nonetheless, its potential to create alternative income and employment opportunities in these countries' narcotics-related activities makes U.S. trade with these countries important. Even collectively, ATPA countries constituted only 1 percent of the world market for U.S. exports, and supplied only 1 percent of total U.S. imports in 1999. The ATPA community ranked 22nd as a destination for U.S. exports among single-country markets, ahead of Venezuela, but behind Israel. Similarly, the four countries combined were the 19th-largest U.S. supplier among all nations—larger than Switzerland but smaller than Israel.

This section covers U.S. trade with ATPA countries in 1995-99, but relies most often on 1999 data. The portion of U.S. imports that enters under ATPA is covered separately, but the discussion of imports is not restricted to the ATPA portion. The data cited are based on official statistics of the U.S. Department of Commerce. The series of annual USITC reports on ATPA, especially the sixth and seventh reports, are the principal source of additional information.

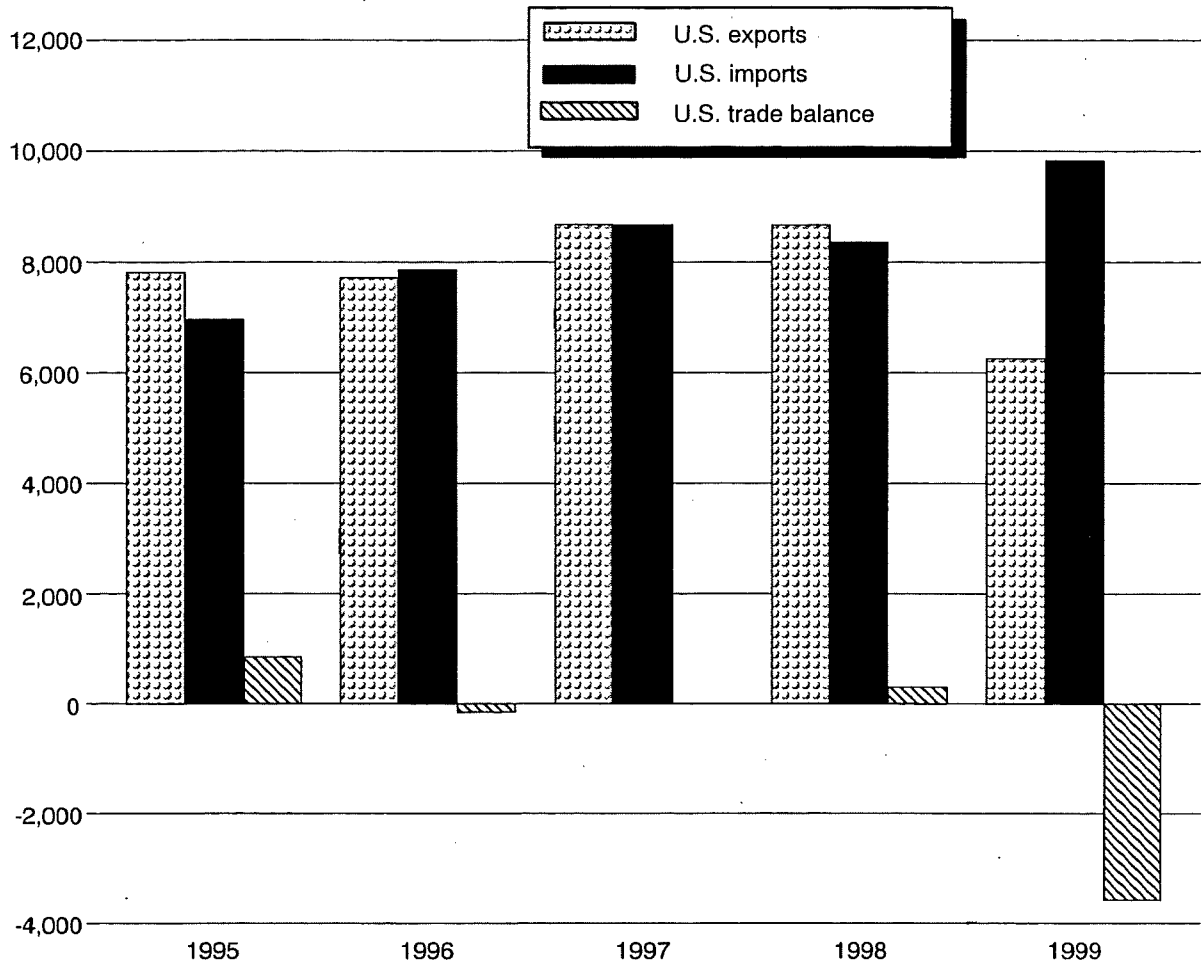
Figure 1 shows overall U.S. trade trends during 1995-99 with the ATPA countries combined. Figure 2 compares the relative significance of each ATPA country in all U.S. exports to the region, and all U.S. imports — both total imports, and those under ATPA only — from the region, as of 1999. The highlights of bilateral trade, based principally on 1999 data, are discussed separately for each ATPA country.




During the 1995-99 period, the United States generally registered a trade surplus with the ATPA countries combined. In 1999 however, U.S. trade with the ATPA community resulted in a deficit for the United States, amounting to \$3.6 billion. This uncharacteristic turn around in the U.S. trade balance was caused by a sharp decline in U.S. exports to ATPA countries (27.8 percent), and a simultaneous increase in U.S. imports from them (17.6 percent) during the year. Colombia was responsible for some 70 percent of this deficit, and Peru and Ecuador of the remainder.

⁴ *Seventh Report*, p. 73.

Figure 1
U.S. trade with ATPA countries, 1995-99

Million dollars

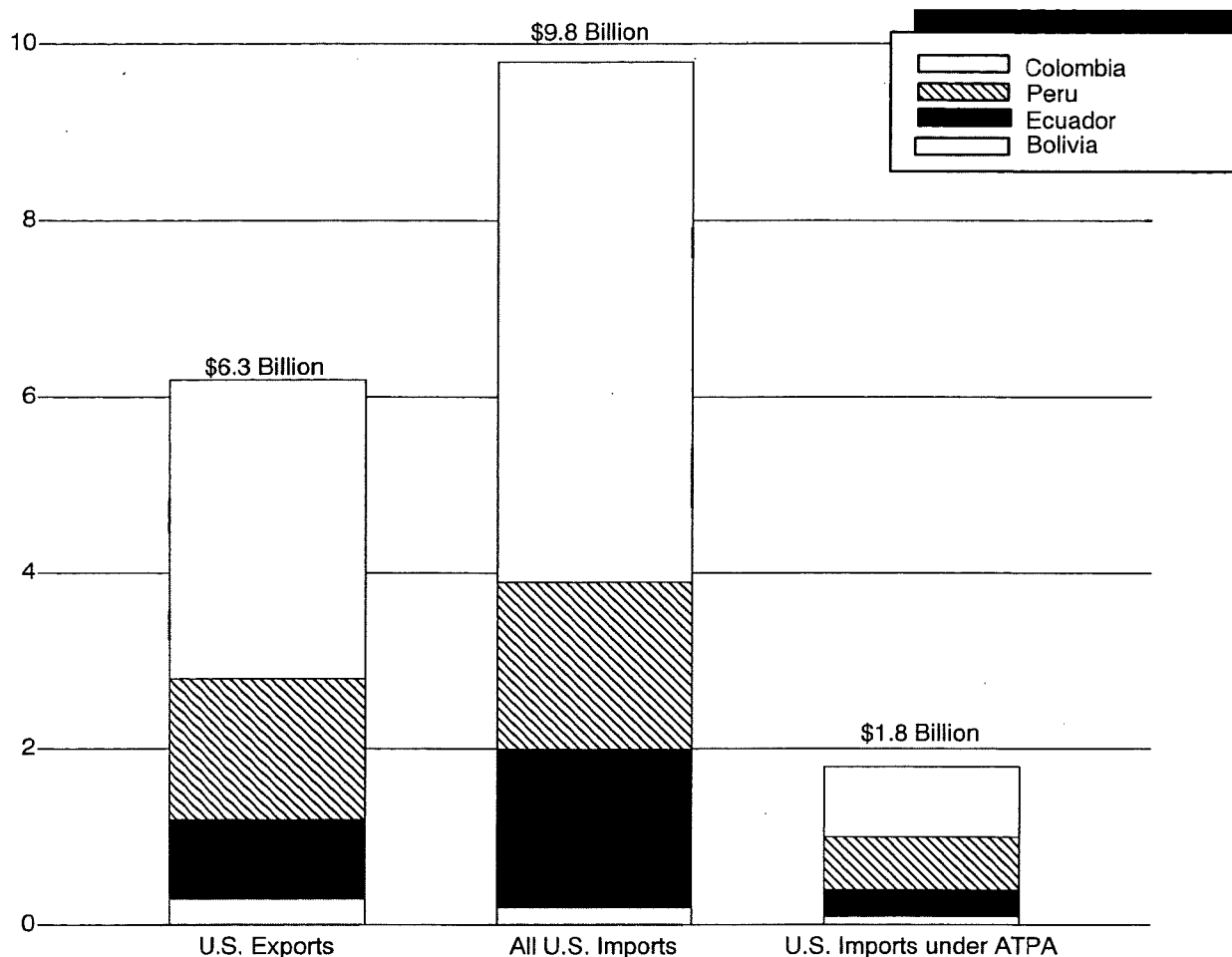


 U.S. exports	7,820.2	7,718.7	8,681.8	8,670.1	6,263.2
 U.S. imports	6,968.7	7,867.6	8,673.6	8,361.0	9,830.2
 U.S. trade balance	851.4	-148.9	8.2	309.1	-3,567.0

Source: Compiled from official statistics of the U.S. Department of Commerce.

Figure 2
ATPA Countries: Their share in U.S. trade with all ATPA countries combined, 1999

Billion dollars



Source: Compiled from official statistics of the U.S. Department of Commerce.

Combined U.S. exports to the ATPA group amounted to \$6.3 billion in 1999 compared to \$8.7 billion in 1998. U.S. exports declined to all ATPA countries, though Colombia alone was responsible for about one-half of the combined loss of U.S. exports to the region. Political and economic instability and the weakness of their currencies in terms of the strong U.S. dollar restricted these countries' ability to import their usual assortment and volume of capital and consumer goods in 1999. U.S. exports diminished in all major traditional sectors; ATPA-country markets for U.S. aircraft, motor vehicles, and electrical machinery, each

have shrunk by about 40 percent. At the same time, ATPA countries were compelled to use some of their export dollars to step up purchases of U.S. corn and wheat.

Total U.S. imports from ATPA countries (including both the portion affected and unaffected by ATPA preferences) registered \$9.8 billion in 1999, up from \$8.4 billion in 1998. Colombia accounted for virtually all of the increase, some four-fifths of which can be explained by sharply higher prices of the petroleum prod-

ucts the United States bought from Colombia, especially during the second half of the year.

Colombia

Despite government initiatives to control the narcotics problem, Colombia still accounts for about 80 percent of the world's cocaine supply, either produced in the country or traveling through it. Narcotics constitute a significant component of Colombia's national economy—about 5 percent of its GDP, according to United Nations estimates.⁵ Colombia is the largest recipient of U.S. counternarcotics assistance of all countries.

Already the few data mentioned above indicate Colombia's dominance among ATPA countries in U.S. trade with the region. Figure 2 illustrates this in terms of all significant trade flows: U.S. exports, U.S. imports, and U.S. imports that enter under ATPA provisions. Year after year, Colombia was the destination of more than one-half of U.S. exports to ATPA countries combined; in 1999, Colombia's share of the total was 55 percent. Buying principally machinery, equipment, and parts from the United States for its petroleum-related operations, as well as for communication, data processing, and transportation, Colombia also purchases a wide range of other capital and consumer goods. In addition, in 1999 Colombia received some 60 percent of corn and one-half of wheat the United States exported to ATPA countries.

Well over half of U.S. imports from all ATPA countries originated in Colombia in 1995-99. In 1999, imports from Colombia constituted almost 60 percent of combined U.S. imports from all ATPA countries, supplying some four-fifths of petroleum-based U.S. imports, and also some four-fifths of U.S. coffee imports from the ATPA community. Notably, Colombia is the second-largest coffee supplier of the United States among all countries of the world, after Brazil.

In terms of imports entered under ATPA provisions only, Colombia's prominence among ATPA suppliers is somewhat less pronounced (figure 2). Neither Colombia's petroleum-based exports nor its coffee — the number one and number two U.S. import categories from that country — contain products that enter the United States under ATPA. Petroleum products are dutiable under general tariff rates, but they are not eligible for duty exemption under ATPA. Coffee is unconditionally free of duty under general tariff rates, therefore does not require ATPA for duty-free entry. Even so, Colombia accounts for close to one-half of all U.S. imports under ATPA provisions, because several other major U.S. imports, mainly or solely from

Colombia, do enter under the program, including fresh-cut flowers, nonadhesive vinyl chloride plates, and pigments.

From the outset, fresh-cut flowers, supplied principally by Colombia, have been the leading products imported from the region under ATPA. The flower industry generated approximately 50,000 direct and 50,000 indirect jobs in the country. U.S. demand for flowers stopped growing after 1996, but other Colombian entries under ATPA surged and compensated for the sluggish export performance of flowers. More recently, pigments proved to be one of the most successful Colombian products benefitting from the program. Their first shipment to the United States took place in 1997, but imports quadrupled by 1999, when Colombia provided some four-fifths of U.S. imports of pigments from all countries of the world.

Peru

Peru, the second-largest U.S. trading partner among ATPA countries, benefits most from ATPA trade, and by implication, from the alternative employment opportunities the program may provide. In 1999, Peru supplied 36 percent of all U.S. imports under ATPA, compared with 45 percent by Colombia (figure 2). Although these shares show Colombia still as the number one ATPA beneficiary, the difference between Colombia's and Peru's percentages is much smaller than the difference between their contributions to overall U.S. imports from ATPA countries: 60 and 19 percent, respectively.

Under ATPA, Peru ships principally products whose main inputs are domestically mined nonferrous metals. Refined copper cathodes from Peru were the number one item on the 1999 list of all leading U.S. imports under ATPA from all ATPA nations. In fact, Peru was the second-largest U.S. supplier of refined copper cathodes among all countries of the world, after Canada. Peru was also the second-largest U.S. supplier of unalloyed, unwrought zinc, and the leading source of U.S. zinc-product imports among all countries of the world.

Duty-free ATPA items from Peru include some articles that are other than metal-based; notably asparagus, whose imports surged during the ATPA years. Peru is the second-ranking U.S. supplier of asparagus from all countries, after Mexico. Peruvian asparagus is grown primarily in the state of Ica, which is close to the areas of illicit coca crops, such as Ayacucho and Apurimac. Many farmers in this area have chosen to cultivate asparagus crops as an alternative to coca crops.

Outside ATPA, Peru ships mostly apparel, petroleum products, specialized coffee, and cacao to the United States. As a U.S. export market, Peru's relative significance has grown in recent years to constitute 26

⁵ U.S. Embassy representative, USITC interview, Bogota, June 8, 1999.

percent of the combined ATPA-country market in 1999.

Ecuador

The third-ranking U.S. trading partner among the ATPA countries (figure 2), in 1999 Ecuador provided 19 percent of overall U.S. imports from the region. Ecuador supplied most of the remainder of petroleum products and coffee imported from the ATPA community that did not originate in Colombia. As pointed out in reference to Colombia, neither petroleum products nor coffee are imported under ATPA. Nor do some other major U.S. imports from Ecuador enter under ATPA—such as bananas and shrimp—both of which are free of duty under general tariff rates. Ecuador had been the leading U.S. supplier of bananas among all countries of the world until 1999, when it was displaced to second place by Costa Rica. Petroleum products, coffee, bananas and shrimp make Ecuador, similarly to Colombia, relatively more important in that portion of U.S. imports from the ATPA community that do not enter under ATPA.

Ecuador also benefits from ATPA; it contributed 15 percent of all U.S. imports under the program in 1999. For example, ATPA can be credited with encouraging Ecuador's diversification into the production of flowers. Colombia the principal U.S. flower supplier, Ecuador is the second one, exporting predominantly roses to the United States. Processed tuna (not in cans) is also an ATPA product, of which Ecuador is the leading U.S. provider worldwide. However, Ecuador's political and economic instability in recent years, which has damaged investor confidence and depressed the country's economic development and trade, may have diminished Ecuador's opportunity to benefit from ATPA.

Bolivia

Diversification of Bolivian exports to the world, including to the United States, has been moderate. Poor

infrastructure, and lack of the technical knowledge necessary to comply with U.S. standards and product specification have made it difficult for Bolivian farmers to market their products in the United States. Some diversification has taken place in the nonagricultural area, assisted by ATPA. Mostly jewelry, and some wood and leather products benefitted from the program.

U.S. imports from Bolivia under ATPA had increased through 1996 to constitute 8 percent of combined imports under the program from all beneficiaries. This could be attributed to rising U.S. imports of jewelry products that are eligible to enter under ATPA. Thereafter, however, Bolivian jewelry sales to the United States declined, depressing U.S. imports from Bolivia under ATPA to less than 4 percent of the total. The plight of Bolivia's jewelry industry is ascribed, in part, to an adverse change in internal tax policies during 1995. Notably, U.S. jewelry imports dropped not only from Bolivia but from all ATPA (and other South American) countries in 1999 in favor of Asian sources—India, Thailand, Hong Kong, and China—apparently because these countries priced their products more competitively in the wake of their recent financial crisis.

On all counts, Bolivia is by far the smallest U.S. trading partner among ATPA countries in 1999; it contributed little over 2 percent to overall U.S. imports from all ATPA countries combined (figure 2). U.S. imports from Bolivia outside the program contained mostly nonferrous metals, mineral fuels, and apparel. Bolivia's major exports, including natural gas and soybean products are destined mostly for South American and Caribbean markets.

Being more important as a destination of U.S. exports than as a source of U.S. imports, Bolivia receives almost 5 percent of combined U.S. exports to ATPA countries. Since 1997, the U.S. trade balance with Bolivia has been positive; in fact, Bolivia was the only ATPA country with which the United States registered a trade surplus in 1999.

New EU Agreements with African Countries Liberalize Two-way Trade

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The European Union (EU) is negotiating new trade agreements with African nations that will improve EU access to their markets. In the year 2000 alone, an EU-South Africa free trade agreement entered into effect, and a new EU agreement with developing African, Caribbean, and Pacific (ACP) countries was signed.

The European Union's (EU) network of preferential trade agreements has been growing rapidly. The nations of Africa have not been left out of this process. In January 2000, an EU-South Africa free trade agreement (FTA) entered into effect, and in June a new EU agreement was signed with developing African, Caribbean, and Pacific (ACP) countries, including 48 African countries, all of which are in Sub-Saharan Africa. In addition, EU negotiations to conclude free trade areas with its Mediterranean neighbors, including nations in North Africa, are underway. In each of these agreements, the EU is requiring partner countries to provide greater EU access to their markets than in the past. An overview of the trade provisions of these agreements is presented below.²

EU-South Africa FTA³

The EU-South Africa Agreement on Trade, Development and Cooperation (TDCA) represents one of the

¹ The views and conclusions expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

² Sources consulted for this article include U.S. Department of State telegram, "Overview of EU Preferential Trade Agreements (TPRM)," message reference No. 3435, prepared by U.S. Mission to the EU, Brussels, June 14, 2000; WTO, *Trade Policy Review, European Union: July 2000*, (WT/TPR/S/72) including accompanying *Press Release and Report by the Secretariat—Summary Observations*, found at Internet address http://www.wto.org/english/tratop_e/tp_r_e/tp137_e.htm, retrieved Sept. 19, 2000; and Europe Information Service, *European Report*, various articles.

³ Additional sources consulted for this section include European Commission, "EU and South Africa Sign A Historic Trade and Development Cooperation Agreement," press release, IP/99/735, Oct. 11, 1999; U.S. Department of State telegram, "Details of EU-South Africa FTA," message reference No. 2051, prepared by U.S. Mission to the EU, Brussels, April 3, 2000; and U.S. Department of State telegram, "SA-EU Free Trade Agreement," message reference

first FTAs (along with the EU-Mexico agreement) for the EU to enter with a nation outside the European sphere. The trade provisions of the agreement, which entered into effect on January 1, 2000, aim to create a free trade area between the EU and South Africa after a transition period of 12 years. The agreement is asymmetrical in terms of both timing and coverage. The EU will grant duty-free status to 95 percent of South Africa's exports over a 10-year period, whereas South Africa will grant duty-free treatment to 86 percent of EU exports over a 12-year period. Also, the EU will cut tariffs more quickly than South Africa; most of the EU's tariff reductions are expected to be implemented by 2002 whereas South Africa's tariff reductions will be made primarily between 2006 and 2012. Within 5 years, the two parties are to assess the possibility of concluding an FTA for services.

Prior to the agreement, approximately 56 percent of EU products entered South Africa duty-free, with the bulk of the remaining exports subject to relatively high import duties of greater than 10 percent. About 75 percent of South African exports entered the EU duty-free, with about 5 percent of such exports facing tariffs greater than 10 percent. However, a number of South African goods, primarily agricultural, faced EU quotas.

The EU has been criticized for its failure to provide meaningful access to South African agricultural products. The following South African products are excluded from the agreement: bovine meat, dairy products, oranges, apples, pears, corn, rice, preserved tomatoes, grape juice, and vermouth, as well as aluminum on the industrial side. The 14 percent excluded products on the South African side are both industrial, including textiles, footwear, and cars, as well as agricultural, including meat, dairy products, wheat, and barley.

³—Continued
No. 5554, prepared by U.S. Mission to the EU, Brussels, April 29, 1999.

EU-ACP Partnership Agreement⁴

In February 2000, the EU and 71 African, Caribbean, and Pacific (ACP) countries concluded a 20-year cooperation agreement, just days before its precursor agreement—the Fourth Lomé Convention—expired.⁵ Under the new agreement, two-way FTAs will replace the unilateral trade preferences the EU has granted its ACP partners under the Lomé Convention.

The Lomé Convention granted non-reciprocal duty-free access to the EU market for most ACP exports, with 95 percent of tariff lines duty-free. ACP exports of industrial goods (including textiles) and processed agricultural products entered the EU duty and quota free, whereas agricultural products faced a more restricted regime, including tariff quotas.

The new EU-ACP Partnership Agreement, sometimes referred to as the Cotonou Agreement because it was signed in Cotonou, Benin, entered into effect provisionally on March 1. The new agreement maintains the one-way preferential treatment of ACP exports until December 31, 2007, at the latest. During the 8-year transition period (2000-2008), the parties agreed to conclude new WTO-compatible trade arrangements that will liberalize access for EU products on ACP markets. These new agreements will likely be negotiated between the EU and regional groups of ACP countries and are often referred to as regional economic partnership agreements (REPAs). The REPAs are supposed to enter into force by January 1, 2008, at the latest.

Negotiations to conclude REPAs are not expected to formally begin until September 2002. Between now

⁴ Additional sources consulted for this section include *Partnership Agreement Between the African Caribbean and Pacific States and the European Community and its Member States*, Title II, Feb. 8, 2000; *Joint Declaration On Market Access in the EC-ACP Partnership*, Feb. 8, 2000; European Commission, Development Directorate, "The New ACP-EC Agreement," found at Internet address http://europa.eu.int/comm/development/cotonou/index_en.htm, retrieved Sept. 6, 2000; *European Union Requests WTO Waiver for the New ACP-EC Partnership Agreement*, found at Internet address http://europa.eu.int/comm/trade/bilateral/acp/wto_waiver.htm, retrieved Sept. 6, 2000; European Commission, "The European Community and its Member States Sign a New Partnership Agreement With the African, Caribbean and Pacific States in Cotonou, Benin," press release, IP/00/640, June 21, 2000; European Commission Delegation, "European Commission Proposes 'Everything But Arms' (EBA) Initiative: Duty-free, Quota-free Access For All Products From All Least Developed Countries Into the EU," press release, No. 55/00, Sept. 20, 2000; and U.S. Department of State telegram, "Outlines of Future EU-Africa, Caribbean, Pacific (ACP) Trade Regime Agreed," message reference No. 7620, prepared by U.S. Mission to the EU, Brussels, Dec. 21, 1999.

⁵ South Africa is an ACP country; however, the TDCA governs South Africa's trade relations with the EU.

and 2002, the EU member states must approve negotiating mandates that will define in more detail the trade regime, including sectoral coverage, envisioned in these agreements. Such mandates are required before the EU Commission can formally enter into specific trade negotiations, including REPAs.

The REPAs will require the "progressive and reciprocal removal of trade barriers," probably over a 12-year transition period. The EU-South Africa free trade agreement is expected to serve as a model. The EU-ACP Partnership Agreement offers some guidelines in concluding REPAs. According to the Agreement, "Negotiations shall take account of the level of development and the socio-economic impact of trade measures on ACP countries, and their capacity to adapt and adjust their economies to the liberalisation process. Negotiations will therefore be as flexible as possible in establishing the duration of a sufficient transitional period, the final product coverage, taking into account sensitive sectors, and the degree of asymmetry in terms of timetable for tariff dismantlement, while remaining in conformity with WTO rules then prevailing."⁶ On the EU side, "trade liberalisation ... shall aim at improving current market access for the ACP countries through inter alia, a review of the rules of origin."⁷ In addition to trade in goods, the Agreement also calls for REPAs to include trade in services.

REPAs will be negotiated with those countries wishing to participate. For those countries that do not want to negotiate a REPA and are least developed countries, which include 33 of the 48 African ACP states, the EU intends to implement a new regime that will offer unilateral free trade treatment on "essentially all products" by 2005. Indeed, the EU Commission proposed a plan in September that will grant duty-free and quota-free access for all products except arms from least developed countries. This proposal essentially extends the duty-free treatment currently accorded to exports of the least developed countries to agricultural products. For those countries that are not among the least developed, and do not wish to negotiate a REPA, in 2004 the EU Commission will examine "alternative possibilities, in order to provide these countries with a new framework for trade which is equivalent to their existing situation and in conformity with WTO rules."⁸ These countries would likely be graduated to the EU's Generalized System of Preferences (GSP), but they would lose substantial margins of preference under the current GSP. The present GSP expires December 31, 2004, and could be revised, but it is currently unclear how the GSP could be amended to offer the non-least

⁶ *Partnership Agreement Between the African Caribbean and Pacific States and the European Community and its Member States*, Title II, Feb. 8, 2000.

⁷ *Ibid.*

⁸ *Ibid.*

developed countries access equivalent to Lomé and remain WTO-compatible.

EU Association Agreements With North African Countries⁹

In 1995, the EU launched the Euro-Mediterranean Partnership (sometimes referred to as the Barcelona Process), a comprehensive initiative governing the EU's economic, political, and social relationship with its 12 Mediterranean neighbors. Four of these 12 partners are countries in North Africa: Algeria, Egypt, Morocco, and Tunisia. One goal of the Euro-Mediterranean Partnership is to create a Euro-Mediterranean free-trade area by 2010. To help achieve this goal, the EU is currently negotiating so-called association agreements to replace the first generation cooperation agreements the EU negotiated bilaterally with Mediterranean countries in the 1970s.

Like the EU-ACP Partnership Agreement, the trade-related provisions of these association agreements can be distinguished from past agreements by

⁹ Additional sources consulted for this section include European Commission, External Relations Directorate, "The Mediterranean and Middle East Policy of the European Union," found at Internet address http://europa.eu.int/comm/external_relations/med_mideast/intro/index.htm, retrieved Sept. 11, 2000; and various Euro-Mediterranean Partnership Information Notes, found at Internet address <http://www.euro-med.net>, retrieved Oct. 4, 2000.

the greater degree of market access granted to EU products. (Under the cooperation agreements, the EU generally grants unilateral duty-free treatment for industrial products (there are some exceptions), with limited concessions for agricultural products.) Each of the Euro-Mediterranean association agreements calls for a bilateral free trade area covering industrial products and the progressive liberalization of trade in agricultural products, such as tariff concessions within quotas. Under the new agreements, EU concessions in agriculture remain limited, and are based on actual trade, which is small, rather than on potential trade flows. However, the agreements each require a review of the agricultural situation at a later time. The agreements also call for the parties to assess the possibility of liberalizing services trade in 5 years from the date of entry into force. Depending on the agreement, the Mediterranean partner country could have up to 12 years to dismantle tariffs on EU exports.

Association agreements with Tunisia and Morocco have already entered into effect, on March 1, 1998 and March 1, 2000, respectively. Negotiations with Egypt were concluded in June 1999 and negotiations with Algeria are at an early stage. In September, the EU Commission issued a Communication (policy paper) recommending accelerating the negotiation and implementation of Euro-Mediterranean association agreements. In particular, the EU Commission is requesting Egypt sign its association agreement and has set a target date of June 2001 to conclude an EU-Algeria association agreement. In the meantime, cooperation agreements continue to govern EU trade with Egypt and Algeria.

Rising U.S. Wage Inequality: Is International Trade the Cause?¹

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The U.S. has experienced a sharp rise in the wage gap between skilled and unskilled workers since the mid-1970s. This rise in wage inequality is highly correlated with rising imports from low-income countries. This article makes the case that trade, while a possible contributor to wage inequality, is not the most important cause. Technological change instead appears to be the primary cause of rising wage inequality.

Are the wages of unskilled U.S. workers imperiled by trade with low-income countries? Certain commentators think so, and economists concede that it's theoretically possible. Although arguments over who wins and who loses from a given trade agreement are nothing new, the stakes in this discussion are particularly high. Over the last two decades the U.S. has seen a dramatic increase in wage inequality at the same time that trade with low-income countries has flourished. It's understandable, then, that some labor leaders, commentators, and even third-party presidential candidates have seized upon this broad correlation as evidence that international trade is the primary cause of rising wage inequality. It's understandable, but a growing consensus in the economics profession doubts whether the rising trade volumes actually cause the rising wage inequality. According to this consensus view, trade probably contributes somewhat to the rising wage gap, but the most important cause lies with forces harder to observe than globalization, forces even harder to resist.

U.S. and International Wage Inequality

For at least a decade before the mid-1970s, there was a narrowing gap between the wages of college-educated workers and the wages of those with only a high-school education. Although this narrowing provoked some concern over the falling returns to education, viewed more positively the falling inequality meant a less economically polarized society. The late 1970s, however, saw a dramatic turnaround in this trend. Having fallen by 10 percent from 1967 to 1979,

¹ The views and conclusions expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

by 1995 the ratio of median earnings for college-educated versus high-school educated male workers increased from 1.3 to about 1.7, a rise of over 30 percent.² The overall change was due to earnings changes at the top and the bottom of the distribution. The top-10 percent of male income earners enjoyed an 8-percent earnings increase (a 14-percent increase for the top 5 percent), while men in the bottom decile of full-time workers saw their earnings decline by a staggering 21 percent.

Such dramatic changes in the labor market have not been unique to the United States. Although only the United Kingdom has experienced similar changes in income inequality, a second group including Canada, Australia, and Israel experienced substantial increases in the gap between the rich and the poor.³ And although most of Europe has escaped these troubling events, they've suffered their own difficulties. Most countries in the European Union (EU) have seen much slower job growth than that experienced in the United States, and much higher rates of unemployment.⁴

² The data are from the U.S. Counsel of Economic Advisors, tabulations of the March Current Population Survey. See Susan Collins, 1999, *Imports, Exports, and the American Worker*, Brookings, for an excellent review of recent trends. The use of data on male full-time workers are used to eliminate other factors, like the seasonality of part-time work, and women's changing work-force participation rates.

³ Peter Gottschalk and Timothy M. Smeeding, 1997, "Cross National Comparisons of Earnings and Income Inequality," *Journal of Economic Literature* 35, June, 633-87 provide a detailed review of changes in inequality for the United States, and other countries in the Organization of Economic Cooperation and Development (OECD).

⁴ From 1970 to 1995 U.S. job creation was three times that found in Japan, and six times that found in the EU. See Collins (1999) page 15. For data and discussion of unemployment in European labor markets, see Stephen Nickell, "Unemployment and Labor Market Rigidities: Europe Vs. North America," *The Journal of Economic Perspectives*, Vol 11, No. 3, Summer 1997, 55-74.

Many European labor markets are more tightly regulated than the U.S. market, with stronger institutions that determine wages. This means that if they faced the same forces active in the United States, the result might be changes in employment rather than changes in wages. There's a growing consensus that, while the labor-market manifestations of the problem may differ across countries, a common cause is at work.⁵

The search is on, then, for this common cause that has resulted in wage declines in some countries, and increases in unemployment in others. While economists have identified a number of possible explanations, including immigration, changes in the quality of schooling, and a loss of union organizing power, two explanations – international trade and technological change – have captured the most attention. And it turns out that the choice is particularly important; the policies one might recommend to combat inequality depend crucially on the source of the problem.

One of the salient characteristics of the late 20th-century global economy is the rising volume of international trade. Liberalization, the lowering of tariffs and other barriers, has led to striking increases in the volume of trade, including trade between high- and low-income countries.⁶ Between 1978 and 1990 the United States turned a \$ 32.8 billion trade surplus with developing countries into a \$ 34.9 billion deficit. And the share of total U.S. imports coming from these same countries increased by 40 percent between 1980 and 1995. Furthermore, the composition of U.S. trade with low-income countries has shifted from primary products to manufactures. While only 18 percent of U.S. manufactures imports arrived from low-income countries in 1973, the share increased to fully 34 percent by 1995.⁷

The Trade-and-Inequality Hypothesis

Economists Wolfgang Stolper and Paul Samuelson in 1941 explained the theoretical link between such changes in trade volume and changes in wages.⁸

⁵ The Organization of Economic Cooperation and Development (*Jobs Study, Evidence and Explanations*, 1993) concludes that there has been a decrease in demand for unskilled workers across member countries.

⁶ Besides the liberalization of trade, the overall political climate has also made low-income country participation in trade possible. Once suspicious of trade with the industrialized countries, the leadership of most low-income countries now seek to deepen such trade links.

⁷ While the EU has also seen increased imports from low-income countries, the change has been more muted than that seen in the U.S.

⁸ Wolfgang Stolper and Paul A. Samuelson, 1941, "Protection and Real Wages", *Review of Economic Studies*, November: 58-73. A volume honoring its 50-year anniversary, *The Stolper-Samuelson Theorem, A Golden Jubilee*, 1994, was edited by Alan Deardorff.

Although unskilled workers in other countries export manufactured goods to the U.S., they put downward price pressure on similar U.S. goods, which in turn forces U.S. workers in these industries to accept lower wages. Eventually the wage competition spreads out into other industries, lowering the wages of unskilled workers in all sectors of the U.S. economy. Increased U.S. exports, Stolper and Samuelson explained, will in a similar fashion lead to wage increases for the high-skilled workers typically employed in export industries. In this way, then, increased imports and exports might be responsible for wage changes at the top and the bottom of the earnings distribution. Phrased differently, the Stolper-Samuelson theorem suggests that unskilled U.S. workers have little to fear from trade with countries like Canada and Japan, but trade with countries like Mexico is another story. In trade with countries where unskilled labor is abundant, the potential U.S. labor market consequences are large.⁹

Although the trade-and-inequality hypothesis had the powerful Stolper-Samuelson Theorem behind it, weaknesses in the argument soon became apparent. First, despite the recent increases in trade with low-income countries noted above, the share of such trade in the U.S. economy is quite small. By 1995 trade with low-income countries was only 3 percent of U.S. GDP (an increase from 0.5 percent in 1973). Furthermore, only 2 percent of the U.S. workforce were employed in industries (apparel, leather, and furniture) that faced substantial competition from low-income countries.¹⁰ Many economists doubted whether a 2.5-percent increase in the share of low-income country imports in the U.S. economy, in competition with 2 percent of our workforce, could be responsible for the dramatic increases in U.S. wage inequality.¹¹

More deeply, as noted above, for trade to be the cause of rising inequality, there had to be price pressure from imports. Apart from such price changes, unskilled workers would not face any pressure to accept lower wages. Close examination, however, failed to

⁹ While the focus of this article is on the consequences of trade for wage inequality, two things should also be noted. While trade with low-income countries might harm low-wage workers, U.S. consumers clearly gain from such trade. In fact, the gains to consumers are larger than the losses workers suffer. Also worth remembering is that if international trade is lowering the wages of certain jobs, it is also raising the wages of workers employed in export industries.

¹⁰ Manufacturing generally accounts for about 15 percent of the workforce.

¹¹ See Edward Leamer, "In Search of Stolper-Samuelson Linkages", pages 141-214 in the Collins 1999 volume for a strong dissent from this generally held view. In Leamer's view, "The 1970s was a Stolper-Samuelson decade with price, trade, and employment data consistent with the presence of Stolper-Samuelson effects on wage inequality."

find such price declines.¹² It's worth focusing on this point for a moment. The trade-and-inequality hypothesis rests on the Stolper-Samuelson Theorem. And this theorem begins with decreases in the price of imports, which leads to increases in trade volumes, which finally causes wage declines for the unskilled. If the import price decline doesn't happen, then Stolper-Samuelson cannot be the primary cause of the rising U.S. wage gap between skilled and unskilled workers.

This does not mean, however, that economists absolve international trade from all responsibility for the rising wage inequality we have observed. A number of "factor-content" studies asked how U.S. wages would look if the import surge from developing countries had never happened. These studies typically found quite small wage effects from international trade, though the results are quite sensitive to assumptions on how easy it is to substitute low-skilled for high-skilled workers. One prominent study by Sachs and Schatz suggested that trade may account for as much as 5 percentage points of the relative decline in wages for high-school educated workers.¹³ Another study by Borjas, Freeman and Katz attributed 8 percent of the relative wage declines of high-school dropouts to the combination of trade and immigration.¹⁴ Taken together, these studies suggest that trade (and immigration) contributes to inequality, but they also suggest that the primary explanation of recent wage trends lies elsewhere.¹⁵

New Insights

As skepticism about the trade-and-inequality hypothesis grew, another theory began to take center

¹² Jagdish Bhagwati and Vivek Dehejia, "Freer Trade and Wages of the Unskilled: Is Marx Striking Again?" in *Trade and Wages: Leveling Wages Down?* 1994, Edited by Jagdish Bhagwati and Marvin H. Kesters, 36-75. Washington: American Enterprise Institute. See also Paul R. Krugman, and Robert Z. Lawrence, 1994, "Trade, Jobs, and Wages," *Scientific American* 270, April, pages 44-49.

¹³ Jeffrey D. Sachs and Howard J. Shatz, "International Trade and Wage Inequality in the United States: Some New Results", in Collins (1999). See also Michael A. Anderson and Stephen L.S. Smith, "Canadian Trade and Wages: Lessons from the Past, Prospects for the Future," *The World Economy*, August 2000, pages 1005-29, for a similar analysis of Canadian wage trends.

¹⁴ George J. Borjas, Richard B. Freeman, and Lawrence F. Katz, "Searching for the Effect of Immigration on the Labor Market," *The American Economic Review*, 86, May 1996, pages 10-16.

¹⁵ Dani Rodrik, in his 1997 book *Has Globalization Gone Too Far?* Washington: Institute for International Economics, has challenged such calculations by proposing alternative channels by which globalization could affect wage trends. For example, he notes that if managers now have a more credible threat to move production off shore, U.S. workers' bargaining position on wages and benefits would be much eroded. This erosion takes place *even if* there's been no observable increase in imports.

stage, albeit only with indirect evidence. If trade really were the cause of wage declines, plant managers would hire more unskilled workers, and fewer skilled workers, to reduce costs. Yet the exact opposite has happened; across manufacturing industries the trend has been to replace unskilled workers with more skilled laborers.¹⁶ While appeals to rising international trade cannot explain this trend, changes in technology can.

The literature studying wage inequality has now turned its attention to technological change, and there is a growing consensus among economists that there has been a profound and widespread change in technology that makes skilled workers more productive while leaving unskilled-worker productivity unchanged. Such changes in technology can explain the changes in wages we have observed, while also explaining why employers continue to prefer skilled to unskilled workers, despite the low wage costs associated with hiring the unskilled. The Bureau of Labor Statistics, for example, has done case studies that show technological innovation lowering the need for unskilled workers.¹⁷ Brauer and Hickok discovered that industries that have engaged in the most "high-tech" capital investment have seen the largest wage gains.¹⁸ Finally, there is also growing evidence that such technological change is not confined to the U.S., but instead is widespread across high-income countries.¹⁹ But it's going to take time before all of this evidence is in. Until then, the jury will remain out on whether international trade or technological change is the cause of recent wage changes, and reputable economists will continue to advance the trade hypothesis, even if they are part of a shrinking minority.²⁰

Implications

The last question is, what's to be done? The literature summarized above suggests that there are multiple sources of growing wage inequality. Recommended policy prescriptions have ranged from limiting imports

¹⁶ The share of "production workers" (those workers directly engaged in the production of goods, a proxy for the share of less-skilled workers) in manufacturing employment began to decrease in about 1970, with sharp declines beginning in the mid-1970s. Intriguing recent work by Professor Matthew Slaughter at the National Bureau of Economic Research shows a turnaround in this trend in the early 1990s.

¹⁷ Jerome S. Mark, 1987, "Technological Change and Employment: Some Results from BLS Research," *Monthly Labor Review*, 26-29.

¹⁸ David A. Brauer, and Susan Hickok, "Explaining the Growing Inequality in Wages Across Skill Levels," *Federal Reserve Bank of New York Policy Review*, 1995, Vol 1, No 1, pages 61-75.

¹⁹ See Eli Berman, John Bound, and Stephen Machin, "Implications of Skill-Biased Technological Change: International Evidence," *The Quarterly Journal of Economics*, 1998, Vol 113, No 4, November pages 1245-1281.

²⁰ Prominent among this group is Adrian Wood. See, for example, his 1994 book, *North-South Trade, Employment, and Inequality*. New York: Oxford University Press.

to worker-focused programs. If trade is the culprit for the wage gap then limiting imports, some argue, would raise the wages of unskilled U.S. workers. But economists generally agree that limiting trade creates more losses than gains. Consumers rely on imports for certain affordable, high-quality goods, and producers count on trade for needed inputs for manufacturers and services output. If technology is the culprit for the growing wage gap, effective policy will focus on workers rather than on imports. A consensus in the economic's literature seems to be forming around the idea focusing policy on at-risk workers (unskilled workers currently employed) and those who have already faced severe losses through unemployment, whatever the cause of their job loss.

Many economists argue that education and on-the-job training, often lumped together and called "skill upgrading" are important policy options for the first group of workers (unskilled but still employed). Other economists suggest that progress could be made by moving society's redistributive programs away from reliance on income transfers and toward the transfer of productive assets.²¹ That is, they propose that instead of being promised a pension at retirement, that people instead be given an endowment at birth that could be used to pay for education and other training. Such productive assets could, they suggest, help level wages whatever the cause of the rising inequality.

²¹ Richard Freeman, *The New Inequality*, 1999, Boston: Beacon Press. The study examines those Pennsylvania workers who, between 1980 and 1986, lost their jobs due to plant closure or mass layoffs.

For unskilled workers who have lost their jobs, recent research has found just how catastrophic are the lifetime income declines. One study, for example, finds that the present value of earnings losses for the average displaced unskilled worker are about \$80,000. And \$60,000 of this total is due to lower earnings on the new job.²² The study notes that, for displaced workers, retraining is not particularly effective. The "take-up rate," the percent of eligible workers who enroll in the training, is low, and many workers who enroll find it difficult to adapt to a classroom setting. This study suggests a potentially more effective approach would be income transfers to support the workers' families, and wage subsidies to make them more attractive to potential employers.²³ This study also suggests that for income transfers to be effective in combating wage inequality arising from technological change, it would be important to not limit such subsidies to those workers who lost their jobs due to trade-related competition.

Taken together, the literature suggests that careful policy choices are necessary if we desire to aid the lowest-income families who have seen the largest wage declines. Given the recent interest in this topic, there is also reason to hope that new ideas and policy options will continue to enliven this discussion.

²² Louis Jacobson, "Compensation Programs," in Collins (1999).

²³ The U.S. Trade Deficit Review Committee divided between Republicans and Democrats on all issues discussed in their report, except for how to help at-risk workers. There was broad agreement on the possible usefulness of wage subsidies and other forms of earnings insurance. For more on this point and other policy options, see Lori G. Kletzer, 2000. "What are the costs of job loss from import-competing industries in the U.S.?: Some basics for policy-making," Institute for International Economics, November.

U.S. TRADE DEVELOPMENTS

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The U.S. Department of Commerce (Commerce News FT 900 (00-08)) reported that seasonally adjusted exports of goods and services of \$93.0 billion and imports of \$122.5 billion in August 2000 resulted in a goods and services trade deficit of \$29.4 billion, \$2.3 billion less than the \$31.7 billion deficit of the month of July. August exports of goods and services were \$3.2 billion more than July exports of \$89.8 billion. August imports were 1.0 billion more than July imports of \$121.5 billion.

August 2000 exports of goods increased to \$68.0 billion from \$65.1 billion in July. August imports of goods increased to \$104.4 billion from \$103.6 billion in July and the August deficit on goods decreased by \$2.1 billion to \$36.4 billion. For services, exports increased to \$25.1 billion in August from \$24.7 billion in

July and imports of services increased to \$18.1 billion from \$17.9 billion, resulting in services August surplus of \$7.0 billion, slightly higher than the July surplus of \$6.8 billion.

The overall change in exports of goods in July-August 2000 reflected increases in capital goods, industrial supplies and materials, automotive vehicles parts and engines, and consumer goods and foods, feeds, and beverages. A decrease occurred in other goods category. The overall changes in imports of goods reflected increases in capital goods, consumer goods, and other goods category. Decreases occurred in industrial supplies and materials, and automotive vehicles, parts and engines. Foods, feeds, and beverages remained virtually unchanged. Additional information on U.S. trade developments in agriculture and specified manufacturing sectors, in January-August 2000, are highlighted in tables 1 and 2 and figures 3 and 4. Services trade developments are highlighted in table 3.

¹ The views and conclusions expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

Table 1
U.S. trade in goods and services, seasonally adjusted, July-Aug.2000
(Billion dollars)

Item	Exports		Imports		Trade balance	
	August 2000	July 2000	August 2000	July 2000	August 2000	July 2000
Trade in goods (see note)						
Current dollars-						
Including oil	68.0	65.1	104.4	103.6	-36.4	-38.5
Excluding oil	67.7	64.8	93.7	92.8	-26.0	-28.0
Trade in services						
Current dollars	25.1	24.7	18.1	17.9	7.0	6.8
Trade in goods and services:						
Current dollars	93.0	89.8	122.5	121.5	-29.4	-31.7
Trade in goods (Census basis)						
1996 dollars	75.7	72.0	112.5	111.1	-36.8	-39.1
Advanced-technology products (not seasonally adjusted) ...	19.7	18.1	20.1	18.5	-0.4	-0.4

Note.—Data on goods trade are presented on a balance-of-payments (BOP) basis that reflects adjustments for timing, coverage, and valuation of data compiled by the Census Bureau. The major adjustments on BOP basis exclude military trade, but include non-monetary gold transactions and estimates of inland freight in Canada and Mexico not included in the Census Bureau data. Because of rounding details may not add to totals shown.

Source: U.S. Department of Commerce News (FT 900), Oct. 19, 2000.

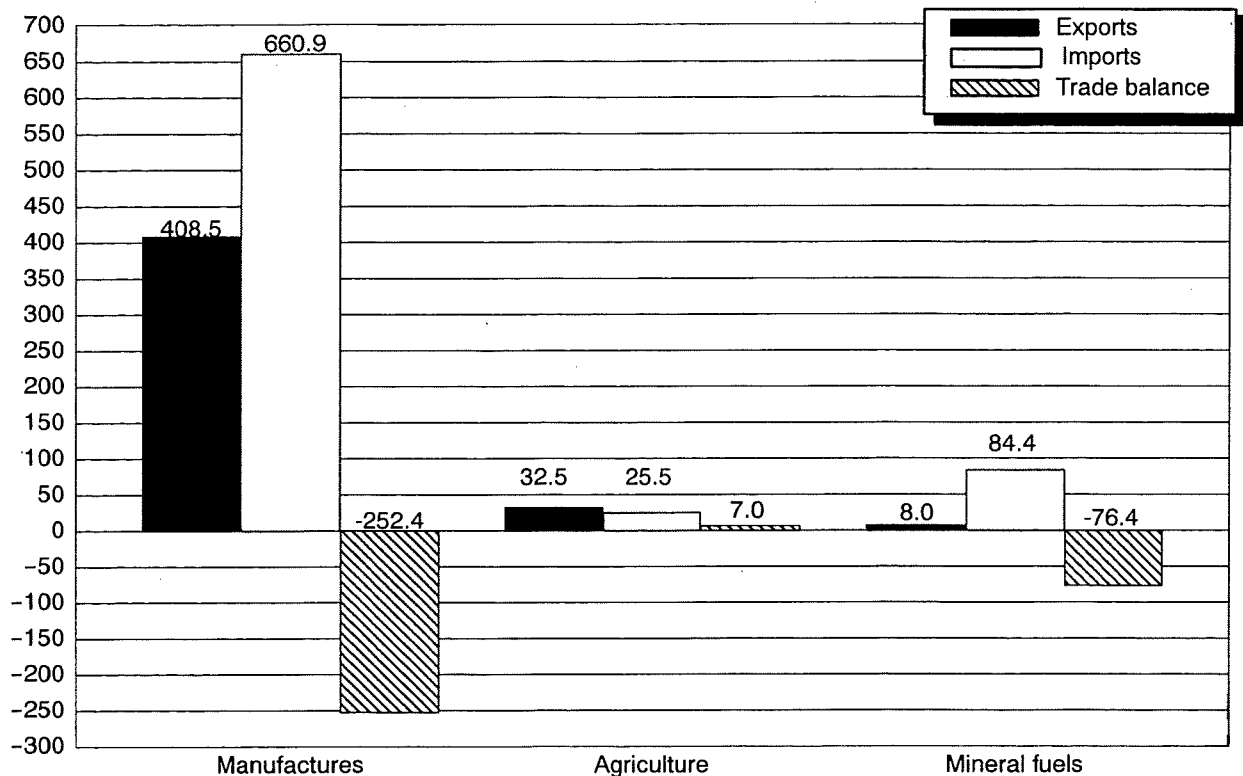
Table 2
Nominal U.S. exports and trade balances, of agriculture and specified manufacturing sectors, Jan.1999-Aug. 2000

	Exports		Change	Share	Trade balance	
	Aug. 2000	Jan.-Aug. 2000	Jan.-Aug. 2000 over Jan.-Aug. 1999	of total Jan.- Aug. 2000	Jan.-Aug. 2000	Jan.-Aug. 1999
	<i>Billion dollars</i>		<i>Percentage</i>		<i>Billion dollars</i>	
ADP equipment & office machinery	4.0	29.6	13.0	5.8	- 29.8	- 28.1
Airplanes	1.8	16.6	-23.5	3.3	9.4	16.0
Airplane parts	1.3	10.0	-3.9	1.9	6.3	6.3
Electrical machinery	8.4	57.6	19.3	11.3	- 12.2	- 7.7
General industrial machinery	2.9	21.7	10.2	4.3	-2.0	-1.3
Iron & steel mill products	0.5	3.8	18.8	0.7	-7.5	-5.5
Inorganic chemicals	0.5	3.5	16.7	0.7	-0.5	-0.4
Organic chemicals	1.5	11.8	22.9	2.3	-6.4	-4.6
Power-generating machinery	2.9	21.6	6.9	4.2	-1.0	0.2
Scientific instruments	2.7	19.6	18.1	3.8	5.5	5.3
Specialized industrial machinery	2.7	20.2	25.5	4.0	4.7	1.2
Televisions, VCRs, etc	2.5	18.0	16.1	3.5	-25.1	-14.9
Textile yarns, fabrics and articles	0.9	7.0	14.8	1.4	-3.3	-2.9
Vehicles	4.6	38.2	7.6	7.5	- 68.3	- 58.7
Manufactured exports not included above	17.0	129.4	13.2	25.4	-122.2	- 105.4
Total manufactures	54.2	408.5	11.5	80.1	- 252.4	-200.9
Agriculture	4.1	32.5	8.7	6.4	7.5	5.4
Other exports not included above	9.7	69.3	32.3	13.5	-35.7	-10.9
Total exports of goods	68.0	510.3	13.8	100.0	- 281.1	-206.4

Note.—Because of rounding, figures may not add to the totals shown. Data are presented on a Census basis.

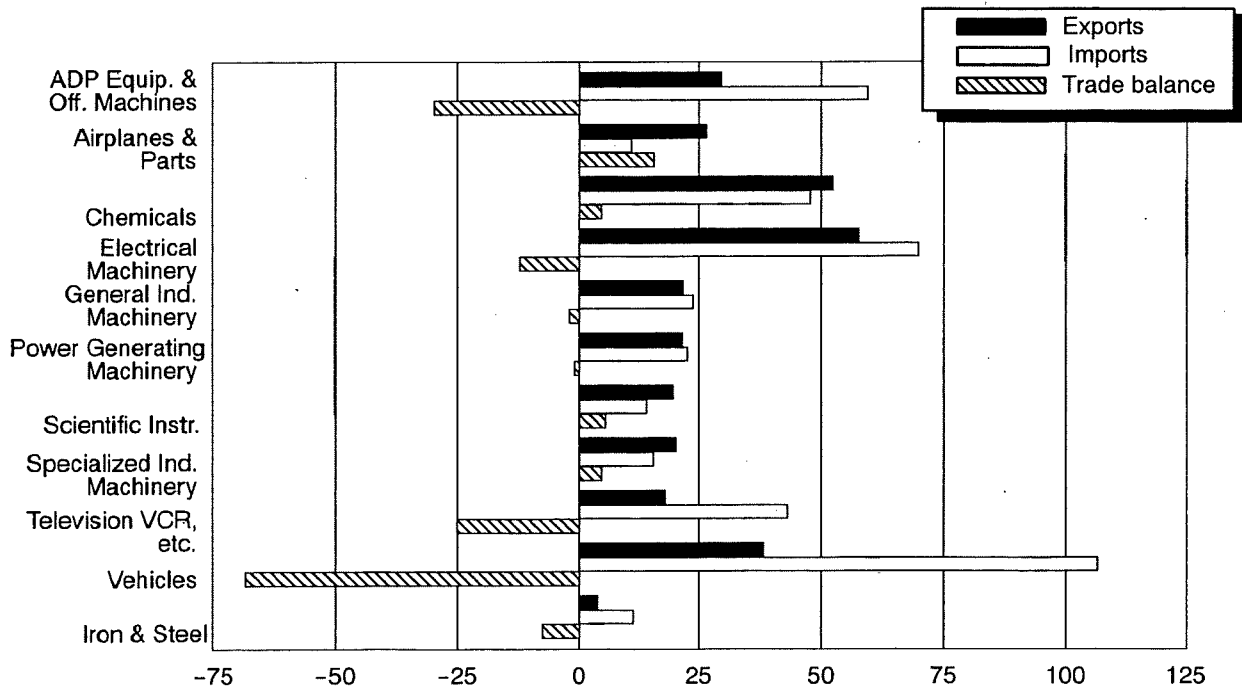
Source: U.S. Department of Commerce News (FT 900), Oct. 19,2000.

Figure 3
U.S. trade by major commodity, billion dollars, Jan.-August 2000



Source: U.S. Department of Commerce, FT 900 (00-07).

Figure 4
U.S. trade in principal goods, billion dollars, Jan.-August 2000



Source: U.S. Department of Commerce, FT 900 (00-07).

Table 3
Nominal U.S. exports and trade balances of services, by sectors, Jan.1999-Aug. 2000, seasonally adjusted

	<u>Exports</u>		<u>Change</u>	<u>Trade balances</u>	
	<u>Jan.- Aug. 2000</u>	<u>Jan.- Aug. 1999</u>	<u>2000 over Jan.- Aug. 1999</u>	<u>Jan. Aug. 2000</u>	<u>Jan.- Aug. 1999</u>
	<i>Billion dollars</i>		<i>Percent</i>	<i>Billion dollars</i>	
Travel	55.4	49.1	12.8	12.4	9.9
Passenger fares	13.6	13.1	3.8	-2.2	-1.0
Other transportation	19.6	17.7	10.7	-6.5	-4.2
Royalties and license fees	25.6	24.3	5.3	15.8	15.8
Other private sales	70.8	63.3	11.8	36.6	32.4
Transfers under U.S. military sales contracts	9.7	11.5	-15.7	0.8	2.4
U.S. Govt. miscellaneous service	0.6	0.6	0.0	-1.3	-1.3
Total	195.3	179.6	8.7	55.6	54.0

Note.—Services trade data are on a balance-of-payments (BOP) basis. Numbers may not add to totals because of seasonal adjustment and rounding.

Source: U.S. Department of Commerce News (FT 900), Oct. 19, 2000.

Advanced technology products exports rose to \$19.7 billion in August 2000 from \$18.1 billion in July. Imports increased to \$20.1 billion in August from \$18.5 billion in July, resulting in a deficit of \$0.4 billion in August virtually the same as the July deficit.

The August 2000 trade data showed U.S. surpluses with Australia, Argentina, Brazil, Egypt, and Hong Kong. Deficits were recorded with Canada, Mexico, Western Europe, China, Japan, Korea, Taiwan, Singapore, and OPEC member countries.

The January-August 2000 exports of goods and services increased to \$703.9 billion, up from \$624.7 billion in January-July 1999. However, imports of goods and services increased to \$939.4 billion, up from \$789.4 billion. The January-August deficit on goods and services increased to \$235.5 billion from \$164.7 billion in the same period of 1999, an increase of about 43.0 percent.

The January-August 2000 exports of goods increased to \$508.6 billion from \$445.2 billion in January-August 1999, but imports of goods rose to \$799.6 billion, up from \$663.9 billion in January-August 1999. The January-August trade deficit on goods rose

to \$291.0 billion from \$218.8 billion, a 33-percent increase from the same period in 1999. As for services, exports in January-August 2000 increased to \$195.3 billion up from \$179.6 billion in the same period of 1999. Imports of services rose to \$139.9 billion up from \$125.5 billion. The January-August surplus on services trade increased to \$55.5 billion from \$54.1 billion in the same period of 1999.

The January-August 2000 exports of advanced technology products rose to \$146.0 billion, up from \$129.1 billion in January-August 1999. Imports rose to \$139.8 billion from \$114.4 billion. The trade surplus decreased to \$6.2 billion from \$14.7 billion in the same period of 1999.

The January-August 2000 trade data in goods and services showed trade deficits with Canada, Mexico, Western Europe, the Euro-11 area, the European Union, EFTA, Eastern Europe, China, Japan, Korea, Singapore, Taiwan and OPEC. Trade surpluses were recorded with Belgium, the Netherlands, Spain, Australia, Argentina, Brazil, Hong Kong, and Egypt. U.S. trade developments with major trading partners are highlighted in table 4.

Table 4
U.S. exports and imports of goods with major trading partners, Jan. 1999-Aug. 2000

(Billion dollars)

Country/areas	Exports			Imports			Trade balances	
	Aug. 2000	Jan.-Aug. 2000	Aug. 1999	Aug. 2000	Jan.-Aug. 2000	Jan.-Aug. 1999	Jan.-Aug. 2000	Jan.-Aug. 1999
Total	68.0	510.3	448.6	107.6	791.4	655.0	-281.1	-206.4
North America	25.5	192.3	162.3	31.9	239.6	198.8	-47.4	-36.6
Canada	15.1	119.6	108.4	19.6	150.9	128.4	-31.4	-20.1
Mexico	10.4	72.7	53.9	12.3	88.7	70.4	-16.0	-16.5
Western Europe	14.7	117.3	108.3	19.9	157.4	137.6	-40.1	-29.3
Euro Area	9.6	74.6	69.3	13.7	106.5	93.8	-31.9	-24.5
European Union (EU-15)	13.5	106.1	99.9	18.2	143.6	126.5	-37.5	-26.5
France	1.7	12.9	12.5	2.3	19.1	16.8	-6.2	-4.4
Germany	2.4	19.1	17.7	5.1	38.9	35.8	-19.8	-18.1
Italy	0.9	6.8	6.5	2.2	16.5	14.8	-9.6	-8.4
Netherlands	1.9	14.0	12.6	0.8	6.4	5.2	7.6	7.3
United Kingdom	3.3	26.7	25.9	3.7	28.7	25.3	-2.0	0.6
Other EU	0.9	7.7	7.2	1.9	13.4	10.1	-5.7	-2.9
EFTA ¹	0.8	7.9	5.7	1.3	11.0	8.9	-3.1	-3.3
FSR/Eastern Europe	0.5	3.9	3.5	1.4	10.5	7.5	-6.6	-3.9
Russia	0.2	1.6	1.0	0.7	5.2	3.8	-3.6	-2.9
Pacific Rim Countries	18.3	132.7	112.1	38.5	269.5	228.9	-136.9	-116.8
Australia	1.1	8.4	7.2	0.6	4.2	3.4	4.2	3.8
China	1.5	10.4	8.6	10.1	52.7	51.2	-52.4	-42.6
Japan	5.7	42.4	37.5	12.5	96.4	83.7	-54.0	-46.2
NICs ²	7.7	55.6	45.7	10.3	71.8	60.6	-16.2	-14.9
Latin America	5.3	38.2	36.2	6.5	48.3	36.9	-10.0	0.7
Argentina	0.4	3.1	3.1	0.3	2.0	1.7	1.1	1.4
Brazil	1.4	9.7	8.5	1.4	9.4	7.3	0.2	1.2
OPEC	1.8	12.0	12.8	6.2	43.2	25.1	-31.2	-12.3
Other Countries	2.6	19.3	18.5	5.9	42.3	33.0	-23.0	-14.6
Egypt	0.3	2.3	2.0	0.1	0.6	0.4	1.7	1.6
South Africa	0.2	1.9	1.7	0.3	2.7	2.0	-0.9	-0.4
Other	2.1	15.1	14.8	5.5	39.0	30.6	-23.9	-15.8

¹ EFTA includes Iceland, Liechtenstein, Norway, and Switzerland.

² The newly industrializing countries (NICs) include Hong Kong, the Republic of Korea, Singapore, and Taiwan. FSR = Former Soviet Republics.

Note.—Country/area figures may not add to the totals shown because of rounding. Exports of certain grains, oilseeds, and satellites are excluded from country/area exports but included in total export table. Also some countries are included in more than one area. Data are presented on a Census Bureau basis.

Source: U.S. Department of Commerce News (FT 900), Oct.19, 2000

PRODUCTIVITY AND COSTS

Third Quarter 2000

The Bureau of Labor Statistics of the U.S. Department of Labor (USDL 00-319) reported preliminary productivity data—as measured by output per hour of all persons—for the third quarter of 2000. The preliminary seasonally-adjusted annual rates of productivity growth in the third quarter were 3.2 percent in the business sector and 3.8 percent in the non-farm business sector.

In both the business and the non-farm business sectors, productivity increases in the third quarter were smaller than the 6.9-percent and 6.1-percent increases recorded in the second quarter of 2000.

In manufacturing, productivity increases in the third quarter were 6.4 percent in manufacturing, 9.6 percent in durable goods manufacturing, and 2.0 percent in nondurable goods manufacturing.

The increase in manufacturing productivity was higher than the 5.7-percent rise reported for the previous quarter. Output and hours in manufacturing, which includes about 17 percent of U.S. business sector employment, tend to vary more from quarter to quarter than data for the more aggregate business and non-farm business sectors. Third-quarter measures are summarized in table 5.

These productivity measures describe the relationship between real output and the labor time involved in

its production. They show the changes from period to period in the amount of goods and services produced per hour. Although these measures relate output to hours at work of all persons engaged in a sector, they do not measure the specific contribution of labor, capital, or any other factor of production. Rather, they reflect the joint effects of many influences, including changes in technology; capital investment; level of output; utilization of capacity, energy, and materials; the organization of production; managerial skill; and the characteristics and effort of the work force.

The U.S. Department of Labor emphasized that the data sources and methods used in the preparation of the manufacturing series differ from those used in preparing the business and non-farm business series, and these measures are not directly comparable. Output measures for business and non-farm business are based on measures of gross domestic product prepared by the Bureau of Economic Analysis of the U.S. Department of Commerce whereas quarterly output measures for manufacturing reflect indexes of industrial production independently prepared by the Board of Governors of the Federal Reserve System.

Business

From the second quarter to the third quarter of 2000, business sector productivity increased at a 3.2 percent annual rate. Output rose 3.0 percent, while hours of all persons engaged in the sector declined 0.2 percent (seasonally adjusted annual rates). Second-quarter productivity in the business sector rose 6.9 percent, reflecting a 6.3-percent increase in output and a drop of 0.6 percent in hours.

Table 5
Productivity and costs: Preliminary third-quarter 2000 measures (Seasonally adjusted annual rates)

Sector	Productivity	Output	Hours	Hourly compensation	Real hourly compensation	Unit labor cost
<i>Percent change from preceding quarter</i>						
Business	3.2	3.0	-0.2	5.8	2.7	2.5
Non-farm business	3.8	3.0	-0.8	6.4	3.2	2.5
Manufacturing	6.4	3.1	-3.0	6.7	3.5	0.3
Durable	9.6	6.0	-3.3	5.9	2.8	-3.4
Nondurable	2.0	-0.6	-2.6	8.1	4.9	5.9
<i>Percent change from same quarter a year ago</i>						
Business	4.8	6.1	1.2	5.0	1.5	0.2
Non-farm business	5.0	6.1	1.1	5.1	1.6	0.1
Manufacturing	7.5	6.3	-1.2	5.0	1.5	-2.4
Durable	10.9	9.9	-0.9	4.8	1.3	-5.5
Nondurable	3.2	1.5	-1.6	5.3	1.8	2.0

Source: U.S. Department of Labor.

Hourly compensation in the business sector increased at an annual rate of 5.8 percent during the third quarter of 2000, after increasing 7.0 percent during the second quarter. This measure includes wages and salaries, supplements, employer contributions to employee benefit plans, and taxes. Real hourly compensation, (which takes into account changes in consumer prices), increased by 2.7 percent in the third quarter, after rising 3.2 percent in the second quarter of 2000.

Unit labor costs, which reflect changes in both hourly compensation and productivity, increased at a 2.5 percent annual rate during the third quarter. During the previous quarter, these costs were unchanged. The implicit price deflator for the business sector increased by 1.7 percent in the third quarter and by 2.4 percent in the second quarter.

Non-farm business

Productivity rose 3.8 percent in the non-farm business sector during the third quarter of 2000.

The increase in labor productivity in the third quarter occurred as output rose by 3.0 percent and hours of all persons fell by 0.8 percent. This decline in hours was the largest since the first quarter of 1992, when hours fell by 2.3 percent. In the second quarter, productivity had risen by 6.1 percent, as output grew by 6.5 percent and hours increased by 0.4 percent.

Hourly compensation increased at a 6.4-percent annual rate in the third quarter of 2000. This was the largest increase in this measure since the first quarter of 1992, when it increased by 8.8 percent.

Real hourly compensation rose at a 3.2-percent annual rate in the third quarter. During the second quarter of 2000, real hourly compensation had risen 2.2 percent.

Unit labor costs increased 2.5 percent during the third quarter of 2000 following a decline of 0.2 percent in the second quarter. The implicit price deflator for non-farm business output rose 1.8 percent in the third quarter of 2000.

Manufacturing

Productivity increased by 6.4 percent in manufacturing in the third quarter of 2000, as output grew 3.1

percent and hours of all persons dropped 3.0 percent (seasonally adjusted annual rates). In the second quarter labor productivity increased by 5.7 percent, reflecting increases in output and hours of 7.7 and 1.9 percent, respectively. In durable goods, productivity rose by 9.6 percent in the third quarter, as output increased by 6.0 percent and hours of all persons fell by 3.3 percent.

Productivity grew more slowly in nondurable goods, 2.0 percent, as hours fell faster than output. Output dropped by 0.6 percent, and hours of all persons decreased by 2.6 percent. Hourly compensation of manufacturing workers increased by an average of 6.7 percent during the third quarter, a more rapid rise than the 4.0-percent increase recorded in the second quarter (seasonally adjusted annual rates). In the third quarter, hourly compensation grew by 5.9 percent in durable goods and by 8.1 percent in nondurable goods. Real hourly compensation in total manufacturing rose by 3.5 percent in the third quarter.

Unit labor costs of manufacturing workers increased by 0.3 percent in the third quarter of 2000 after falling by 1.6 percent in the second quarter of 2000. In the durable goods sector, unit labor costs in the third quarter fell by 3.4 percent; these costs also had fallen in the previous three quarters. In contrast, unit labor costs in the nondurable goods sector rose by 5.9 percent in the third quarter, following a 5.4-percent rise in the second quarter.

Durables include the following 2-digit SIC industries: Primary metal industries; fabricated metal products; non-electrical machinery; industrial and commercial machinery and computer equipment; electronic and other electrical equipment; transportation equipment; instruments; lumber and lumber products; furniture and fixtures; stone, clay, and glass and concrete products; and miscellaneous manufactures. Non-durables include: Food and kindred products, tobacco products, textile mill products, apparel products, paper and allied products, printing and publishing, chemicals and chemical products, petroleum refining and related industries, rubber and plastic products, and leather and leather products.

INTERNATIONAL ECONOMIC COMPARISONS

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U.S. Economic Performance Relative to Other Group of Seven (G-7) Members

Economic growth

U.S. real GDP—the output of goods and services produced in the United States measured in 1996 prices—grew at an annual rate of 2.7 percent in the third quarter of 2000, following a 5.6-percent growth rate in the second quarter, according to preliminary estimates by the U.S. Department of Commerce (Commerce News BEA 00-32). The deceleration in real GDP in the third quarter reflected a deceleration in inventory investment, a downturn in government spending, and a deceleration in nonresidential fixed investment that were partly offset by an acceleration in personal consumption expenditures. For the year 1999, real GDP grew by 4.2 percent.

The annualized rate of real GDP growth in the second quarter of 2000 was 3.2 percent in the United Kingdom, 5.3 percent in Canada, 3.3 percent in France, 3.1 percent in Germany, 2.6 percent in Italy, and 0.8 percent in Japan. The annualized rate of real GDP growth in the second quarter was 3.8 percent in Euro-11.

Industrial production

The Federal Reserve Board (Federal Reserve Statistical Release -G.17 (419)) reported that U.S. industrial production increased 0.2 percent in September 2000 and following an increase of 0.4 percent in August. Manufacturing output inched up by 0.3 percent in August. The output of consumer goods increased by 0.8 percent in September after having edged up by

0.1 percent in August. The production of durable consumer goods increased by 1.6 percent after two months of declines. The production of autos and light trucks rose by 1.1 percent in September. Auto parts and allied goods jumped by 2.1 percent in September, in large part because of strong gains in the production of replacement tires. Mining output declined by 1.0 percent in September but utilities output increased by 0.7 percent. Total industrial production in September 2000 was 5.7 percent higher than in September 1999. Overall industrial capacity utilization was 3.7 percent higher in September 2000 than in September 1999.

For the third quarter as a whole, total industrial production index increased at an annual rate of 2.8 percent, the slowest quarterly rate since the first quarter of 1999.

Other Group of Seven (G-7) member countries reported the following growth rates of industrial production. For the year ended August 2000, Japan reported an increase of 8.3 percent. For the year ended July 2000, the United Kingdom reported an increase of 1.1 percent, Canada reported an increase of 5.7 percent, Germany reported an increase of 5.5 percent, but Italy reported a decrease of 0.1 percent. For the year ended June 2000, France reported an increase of 4.1 percent. The Euro-11 reported an increase of 3.8 percent for the year ended June 2000.

Prices

The seasonally adjusted U.S. Consumer Price Index (CPI) increased by 0.2 percent in October, following an increase of 0.5 percent in September according to the U.S. Department of Labor (USDLE-00-299). The upturn reflects a sharp turnaround in the energy price index, which rose by 3.8 percent in September after declining by 2.9 percent in August. For the 12-month period ended September 2000, the CPI-U increased by 3.5 percent.

During the 1-year period ended September 2000, prices increased by 2.4 percent in Germany and by 2.6 percent in Italy. During the 1-year period ended August 2000, prices increased by 2.5 percent in Canada, by 3.0 percent in the United Kingdom, by 1.8 percent in France.

¹ The views and conclusions expressed in this article are those of the author. They are not the views of the U.S. International Trade Commission as a whole or of any individual Commissioner.

During the 1-year period ended August 2000 prices declined by 0.8 percent in Japan. Prices increased by 2.3 percent in the Euro-11 in the year ended August 2000.

Employment

The Bureau of Labor Statistics (USDL 00-320) reported that the unemployment rate held at 3.9 percent in October 2000. The jobless rate has been in the 3.9-

to 4.1 percent range since October 1999. Employment was unchanged in manufacturing, but rose in construction and little changed in the services industry.

In other G-7 countries, their latest unemployment rates were: 7.1 percent in Canada, 9.0 percent in Germany, 5.3 percent in the United Kingdom, 9.6 percent in France, 10.5 percent in Italy, and 4.6 percent in Japan. The unemployment rate in the Euro-11 was 9.0 percent.

Forecasts

Seven major U.S. forecasters expect real GDP growth in the United States to average about 3.0 percent (at an annual rate) in the third quarter of 2000, and to increase to 3.6 percent in the fourth quarter. The average growth rate for the year 2000 would reach 5.3 percent. Table 6 shows macroeconomic projections for the U.S. economy from July 2000 to June 2001, and the simple average of these forecasts. Forecasts of all 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.

The average of the forecasts points to an unemployment rate of 4.1 percent in the third and fourth quarters of 2000. Inflation (as measured by the GDP deflator) is expected to remain subdued to about 1.7 percent in the third quarter and rise slightly in the fourth quarters reaching an annual average rate of 2.1 percent.

Table 6
Projected changes in U.S. economic indicators, by quarters, July 2000-June 2001
(Percentage)

Period	Confer- ence Board	E.I. Dupont	UCLA Business Forecasting Project	Merrill Lynch Capital Markets	Macro Economic Advisers	Eaton Corp.	Regional Financial Associates	Mean of forecasts
<i>GDP constant dollars</i>								
2000:								
July-Sept.	4.2	2.3	2.8	3.0	2.7	3.0	3.2	3.0
Oct.-Dec.	6.6	1.4	2.9	3.7	3.6	3.7	3.4	3.6
2001:								
Jan.-March	5.9	1.8	2.6	3.7	3.5	3.7	3.5	3.5
April-June	2.1	3.2	2.9	3.8	3.5	3.8	3.2	3.2
Annual 2000	5.6	5.0	5.1	5.3	5.2	5.3	5.3	5.3
<i>GDP Price Deflator</i>								
2000:								
July-Sept.	1.1	2.3	0.8	1.5	1.9	1.5	2.6	1.7
Oct.-Dec.	2.3	2.3	1.7	1.4	2.3	1.4	2.6	2.0
2001:								
Jan.-March	2.6	2.2	1.7	1.6	2.2	1.6	2.6	2.1
April-June	3.0	2.2	1.9	1.3	2.6	1.3	2.2	2.1
Annual 2000	2.1	2.2	2.0	2.1	2.1	2.1	2.3	2.1
<i>Unemployment average rate</i>								
2000:								
July- Sept.	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
Oct.-Dec.	3.9	4.2	4.3	4.1	4.1	4.1	4.0	4.1
2001								
Jan.-March	4.0	4.3	4.4	4.1	3.9	4.1	4.1	4.1
April-June	3.9	4.3	4.5	4.1	3.9	4.1	4.3	4.2
Annual 2000	4.0	4.1	4.1	4.1	4.1	4.1	4.0	4.1

Note.—Except for the unemployment rate, percentage changes in the forecast represent annualized rates of change from preceding period. Quarterly data are seasonally adjusted. Forecast date, Sep. 2000.

Source: Compiled from data of the Conference Board. Used with permission.

STATISTICAL TABLES

Unemployment rates (civilian labor force basis)¹ in G-7 countries, by specified periods, 1998-Sep. 2000

Country	1999					2000						
	1998	IQ	IIQ	IIIQ	IVQ	IQ	IIQ	June	July	Aug.	Sep.	Oct.
United States	4.5	4.3	4.3	4.2	4.1	4.1	4.0	4.0	4.0	4.1	3.9	
Japan	4.1	4.7	4.8	4.8	4.7	4.9	4.8	4.7	4.7	4.6	4.6	
Canada	8.3	7.9	7.8	7.6	7.0	6.8	6.7	6.6	6.8	7.1	6.8	
Germany	9.4	9.0	9.0	9.1	9.0	8.4	8.4	8.3	8.3	8.3	8.2	
United Kingdom	6.3	6.3	6.1	5.9	5.9	5.8	5.5	5.4	5.4	5.4	5.3	
France	11.7	11.3	11.2	11.0	10.6	10.2	9.8	9.6	9.7	9.7	9.7	
Italy	12.3	12.3	12.1	12.1	12.1	11.2	10.8	10.6	10.6	10.6	10.6	

¹ Seasonally adjusted; rates of foreign countries adjusted to be comparable with the U.S. rate.

Source: *Unemployment Rates in Nine Countries*, U.S. Department of Labor, Nov.3, 2000

Consumer prices of G-7 countries, by specified periods, 1998-Sep. 2000

(Percentage change from same period of previous year)

Country	1998				1999				2000						
	IQ	IIQ	IIIQ	IVQ	IQ	IIQ	IIIQ	IVQ	IQ	IIQ	June	July	Aug.	Sep.	Oct.
United States	1.5	1.6	1.6	1.5	1.7	2.1	2.3	2.6	3.2	3.2	3.7	3.5	3.4	3.5	
Japan	2.0	0.3	-0.2	0.5	-0.1	-0.3	-0.0	-1.0	-0.7	-0.7	-0.7	-0.5	-0.8	-0.8	
Canada	1.0	1.0	0.9	1.1	2.6	2.3	2.2	2.6	2.7	2.4	2.9	3.0	2.5	2.7	
Germany	1.2	1.4	0.7	0.4	0.7	0.8	1.0	1.2	1.8	1.6	1.9	1.9	1.8	2.5	
United Kingdom	3.4	4.0	3.3	3.0	1.1	1.2	1.4	1.8	2.3	3.1	3.3	3.3	3.0	3.3	
France	0.7	1.0	0.7	0.4	0.7	0.8	0.9	1.3	1.5	1.5	1.7	1.7	1.8	2.2	
Italy	2.0	2.0	2.0	1.7	1.8	2.1	2.1	2.1	2.4	2.5	2.7	2.6	2.6	2.7	

Source: U.S. Department of Labor, Nov.3, 2000.

U.S. trade balances by major commodity categories and by specified periods, 1998-Aug. 2000
(In billions of dollars)

Commodity categories	2000										
	1998	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May.	June	July	Aug.
Agriculture	14.9	1.4	1.0	1.0	1.2	1.0	0.5	0.5	0.8	0.9	1.1
Petroleum and selected products (unadjusted)	-43.4	-6.5	-6.0	-7.1	-9.0	-9.6	-8.6	-8.5	-10.0	-10.7	-10.6
Manufactured goods	-241.1	-31.1	-25.5	-27.9	-27.8	-31.6	-28.7	-32.9	-31.4	-36.4	-35.8
Unit value of U.S. imports of petroleum and selected products (unadjusted)	\$10.81	\$20.9	\$20.90	\$23.18	\$23.18	\$25.01	\$24.42	\$24.16	\$26.65	\$27.76	26.59

¹ Exports, f.a.s. value, unadjusted. Imports, customs value, unadjusted.

Source: *Advance Report on U.S. Merchandise Trade*, U.S. Department of Commerce, FT900 (00-07), Oct.19, 2000.

WORKING PAPERS

The following is a list of recent Office of Economics working papers. Copies of papers can be downloaded from the Commission's Internet web site, <http://www.usitc.gov> (use the search option at the top of the Reports and Publications page), or may be obtained from the Office of Economics. Please request working papers by reference code, title, and author. All requests to the Office of Economics, U.S. International Trade Commission, 500 E Street, SW, Washington, DC 20436, USA, or by fax at (202) 205-2340.

Reference Code	Title	Author
2000		
00-01-A	Exchange Rates: Definitions and Applications	Gerry Benedick and Peter Pogany
1999		
99-11-B	Preferential Trading Arrangements: Endogenous Response of the Excluded Country	Soamiely Andriamananjara
99-11-A	Inventing Around and Impacts on Modes of Entry in Japan: A Cross-Country Analysis of U.S. Affiliate Sales and Licensing	Christine McDaniel
99-10-A	Modeling the Effects of Trade Liberalization on Forest Cover: Some Methodological Issues	Michael J. Ferrantino
99-09-A	Regionalism and Incentives for Multilateralism	Soamiely Andriamananjara
99-04-A	An Overview of Quasiconcavity and its Applications in Economics	Peter Pogany

