The Anatomy of Trade

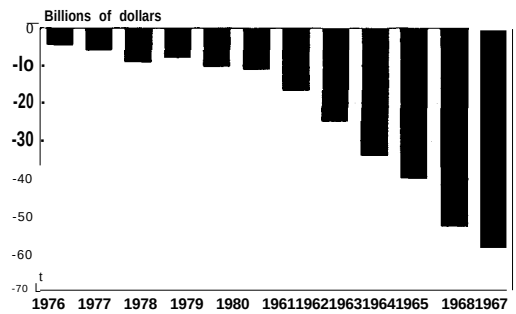
In thinking about different ways in which the United States might turn the trade deficit around, it is useful to consider first what U.S. trade consists of–what we trade, what are the biggest items in the deficit, who are our most important trading partners, and which of them run the biggest surpluses with the United States. These facts about the anatomy of trade as it is now point to the adjustments that will have to be made when U.S. trade comes back into balance.

Products

Manufactured goods account for most of the merchandise trade deficit. Among manufactured goods, by far the most important deficit item is motor vehicles, parts and engines. The deficit in automotive imports alone was over $53 billion in 1987, having risen more than tenfold since 1976 (figure 26); it now amounts to about one-third of the entire deficit in merchandise trade. When U.S. trade deficits fall, it is clear that much of the reduction must be in automotive products — either through importing less or exporting more or both.

Other industrial sectors are also running sizable deficits, and also face pressures for adjustment (table 12). Of course, it is not necessary to reach a balance in every industry; some with surpluses can compensate for others that are in deficit. But the deficits are so great in a few industries that it is hard to see what others could generate high enough surpluses to offset these deficits. As table 12 shows, electronic equipment, including items ranging from semiconductors to television and radio sets, ran a $23 billion deficit in 1987, mitigated only slightly by a $1 billion surplus in computers and automatic data processing equipment. The textile and apparel industry complex hit an all-time high (or low) of $21 billion in deficit. The industry groups with the strongest trade performance were aircraft and other transportation equipment (excluding autos) with a surplus of over $12 billion, and chemicals, with a healthy and rising surplus of nearly $10 billion.

Figure 26
Balance Of Trade in Automotive Products, 1976-85



SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis, Business Statistics, 1986, p. 80-81, Foreign Trade of the U.S. - Value of Exports and Imports

It is noteworthy that the worsening trade balances in manufacturing have not spared high technology products.[111] Between 1985

[111] For international trade, the Department of Commerce defines high technology products as those embodying high levels of research and development expenditures per unit of output; the set of industries producing these goods is similar to the list based on the Bureau of Labor Statistics criteria. See U.S. Department of Commerce, International Trade Administration, United States Trade Performance in 198.S and Outlook (Washington, DC: U.S. Government Printing Office, 1986).

and 1987, for example, the positive trade balance in computers and automatic data processing machinery dropped by $2.8 billion, to about $1 billion (table 12). Overall, the trade balance in high technology products shrank from a surplus of $27 billion in 1980 to a surplus of only $600 million in 1987, having gone through a deficit of $2.6 billion in 1986. The improvement in 1987 was due mostly to rising surpluses in the aircraft and chemical industries.[112]

The record still illustrates something fundamental: high technology industries have come under many of the same pressures affecting other manufacturing industries.

Table 12.–Trade Balance In Selected Manufacturing Industries
(billions of **dollars)**

Industry	1985	1986	1987
Total manufacturing	**$101.6**	**$1289**	$137.7
Durable goods			
Wood and cork manufactures	**$1.4**	**$1.4**	-$1.6
Furniture and parts	**3.1**	**3 9**	-4.4
Nonmetallic mineral manufactures	**5.8**	**6 7**	-6,8
Iron and steel	**9.9**	**8 4**	-8.5
Nonferrous metals	**5.3**	**-6 3**	-6,0
Misc. metal manufactures*	**3.7**	**4 5**	4 9
Industrial machinery	**0.1**	**5 4**	-6,7
Power generating machinery	**0.4**	**0 5**	-0.6
Special industrial machinery	**2.2**	**0 2**	-1.6
Metalworking machinery	**1.6**	**1.9**	-1,4
Other industrial machinery	**0.9**	**2 8**	[illegible]
Electronic, computing, and office machinery	**15.3**	**208**	21.6
Office and ADP machinery	**3.8**	**14**	1.0
Telecomm and sound reproducing equip	**14.4**	**162**	156
Semiconductors and other electrical equip	**4.7**	**5 9**	-7 0
Motor vehicles	**39.8**	**516**	53.3
Aircraft and other transport equipment	**11.2**	**108**	12.5
Prof. , scientific and control inst	**3.4**	**3 0**	3,0
Photo equip , optical goods and timing equip	**2.4**	**2 9**	3.1
Misc. manufacturing**	**10.3**	**119**	12.8
Military arms, ammo, vehicles	**2.7**	**2.0**	2.0
Non durable goods			
Textiles and apparel	**153**	**17.6**	208
Yarns, fabrics and textile articles	**2 8**	**3 5**	-3 9
Wearing apparel and accessories	**124**	**141**	169
Footwear	**6 0**	**6 7**	7 4
Paper, paperboard and manufactures	**3 9**	**4 0**	-44
Chemicals	**6 7**	**7 2**	9 6
Organic chemicals and related products	**13**	**14**	1 9
Medicine and Pharmaceuticals	**16**	**19**	1.7
Fertilizers	**11**	**10**	1.4
Synthetic resins, rubbers and plastics	**2.1**	**2 4**	3.4
Other chemical materials and products	**0 6**	**0 6**	11
Tires and tire tubes	**17**	**18**	1 9
Luggage, handbags, and similar articles	**15**	**16**	2.0

* Not specified elsewhere
** Not specified

SOURCES: U S Department of Commerce, Mice of Trade and Investment Analysis, unpublished **data**

112Information provided by the U.S. Department of Commerce, Office of Trade and Investment Analysis,

Trade in high technology products is substantial, with imports and exports both reaching just over $80 billion in 1987; high tech imports were almost one fourth of all manufactured imports, and high tech exports were 42 percent of all manufactured exports. While American high tech companies are still quite competitive, it is unlikely that they can regain the kind of dominance they had just a decade ago, relative to producers in Europe, Japan, and a few developing Asian nations. It is therefore unlikely that hightech trade can generate a large enough surplus to offset substantial deficits in traditional sectors.

Countries

The United States trades mostly with other developed nations, although trade with several developing nations has expanded greatly in recent years. The top ten suppliers of U.S. imports in 1987, in descending order, were Japan, Canada, West Germany, Taiwan, Mexico, the United Kingdom, South Korea, Italy, France, and Hong Kong.[113] When the trade deficit is reduced, most of the adjustment will fall on these countries (figure 3). The impact of the adjustment will vary by nation and by region, depending on how important trade with the United States is to our trading partners. It will also depend on how fast the economies of other countries are growing; the more other markets expand, the easier will be the adjustment to reduced sales (or slower growth in sales) to the United States.

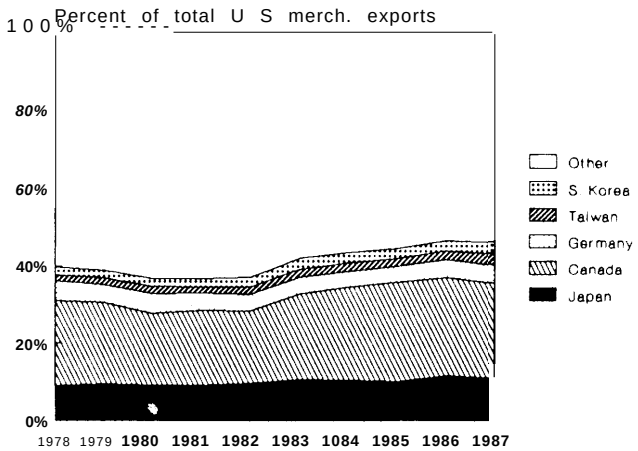
The developed nations that are our largest trading partners will probably have to bear most of the adjustment costs. Six of the top ten suppliers of U.S. imports are developed nations: Japan, Canada, West Germany, the United Kingdom, Italy, and France. Their merchandise trade surpluses with the United States totaled nearly $96 billion–about 60 percent of the U.S. merchandise trade deficit. Figures 27 and 28 show, in percentages, the part played in U.S. trade by our leading trading partners from 1950 to 1986.

Adjustment costs will mean different things to different nations. If American exports are to grow faster than imports, nations that export to the United States can maintain export levels only if worldwide economic growth, including U.S. growth, is substantially greater than it has been in recent years. Faster growth" in the American economy– the world's largest — is not likely, since we cannot continue to maintain consumption, investment, and government deficits at current levels indefinitely. Under these circumstances, it will be difficult for foreign producers to maintain their levels of exports to the United States, and many will find that they must replace U.S. customers with others or produce in the United States instead of in the home country. The alternative to these cutbacks would be rapid economic growth rates in the exporting countries, thus enabling them to substitute their own markets as well as others for the U.S. market. Except for Japan these countries have so far shown little evidence of being able or willing to do so.

113U.S. Department of Commerce, International Trade Administration, U.S. Merchandise Trade Position at Midyear 1987, (Washington, D. C.: U.S. Government Printing Office, October 1987).

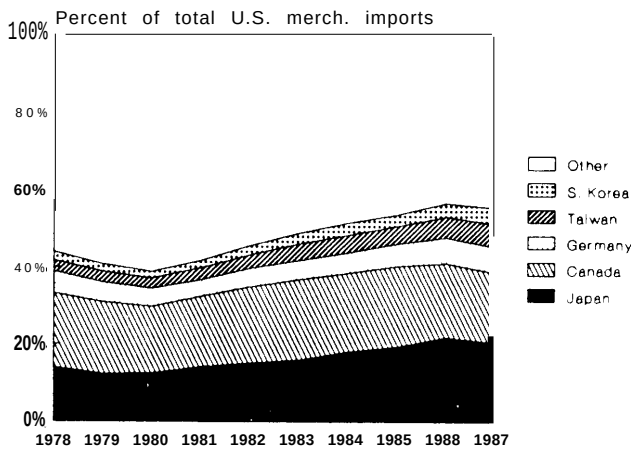
114Until 198S, however, investment by foreign countries in the United States had done nothing to improve the U.S. merchandise trade balance, in fact quite the contrary. This situation may already have begun to change with the falling dollar, but whether or how soon foreign direct investment in American producion replaces imports is uncertain..

Figure 27
Volume of U.S. Exports, 1978-86



SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis, Survey of Current Business, table 3, June 1987 and March 1988.

Figure 28
Volume of U.S. Imports, 1978-86



SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis, Survey of Current Business, table 3, June 1987 and March 1988,

The greatest bilateral merchandise deficit of the United States – $57 billion in 1987, or about 36 percent– is with Japan. Twenty-one percent of U.S. merchandise imports, or $85 billion, were from Japan, and about 11 percent of our exports ($28 billion) are sent there. The deficit with Japan has been one-third to one-half of the U.S. merchandise trade deficit for about the last decade, growing during that time approximately tenfold. In 1986, the leading import by far from Japan was passenger motor vehicles (table 13).[115] This item accounted for $23 billion, or over one-fourth of all imports from Japan, and nearly half the U.S. deficit in motor vehicle trade. Besides motor vehicles, other major imports from Japan include consumer electronics, telecommunications equipment, automatic data processing and office machinery, and electronic components.

Some adjustment has already taken place. For example, even before the fall of the dollar against the yen, beginning in early 1985, there were pressures on and within Japan to change its postwar policies of export-led development.[116] Many nations were exhorting Japan to reduce its trade surplus, and increasing saturation of some export markets was apparent. The Japanese government has announced an official policy of lesser reliance on exports. But shifting to an economy more dependent on growth of domestic consumption is not simple; export growth accounted for almost 40 percent of Japan's economic growth between 1980 and **1985.**[117] As exports slackened in 1986, Japanese GNP growth faltered somewhat, rising only 2.4 percent compared to 4 and 5 percent in the earlier 1980s. Capital-investment plans were revised downward.[118] Japanese firms and industries that were particularly hurt by stagnating demand, like the steel industry, began to diversify, entering high technology fields like special chemicals, new materials and biotechnology.[119] At the same time, there were layoffs, especially in the steel industry. Nippon Steel, for ex-

Table 13.-Major U.S. Imports From and Exports to Japan, 1986

	C i f value* (millions of dollars)	Compound annual growth rate 1982-86
Import category		
Passenger motor vehicles	$22.8	21 .2%
Phonographs, IV image & sound reproducing equipment .	6.0	371
Special purpose motor vehicles	51	316
Telecommunications equipment, nspf**	4.0	239
Parts of motor vehicles, nspf**	3.1	508
Automatic data processing machines	2.9	64.1
Export category		
Gold (nonmonetary, except ores)	3.3	695
Air and spacecraft, etc.	1.8	189
Corn or maize, unmilled	0.9	69
Oilseed and oleag. fruit .,	0.8	37
Wood (rough cut) ., .,	0.8	17
Meat (fresh, chilled, frozen)	0.7	97
ADP machines	0.7	169
Parts for office machines	0.7	131
Radioactive and assoc. material	0.6	88
Organic chemicals and products	06	39
Medicinal and pharmaceutical prod	O 6	66
Fish (fresh, chilled, frozen)	06	123
Measuring and checking instruments	O 6	74
Coal and lignite	06	408
Petroleum products (refined)	04	27

"C i f value of imports includes cost, insurance and freight
● *Not specified

SOURCE U S Department of Commerce, International Trade Administration, 1986 *U S foreign Trade Highlights, Office* of Trade and Investment Analysis, March 1987

115 Detailed figures on trade by product and by country were not yet available for 1987 when this report was written.

116 Jon Woronoff, "Japan's Structural Shift from Exports to Domestic Demand, "in Japan's Economy and Trade with the United States: selected Papers, Subcommittee on Economic Goals and Intergovernmental Policy of t he Joint Economic Committee. Congress of the United States (Washington, D. C.: U.S. Government Printing Office, December 1985).

117 Robert J. Samuelson, "Japan's Case of Malaise, ''Newsweek, May 4, 1987.

118 No Big Deal,' The Economist, November 8, 1986.

119 Japan: Steelmaker are Vigorously Restructuring, ''Foreign Broadcast Information Service, 2.5 February 1987.

ample, announced a temporary layoff of 3,000 of its workers in October 1986.[120]

After this rather rough year, the Japanese economy bounded back in 1987, with a GNP growth rate of 4.2 percent. The revival was fueled by a housing boom, an increase in consumer spending (spurred by a tax cut), and a $46 billion government spending package, including a 20 percent increase in the public works budget. A tax deduction on mortgage loans and a cut in interest rates encouraged the housing boom; housing starts rose over 18 percent in the first half of 1987.[121] The construction activity spilled over into greater demand for steel, which staged a substantial recovery, and a whole range of consumer and household goods.[122] Whether domestic demand will continue to rise at the 1987 rate, compensating for slowing or declining external demand and a shrinking trade surplus, is yet to be seen. The Japanese economy has proven extraordinarily resilient in difficult circumstances before, notably after the oil shock of the early 1970s. And Japanese manufacturers are responding to the high yen by paring profit margins and redoubling efforts to raise productivity.[123] At the same time, Japanese companies are beginning to move some manufacturing operations offshore, in response to the high yen, and these moves are bound to have some dislocating effects on employment and the economy. The adjustment to a higher yen is not yet over.

While the coming changes are not simple and easy for Japan, they could be harder for some of our other trading partners. Among developed nations, Canada and the United Kingdom – our second and fifth largest suppliers of imports, respectively–are in the most difficult positions; both countries run trade surpluses with the United States, but sustain overall trade deficits and relatively shaky economies. Canada, whose economy is heavily dependent on the American market, may face great difficulty — even if the newly established free trade agreement is effective in further liberalizing trade between the two countries.

Between 1976 and 1987, the U.S. merchandise trade deficit with Canada increased from $316 million to $11.9 billion. The 1982 recession and the rise in the value of the dollar were clearly the major factors accounting for the change in trade deficits with Canada. Canada's share of the U.S. merchandise trade deficit rose from its normal 5 or 10 percent to 25 percent in 1982. In absolute terms, the U.S. merchandise trade deficit with Canada increased over 4000 percent, peaking at $15 billion in 1985. The leading import from Canada in 1986 was passenger motor vehicles ($11.9 billion). Canada's top five exports to the U.S. consist of motor vehicles and parts and wood products (table 14).

It could be very costly to Canada to reduce exports to the United States. Nearly four-fifths of Canada's manufactured products are sent here.[124] Finding other markets to

120 Japanese Steelmaker, Blasted,'The Economist, January 3, 1987.
121 "A Shopping Spree Starts Turning Japan Around, ''Business Week, August 17, 1987, p. 50.
122 Charles Smith, "Under Its Own Steam, ''Far Eastern Economic Review, Feb. 4, 1988.
123 See, for example, John Burgess and Fred Hiatt, "Toyota Finds Ways to Hold Down Prices,' The Washington Post, Feb. 16, 1988,
124 Marc Levinson, "More Bucks Out of the Maple Leaf?" Dun's Business Month, July 1986, p. 45.

replace lost opportunities will be difficult, particularly if other U.S. trade partners are trying to do the same thing. Past Canadian efforts to diversify exports, and reduce the heavy reliance on the United States, have failed.[125] Moreover, Canada has begun to run current account deficits: about $7 billion in 1987 down from a surplus of $2 billion in 1984.[126] If exports to the United States are curtailed, Canada's trade deficit could increase, putting further downward pressure on an already low Canadian dollar and on Canadian living standards. Canadian unemployment has been higher than that of the United States and many other industrialised countries in the 1980s, though it had declined to 7.8 percent in early 1988. This compares to the current rate of 5.6 percent in the United States, 2.7 percent in Japan, and historical rates in Canada of 3 to 6 percent in the 1960s and early 1970s.[127]

In another break with the past, the United States is running large deficits with Western European countries. Our merchandise trade with Western Europe fell from a surplus of $20 billion in 1980 to a deficit of $27 billion in 1987. Over one-half of the European deficit – $15.3 billion – was with West Germany; Italy accounted for $5.5 billion, or 20 percent, and the United Kingdom for $3.4 billion. Again, as with Japan and Canada, the largest import item from Western Europe is passenger motor vehicles –$11.7 billion in 1986–with West Germany the major supplier. Motor vehicle imports dwarf the next most important European import, organic chemicals (table 15).

The cost of adjustments will vary among European countries. Unemployment is high in France, the United Kingdom, West Germany and Italy, relative to historical standards. The worst off is France with an unemployment rate of nearly 11 percent in early 1988. The United Kingdom is recovering from a prolonged bout of unemployment at around 12 percent; the rate is currently 9 percent and declining. West Germany's unemployment rate, over 7 percent, is lower, but high by historical standards; the rate throughout most of the 1960s and early 1970s

Table 14.--Major **U.S. Imports From and Exports to Canada, 1986**

	C.i.f. value* (millions of dollars)	Compound annual growth rate 1982-86
Import category		
Passenger motor vehicles	$11.9	19.4%
Parts of motor vehicles, nspf**	4.9	21.3
Paper and paperboard (not cut)	4 5	8.1
Wood (shaped or simply worked	3.1	16.2
Special purpose motor vehicles	3.1	4.5
Crude petroleum	2 9	7,2
Gas (natural and manufactured)	2.5	-15.1
Gold (nonmonetary, except ores)	2.4	21.5
Export category		
Parts of r&d vehicles and tractors	63	7.6
Passenger motor vehicles	5.9	25.2
General merchandise, low-value	3.2	41.4
Internal combustion & piston engines	1.8	3.0
Trucks & special purpose motors	1.7	4 1 6
Parts for office and ADP machines	1.2	17.1
Gold (nonmonetary, except ores)	1.1	14.2
Coal and lignite	0.7	-8.2

• C. i. f value of imports includes cost, insurance and freight
**Not Specified

SOURCE: U S Department of Commerce, International Trade Administration, Office of Trade and Investment Analysis, 1986 U.S. Foreign *Trade Highlights*, Much 1987

125Alan M. Rugman, "U.S. Protectionism and Canadian Trade Policy, ''Journal of World Trade Law, July-August, 1986.
126Organization for Economic Co-Operation and Development, OECD Economic Outlook, (Paris: OECD Publications, May 1986 and June 1987)p. 58.
127U.S. Department of Labor, Bureau of Labor Statistics.

was less than 1 percent. In Italy the current unemployment rate of about 7 percent, is more than double the levels of the 1960s and 1970s. In terms of trade balance, Germany's merchandise trade surplus —exceeding $20 billion in the mid-1980s–puts that country in better shape to handle a diminishing American export market than Italy or the United Kingdom, both of which were in deficit in 1983.[128] These deficits were small: $1.7 billion for Italy, and $0.8 for the United Kingdom. Nonetheless, since both countries ran substantial merchandise trade surpluses with the United States, any loss of U.S. markets would almost certainly mean deeper deficits, and downward pressure on living standards and currency values.

Table 15.– Major U.S. Imports From and Exports to Western Europe, 1986

	C.i.f. value* (millions of dollars)	Compound annual growth rate 1982-86
Import category		
Passenger motor vehicles	$11.7	23.7%
Organic and related chemicals	2.8	12.0
Beverages, alcoholic	2.7	5.1
Air and spacecraft, etc.	2.6	17.4
Crude petroleum	2.3	-23.7
Motor vehicle parts, nspf**	2.2	23,2
Special transactions, nspf**	2.2	7.1
Gold (nonmonetary except ores)	2,2	90.0
Petroleum products	21	9.0
Specialized industrial machinery	1.9	24.9
Export category		
Air and spacecraft, etc.	5.1	12.7
Office and ADP machine parts	4.0	14,2
ADP machines	4.0	8 9
Measuring and checking instruments	2.3	2.6
Internal combustion engines	2.2	8.9
Oilseed and oleag. fruit	2.2	-14.5
Coal and lignite	1.8	-10,0

• C.i.f value of imports includes cost, insurance and freight
• *Not specified

SOURCE: U S Department of Commerce, International Trade Administration, Office of Trade and Investment Analysis, 1986 U.S. Foreign *Trade Highlights*, March 1987

Certain developing nations are important suppliers of imports to the United States and major factors in the U.S. merchandise trade deficit. Those facing the largest adjustment costs are the East Asian newly industrializing countries (NICs) — Taiwan, South Korea, Hong Kong, and Singapore –and two Latin American NICs, Mexico and Brazil. Like the developed nations, different developing countries vary in their abilities to cope with the adjustments.

About one-quarter of the U.S. merchandise trade deficit in 1987–$47.2 billion– was with Asian countries, excluding Japan; the four East Asian NICs accounted for three-quarters of this. The deficit with Taiwan was much the largest: $17.4 billion, compared with $9.4 billion with the Republic of Korea, $5.6 billion with Hong Kong, and **$2.1** billion with Singapore. Table 16 lists the most important imports from and exports to the Asian NICs in 1986. If all the separate categories of apparel and footwear are aggregated, this is by far the largest category of imports, amounting to at least $14 billion.[129] Apparel and footwear top the list of imports from three of the Asian NICs (Hong Kong,

128 U.S. Department of Commerce, International Trade Administration, International Economic Indicators, op. cit.

129 Trade data are published in ways that make it difficult to sum up large categories of imports, such as apparel, so this estimate is only approximate. Eight of the 35 leading imports from the East Asian NICs in 1986 were apparel and footwear; they added up to $13.8 billion. It is likely that more articles of apparel were imported, but were not among the leading 35. In addition, detailed data on imports and exports by country and by region are published by the International Trade Administration (ITA), U.S. Department of Commerce, and are on a different basis from the more general trade figures published by the Department's Bureau of Economic Analysis (BEA). In the BEA data, both imports and exports are reported on a free alongside ship (f.a.s.) basis, which means the price of the item as it is loaded for shipment. In the ITS data, exports are f.a.s., but imports are reported on a cost, insurance, and freight (c.i.f.) basis, which adds the cost of insurance and freight to the original cost of the item. Thus, in the ITA accounts, imports appear to be greater than in the BEA accounts. Where possible, the BEA figures have been used, because they present imports and exports on the same basis. However, some of the detailed data are available only from ITA.

Table 16.-Major U.S. Imports From and Exports to East Asian NICs, 1986

	C.i.f. value* (millions of dollars)	Compound annual growth rate 1982-86
Import category		
Footwear (new, exe. military)	$39	20.5%
Toys and baby carriages, etc.	3.0	13.0
Sweaters and other outerwear	2.9	26.2
Outerwear apparel, (cotton & wool)	2.6	14.4
Office and ADP machine parts	2.2	44.7
Telecommunications equipment, nspf**	2.2	23.8
Electronic components and parts	1.7	8.3
ADP machinery	1.4	128,4
Furniture and parts	1.3	34.3
Television receivers, etc.	1.2	20.2
Undergarments	12	12,6
Rubber and plastic articles	1.1	30.4
Export category		
Electronic components and parts	1.5	10,6
Air and spacecraft, etc.	1.2	9.5
Office and ADP machine parts	0.9	23.9
Organic chemicals and products	08	14,9
Hides and skins (except fur)	06	32,2
Oilseed and oleag. fruit	0.6	7.1
Rubber, plastic and syn. resin	05	10.2
ADP machines	0.5	18.1
Measuring and checking instruments	05	4.6
Telecommunication equipment	04	-45
Corn or maize (unmilled)	0.4	-8.5
Pulp and waste paper	0.4	19.1
Wheat (unmilled)	0.4	4.3

● C.i.f value of imports Includes cost, insurance and freight
● *Not specified

SOURCE: U S Department of Commerce, International Trade Administration, Office of Trade and Investment Analysis, 1986 U.S. *Foreign Trade Highlights,* March 1967

Korea, and Taiwan) and place in the top ten from Singapore. The fastest-growing imports are passenger motor vehicles, which rose from $10 million to $854 million in one year, 1985-86, and automatic data processing machines (including computers and calculators), which increased from $53 million to $1.4 billion in the 4 years 1982-86. Almost all automobile imports from the Asian NICs are from Korea, while automatic data processing machinery exports are from all four nations, with Taiwan accounting for 52 percent, Korea for 26 percent, Singapore for 16 percent, and Hong Kong for 6 percent.

In general, developing nations are less able to cope with a diminishing American market for their exports than developed nations. Even Taiwan, with a healthy and growing trade surplus and massive reserves of foreign exchange, could have problems with adjustment.[130] Like many other developing nations, it is highly dependent on export-led growth, particularly in exports to the United States. America is the market for half of Taiwan's exports, and over half of Taiwan's GNP depends on exports.[131]

South Korea's economy may be more vulnerable, as Korea is only just beginning to reverse chronic trade deficits, and is still trying to pay off a massive international debt.[132] Like other Asian NICs, Korea has pursued a strategy of export-led growth, which is successful as long as exports are able to expand fairly rapidly. In 1987, for example, Korean GNP rose 24 percent, pulled by a 36 percent expansion in exports. Korea was able to run a current account surplus in 1986, for the first time in modern history, mainly

130 Carl Goldstein, "Economic Monitor Taiwan: Exports Hit New Peaks,'' Far Eastern Economic Review, 9 April 1987, p. 137.
131 Robert G. Sutter, 'Taiwan: Recent Developments and Their Implications for the United States, ''Congressional Research Service Issue Brief IB87092, Updated June 16, 1987; information provided by the Cm-ordination Council for North American Affairs.
132 Lawrence A. Veit, "Time of the New Asian Tigers, ''Challenge, July-August 1987. Korea's international debt totaled $45 billion in 1986 –45 percent of Korea's $100 billion GNP.

due to its increasing import penetration of U.S. markets. Lower oil prices, the appreciation of the yen, and falling interest rates helped, but Korea's $9.4 billion trade surplus with the United States in 1987 offset its $5.2 billion deficit with Japan. However, Korea's dependence on exports could backfire when the U.S. merchandise trade deficit shrinks. Exports account for 40 percent of Korean GNP, and 39 percent of Korea's exports go to the United States – up from 30 percent a decade ago.[133] Reducing the U.S. trade deficit might cause political as well as economic trouble in Korea.

The U.S. merchandise trade deficit with Latin America was $12.2 billion in 1987, amounting to only 8 percent of the total. This represented a steep deterioration for the United States, however, with U.S. merchandise trade having descended from a surplus with Latin America of $1.3 billion 1981. Most of the deficit is with just three countries: Mexico ($5.7 billion), Brazil ($4.1 billion), and Venezuela ($2.0 billion) as shown in table 17. In contrast to imports from Asian developing countries, or developed countries, imports from Latin America are tilted heavily towards natural resource commodities: petroleum and agriculture and fishery products account for 40 percent. However, imports of internal combustion piston engines have been growing very rapidly in the 1980s, from $362 million in 1982 to $1.1 billion in 1986, mostly an indicator of the importance of Mexican production. The trade deficit with Latin America peaked in 1984, declining since then as a result of both modest increases in exports and contractions in imports. A part of the drop in value of imports is due to the sharp drop in oil prices in 1986.

Table 17.– Major U.S. Imports From and Exports to Latin America, 1986

	C.i.f. value* (millions of dollars)	Compound annual growth rate 1982-86
Import category		
Crude petroleum . . . . . .,	$6.9	-11 .9%
Petroleum products	48	-12.0
Coffee . . . . . .,	34	13.1
Fruits and nuts (prepared), nspf** .,	16	9.0
Shellfish (fresh, frozen, salted) . .	12	70
Internal combustion engines	1.1	31.1
Footwear (new, exe, military) .,	10	20.4
Electrical distributing equipment .,	0 8	336
Special transactions, nspf** .	0 8	0.6
Motor vehicle parts, nspf**	0 8	284
Export Category		
Road vehicles and tractor parts	1,7	08
Organic chemicals and products	11	4.1
Air and spacecraft, etc.	09	3.1
Telecommunication equipment .,	10	9.2
Civil engineer and contractors	09	13,8
General merchandise, low value	09	28.4
Rubber plastic and syn. resins .,	08	3,2
Internal combustion engines . .	0.8	46
Petroleum products (refined) .,	0.8	139
Office and ADP machine parts	07	13,3
Electronic components and parts	07	150
Electrical appar. (current carrying)	06	65
Wheat, unmilled	05	193
ADP machines	05	50
Measuring and checking instruments	05	-2.7
Electrical machinery	05	00
Specialized industrial machinery	05	23
Electrical distributing equipment	04	276
Fertilizers and materials .,	04	64
Misc. chemical products .,	04	-19
Paper and paperboard	04	-43
Non-electric parts, nspf**	04	05

*C ıf value of imports Includes cost, insurance and freight
* Not specified

SOURCE U S Department of Commerce, International Trade Administration, Office of Trade and Investment Analysis, 1986 U S Foreign Trade *Highhights*, March 1987

Much of the deterioration in our merchandise trade balance with Latin America in the 1980s has to do with indebtedness. Brazil, the largest Latin American debtor, owed nearly $107 billion to foreign creditors in

133Christopher Madison, "Korea: A New Interest, ''National Journal, April 5, 1986; information provided by the Korean Embassy

1985; Brazil's foreign debt was equal to 51 percent of its GNP. Mexico owed $97 billion, with debt at over 58 percent of GNP; Venezuela's debt was $32 billion, or 66 percent of GNP. Nations facing heavy international debt burdens have been forced by their major creditors (the International Monetary Fund and U. S., European, and Japanese banks) to devalue their currencies and institute austerity programs —which boost exports and curtail imports–before their creditors would refinance their debts. So far, these countries have made little progress in reducing their debt levels; one result is a conflict between the needs of the United States to curb its merchandise trade surplus and needs of Latin American debtors to run trade surpluses to pay off their debts. Many proposals have been made to deal with the Latin American debt crisis, but whatever the outcome, the difficulties of managing these debts are sure to intensify as U.S. trade deficits fall.

The U.S. trade deficits of the 1980s not only enabled Americans to consume beyond the nation's means –for the time being. They also helped to fuel the economic growth of a number of countries that based their growth on rising exports to the world's largest market. Leaving aside the costs that went along with the benefits of America's buying spree (e.g., job losses of American factory workers), the situation cannot last. As noted earlier, foreign capital will not indefinitely make up a widening difference between what we buy from other nations and what we sell. The burdens of the inevitable adjustment, when it comes, will fall both on American consumers and on foreign exporters. The adjustment might take a number of different forms, some easier than others, but none painless.

International Companies

American companies with affiliates in other countries, and foreign companies with affiliates in the United States, are important players in international trade. Their trade effects (at least through 1985, the last year for which data are available) are not entirely what might be expected. From 1982 to 1985 –years of large and growing national trade deficits – all American companies with affiliates abroad showed consistent merchandise trade surpluses of $3 billion to $5 billion with their affiliates (see table 18).[134]

Foreign affiliates of U.S. manufacturing companies accounted for 43 percent of the total $898 billion sales of the foreign affiliates of all American companies in 1985. Trade surpluses of manufacturing parents and their affiliates amounted to $11 billion to $15 billion in 1977 and 1982-85. For the U.S. parent companies overall, trade in petroleum inflated imports, resulting in a small deficit in 1977, and in the 1980s diminishing to some extent the surpluses due to trade between U.S.-based manufacturing companies and their affiliates.

Since World War II, many U.S.-owned companies have engaged in large scale

134The data in table 18 are for U.S. parent companies in the manufacturing indust V and foreign affiliates in which they hold a majority interest.

Table 18.–Balance of Merchandise Trade, U.S. Parent Companies and Majority-Owned Foreign Affiliates, 1977 and 1982-85 (billions of U.S. dollars)

	All U.S. companies	U.S. manufacturing companies
1977	$-1.6	$12.3
1982	5.8	14.7
1983	3.6	11.2
1984	3.4	11.7
1985	5.7	14.4

NOTE: Majority-owned foreign affiliates are those in which the U S parent company holds a mqo~-ownership

SOURCES U S Department of Commerce, Bureau of Economic Analysis, *U.S. Direct Investment Abroad,* 1977 (Alexandria, VA: National Technical Information Service, April 1981) tables III T 1 and III T 4, U.S. Direct Investment Abroad: *1982 Survey* (Washington, DC: U S Government Printing Offfice, December 1985), tables III P 1 and III P 4, *U.S. Direct Investment Abroad: Operations of Parent* Companies and *Their Foreign Affiliates,* 1983-85, available from the Bureau of Economic Analysis, tables 57 and 58

manufacturing operations overseas, mostly in the developed world. About three-quarters of the sales by foreign manufacturing affiliates of U.S. companies are in developed countries — nearly 50 percent in Europe and another 20 percent in Canada. It is generally accepted that the main reason American companies produce goods in Europe is to sell the goods there; and these operations are associated with trade surpluses for the U.S. parent companies.[135]

Some production by affiliates of U.S. companies in developing and newly industrializing countries is for the same purpose, but another important reason is to reduce costs of producing goods to be sold back in the United States and in other markets. While manufacture by U.S.-affiliated companies in less developed countries is still on a much smaller scale than activities in the industrialized world, there is evidence of change in regional patterns. Manufacturing by and for American companies in Korea, Southeast Asia, and Mexico is growing fast–much faster than production by U.S. affiliates in developed countries. These are the most favored locations for going offshore to lower labor costs. And these operations are generally associated with trade deficits for the U.S. parent company. However, the amounts involved were not yet large enough in 1985 to make much of a dent in the surpluses from operations in Europe and Canada. The large and growing national trade deficits of the 1980s were reduced, not aggravated, by operations of U.S.-based companies abroad.

The opposite has been true of foreign companies and their affiliates in the United States. The deficit arises chiefly from wholesale trade — evidence that the main reason for foreign companies to operate in the United States is to sell here, just as U.S. companies operate in other industrialized countries principally in order to sell there. Merchandise trade between foreign parents and U.S. affiliates showed sizable and growing deficits on the U.S. side, from 1977 to 1985 (table 19). Most of the deficit is due to sales of foreign goods – cars, VCRs, compact disk players– through local wholesale outlets of foreign companies. For example, in 1985,$45 billion of the $54 billion deficit associated with trade between U.S. affiliates and their foreign parents was in wholesale trade –$22 billion in motor vehicles and equipment and another $21 billion in other durable goods.

135 Data published by the U.S. Department of Commerce, Bureau of Economic Analysis on U.S. Direct Investment Abroad, Operations of U.S. Parent Companies and Their Foreign Affiliates, show that nearly half of all sales by foreign manufacturing affiliates of U.S. companies are in Europe; that most goods produced by these European affiliates are sold in Europe; and that exports from the U.S. parents to their manufacturing affiliates in Europe are substantially greater than imports.

Table 19.-Balance of Merchandise Trade, Foreign Companies and U.S. Affiliates, 1977-85
(billions of U.S. dollars)

	All U.S. affiliates	U.S. manufacturing affiliates
1977	$ -19.2	$ -3.1
1978	-22.7	-4.2
1979	-23.2	-6.1
1980	-26.0	-5.2
1981	-25.3	-5.1
1982	-26.9	-4,6
1983	-32.2	-6.1
1984	-43.4	-7.7
1985	-54.1	8.4

NOTE: US affiliates are those in which a single foreign person owns or controls directly or in directly a 10 percent or greater share

SOURCES: US Department of Commerce, Bureau of Economic Analysis, *Foreign Direct Investment in United States, Operations of* U.S. Affiliates, *1977-60,* table G-3; *Foreign Direct Investment in the United States, 1980,* table G-3, *Foreign Direct Investment in the United States, Opereations of* U.S. *Affiliates of Foreign Companies,* 1981-85, table G-3, all available from the Bureau of Economic Analysts

U.S. manufacturing affiliates of foreign parents have also had persistent and growing deficits in merchandise trade, but on a much smaller scale. Considering only trade between the affiliates and their parents, the deficit rose from $3.1 billion in 1977 to $8.4 billion in 1985; if trade with unaffiliated foreigners (on both the import and export sides) is added in, the deficits were smaller, rising from $2.1 billion to $5.6 billion. These deficits are more or less comparable with the surpluses associated with trade between foreign affiliates of U.S. manufacturing companies and their parents. One way that these deficits could arise in the affiliate's country is that the parent company exports parts and materials to its affiliate abroad, where more value is added – but not enough to offset the import of parts and materials. If the item is sold in the affiliate's country, then the sale helps the home country's trade; if it is sold back in the parent country or in a third country it has a negative effect on the home country's trade balance.

The idea that foreign investment in the United States–specifically, investment in manufacturing plants –will reduce merchandise imports very substantially is not necessarily or always true. To the extent items made in the foreign investor's plant replace imported goods, they do reduce imports, and improve the trade deficit. But if they replace goods made by a domestic manufacturer, then they could increase imports and worsen the deficit.

The persistently low dollar may stimulate production of goods in foreign-owned plants in the United States at the expense of imports. There was some evidence by mid-1988 that higher prices, reflecting the high value of the yen, was finally beginning to stem imports of Japanese cars. It would not be surprising if Honda, Toyota, and Mazda were to switch as much production as possible for the U.S. market (and possibly some production for other countries as well) to their American plants. This would help to reduce the trade deficit--and the more U.S. suppliers replace Japanese suppliers, the greater the effect.