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Fair or Foul?

A major protectionist measure, apparently designed to greatly restrict the ability of Japanese automakers to sell in the United States, has widespread sponsorship in Congress. Enactment of this bill, grossly misnamed the "Fair Practices in Automotive Products Act," would be a setback for the U.S. economy. Protection of an industry (particularly one that has clearly demonstrated its inability to provide what consumers want) would quickly be offset by declines in some other sector, even if it is now doing its job well. This is because a reduction in imports by legal mandate will perforce result in fewer exports to foreign consumers with fewer dollars to spend here. That other countries restrict their international commerce mainly hurts their own citizens and is no reason why we should follow their example.

According to Douglas Fraser, the President of the United Auto Workers' Union (UAW), "A failure to ensure a strong American auto industry would be economically devastating to the entire United States economy." Mr. Fraser was writing in support of a bill, the "Fair Practices in Automotive Products Act," which would require automakers selling 500,000 cars a year in the United States to have 90 percent "domestic" parts and labor in their autos. The bill would impose smaller required "domestic" content on producers selling fewer than 500,000 cars annually and producers selling fewer than 100,000 cars would be exempt entirely.

Although seemingly straightforward, the bill, like most such measures, would be a nightmare for anyone except the most dedicated bureaucrat. Would the permissible "foreign" content be calculated on the basis of dollars or of the producer's currency? What if the exchange rate changes? What if the "foreign" and "domestic" content differs among the same producer's models? Etc., etc.

Despite the difficulties of administering such a measure, and despite the more fundamental considerations discussed below, the bill reportedly has 218 sponsors in the House of Representatives (more than enough to support its passage there) and 17 in the Senate. This support is testimony to the influence and power of the UAW. Reportedly, the auto companies (who might like to use more foreign parts and components, but also who would like to sell more cars) have neither supported nor opposed the bill publicly.

Fair to Whom?

The title of the bill suggests that heretofore someone has been engaged in "unfair" practices. Only six foreign producers sold more than 100,000 cars in the United States during 1980 and 1981 and all six were Japanese.* Thus the bill seems clearly aimed at automobile imports from Japan. How have the Japanese been unfair?

Although there is no doubt extensive documentation regarding Japanese policies with respect to taxation, finance, employment, etc., relative to our own, the only indisputable evidence that the Japanese have been "unfair" in the production and sale of automobiles is the trend of sales. Over 1.8 million Japanese cars were sold in the United States during 1981, which was 37 percent more than were sold during 1978. Domestic sales of U.S. model cars decreased 33 percent between 1978 and 1981. Clearly if these trends had not occurred, or even if sales of Japanese cars had decreased 33 percent between 1978 and 1981, along with those of U.S. models, no one (not even the UAW) would be knocking on the doors of Congressmen demanding legislation such as the proposed "Fair Practices in Automotive Products Act."

Moreover, there is every reason to believe that, in the eyes of the millions of Americans who have purchased Japanese cars in recent years, it has been the U.S. automobile industry that has been "unfair," by not producing the cars they wanted or offering them at prices they wanted to pay.

But the entire notion of "fairness" misses the point. As Henry George wrote nearly 100 years ago:

"Can there be any greater misuse of language than to apply to commerce terms suggesting strife, and to talk of one nation invading, deluging, overwhelming or inundating another with goods? Goods! What are they but good things – things we are all glad to get? Is it not preposterous to talk of one nation forcing its good things upon another nation? Who individually would wish to be preserved from such invasion? Who would object to being inundated with all the dress-goods his wife and daughters could want; deluged with a horse and buggy; overwhelmed with clothing, with groceries, with good cigars, fine pictures, or anything else that has value? And who would take it kindly if any one should assume to protect him by driving off those who wanted to bring him such things?"†

The Other Side of the Coin

When the Japanese, or anyone else sells goods in the United States, what do they receive? The first thing they receive is, of course, dollars, but presumably few foreign vendors wish to acquire dollars simply to hold them. What they want is the things that dollars can buy. Many things outside the United States, notably oil, can be purchased for dollars, but eventually most of the dollars used to buy goods from foreigners find their way back to U.S. markets. Some may be used to buy U.S. goods, but they also may be used to buy

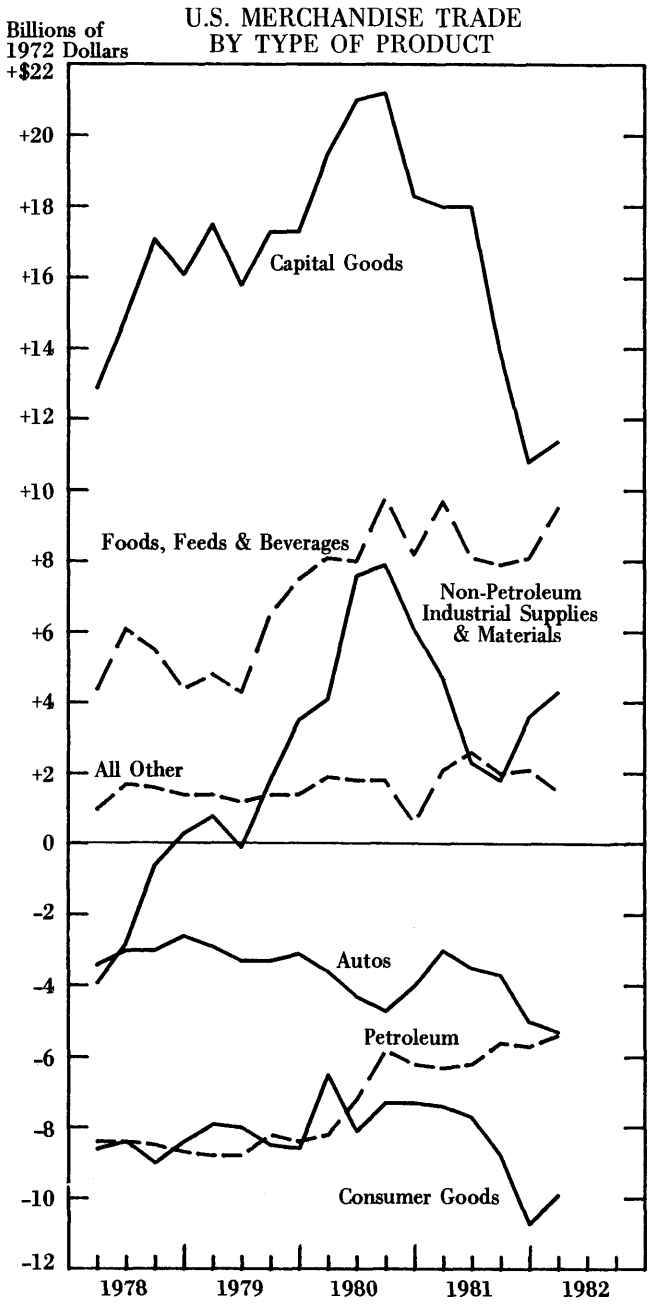
* These six (and their 1981 sales) are: Toyota (576,491), Datsun (464,806), Honda (307,705), Mazda (166,105), Subaru (152,062), and Mitsubishi, imported by Chrysler (110,940).

† Henry George, *Protection or Free Trade*, 1886.

services or to buy U.S. securities, or other investments.

The accompanying chart shows the components of the U.S. merchandise trade since 1978. The data are shown in 1972 dollars and thus provide an indication of the trends of the physical volume of our imports and exports. As the chart shows, net imports of automobiles are a relatively small portion of our international trade. The recent deterioration in the U.S. trade balance is mainly the result of decreased net exports of capital goods and increased net imports of consumer goods.

More importantly the chart indicates that any artificial curtailment of auto imports by regulation or fiat is likely to quickly result in an equivalent change in some other component of international trade. This is because if Americans are prevented by law from buying, say, the Japanese cars they would like to buy, then the Japanese, or other foreigners they trade with, will have fewer dollars with which to buy American goods. Thus, the "economic devastation" that Mr. Fraser asserts would result from "failure to ensure a strong American auto industry" would be simply shifted to another sector of the U.S. economy if the auto industry's "strength" is "ensured" by law rather than by an ability to produce the cars consumers want at the price they wish to pay.



Note: Quarterly data shown at annual rates. A positive value indicates net exports.

"Others Do It"

A common argument for protectionist measures such as the Fair Practices in Automotive Products Act is that, despite the arguments against protection, most other countries support their domestic industries via various tariff and non-tariff barriers to trade. Thus, we are often told, the United States needs to respond in kind to maintain its position in the world.

Unfortunately, the response to this line of reasoning all too often is to dispute the evidence regarding the "dumping," quotas, regulations, and "red tape" designed to harrass our exporters and so forth. The 31 countries that, according to Mr. Fraser, "now have content laws for their auto industries," in fact are harming their own citizens' interests more than anyone else's. That other countries' governments stand in the way of their citizens' wishes (in this case their wish to buy the cars of their choice) is no reason why we should. We reject government censorship of the press and we insist that our police cannot arrest people without charging them with a crime and bringing them to trial. These and many other of our freedoms are unknown in most of the world today. Why should the situation be any different with respect to trade?

Foreign governments *do* discriminate against our exports and subsidize their exports. To the extent that these practices succeed, they work to provide more goods for Americans and fewer for foreigners. As Henry George observed, this is not cause for complaint for Americans: it is the foreigners who are ill-served by their own restrictions. This has always been a difficult point for the public to grasp, perhaps because the benefits of free trade are diffused throughout the population, while the special interest groups are vocal and insistent.

Most analysts believe that the Fair Practices in Automotive Products Act will be allowed to die somewhere in the legislative process, despite its widespread Congressional sponsorship. If it somehow becomes law, it would represent a major setback for the American economy.

MOTOR VEHICLE PRODUCTION, SALES, AND INVENTORIES

Sales of U.S.-made cars and trucks increased substantially during the first 6 months of 1982 from the low levels of 1981's last quarter. Recent sales may have reflected "rebates" and other incentives that the manufacturers are finding too costly to continue. Production levels also increased substantially during the second quarter, but auto production remained below year-earlier levels. Production schedules for the second half of 1982 were recently curtailed to levels that suggest that automakers do not expect sales to increase for 1982 as a whole.

Sales of U.S.-made automobiles continued to increase during the 3 months ended in June 1982. Average monthly sales, then of 525,305 cars, were 12.5 percent more than that during the first quarter. This was substantially larger than that for the fourth quarter of 1981, 426,804

Table 1
RATES OF CHANGE IN VEHICLE SALES, PRODUCTION, AND INVENTORIES

	Percent Change from Preceding 3 Months to the 3 Months Ended in			
Sales	*Sept. '81*	*Dec. '81*	*Mar. '82*	*Jun. '82*
U.S. cars	+2.7	−20.8	+9.4	+12.5
U.S. trucks	−11.5	−15.7	+43.1	−0.2
Total U.S. vehicles	−1.0	−19.6	+17.7	+8.7
Imported cars	−9.3	−17.5	+14.5	+3.0
Total cars	−0.8	−20.0	+10.8	+9.9
Production				
U.S. cars	−31.7	−5.8	−17.6	+46.1
U.S. trucks	−33.2	+17.9	+17.0	+28.4
Total U.S. vehicles	−32.0	−1.1	−9.5	+40.8
*Inventories**				
U.S. cars	−14.3	+3.1	−15.2	+9.5

* Percent change from end of period to end of period.

cars, which was the worst sales quarter of the worst sales year since 1961.

U.S.-made truck sales did not fare as well, on average, in the second quarter of 1982, declining by 0.2 percent after a large first quarter increase. The first quarter increase was magnified by the poor performance of truck sales during the last quarter of 1981. Overall, sales of U.S.-made vehicles rose by 8.7 percent in 1982's second quarter following the previous quarter's 17.7 percent rise. Imported car sales also continued to rebound from the disastrous fourth quarter, yet they also remained fewer than last year's second quarter.

Production of U.S. cars increased sharply during the second quarter of 1982 after decreasing substantially during the prior three quarters. Truck production also increased, and its level during June was 16.2 percent higher than last June. June automobile production was 20.3 percent lower than June 1981.

Even though the data for 1982's second quarter are somewhat encouraging, the year-to-year sales and production figures presented in Table 2 indicate the magnitude of the industry's decline. That automobile sales have been decreasing continually since 1979 lends additional support to recent suggestions that the United States has been experiencing one continuous recession since mid-1979, not two as "officially" determined by the National Bureau of Economic Research and the Department of Commerce. This is also evident in the accompanying charts, especially the sales data. The 3-month moving average for total vehicle sales peaked during June 1978 at its highest recorded level of 1,289,705 vehicles. The sales peak occurred 18 months before the general cycle's peak. Total sales trended downward for 3.5 years (hardly participating at all in the 1980-81 expansion of general business activity) and apparently troughed in January 1982 at 527,592 units, their lowest level since October 1961. Total production followed roughly the same pattern, peaking in May 1978 and reaching an apparent trough in February 1982.

Table 2
U.S. AUTOMOBILE PRODUCTION AND SALES

	Total Production	*Percent Change from Year Earlier*	*Total Sales*	*Percent Change from Year Earlier*
1977	9,211,411	+8.5	9,104,400	+5.8
1978	9,173,606	−0.4	9,308,000	+2.2
1979	8,422,074	−8.2	8,328,000	−10.5
1980	6,372,304	−24.3	6,578,300	−21.0
1981	6,251,003	−1.9	6,205,856	−5.7
1982*	2,635,269	−26.2	2,976,603	−10.0

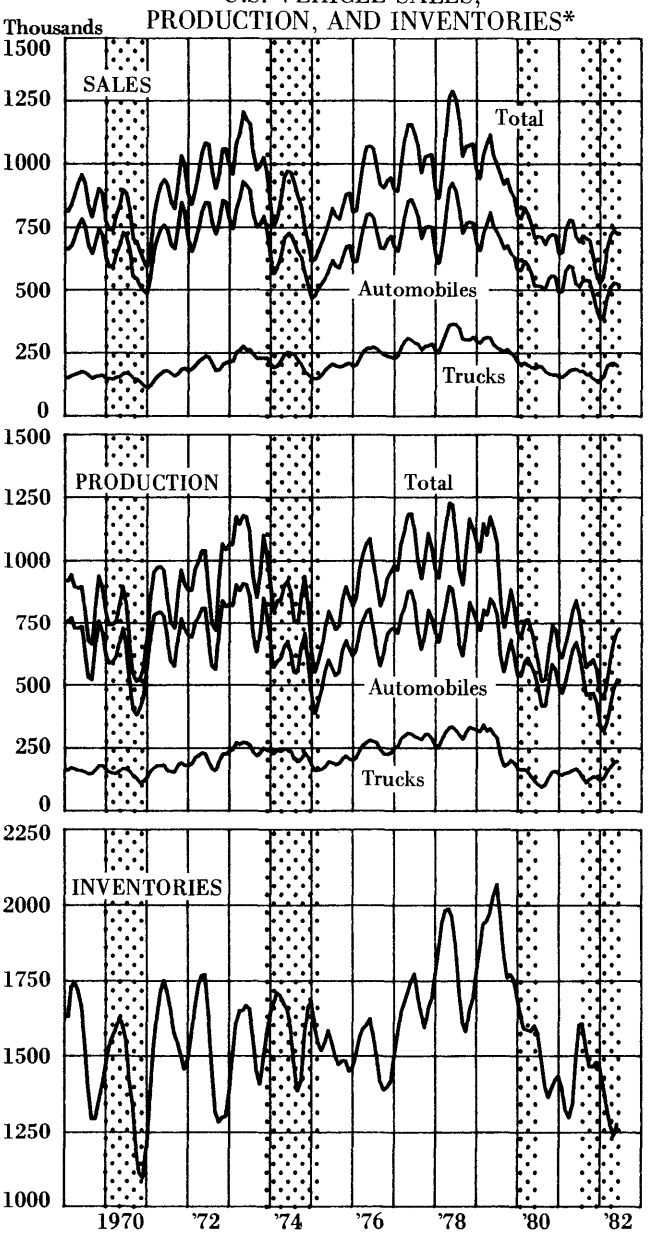
* Six months only.

We say "apparent" because of the uncertainty of future sales and production trends.

Over the past four business cycles production trends for U.S. motor vehicles have followed the sales patterns fairly closely as can be seen in the accompanying tables and charts. Yet over the last two cycles, U.S. auto producers have done a much better job in quickly adjusting motor vehicle output to sales rates and have brought inventories down to 1971 levels (see chart). At the end of 1982's second quarter, U.S. car dealers' inventories totaled 1,365 million new domestic automobiles. This was 18.0 percent fewer than last June's inventory figure. Even so, June 1982's inventories increased substantially over May's level and may reflect unfounded optimism on the part of auto manufacturers.

Even though sales and production figures have rebounded of late, there is no reason to believe that these trends will continue to a point where they will come any-

U.S. VEHICLE SALES, PRODUCTION, AND INVENTORIES*



* Three-month moving averages, not seasonally adjusted.

where close to the production and sales of 1973 or 1978. In fact, industry analysts don't foresee the third and fourth quarters of this year as matching the production total for the second quarter. *Ward's Automotive Reports* recently noted that GM and Ford eliminated 200,000 cars from their production schedules for the last half of 1982. Third quarter production expectations are reduced by 97,000 cars to 1,334,000 and the fourth quarter suffers a 101,000 car reduction to 1,454,000 cars. Total production for 1982 is projected by Ward's to be 5,423,000, 13.2 percent below last year's total of 6,251,003 units. It appears as if the auto producers have tailored their production schedules to what one analyst called a "declining market."

This change in attitude is probably influenced by continuing high interest rates and the manufacturers' own realization that recent "rebate" strategies (including interest rate subsidies) are too expensive to maintain. Consumers reacted in a highly favorable fashion to these schemes in the first two quarters of 1982 and may have built the expectation of rebates into their consumption decision-making processes. Hence, consumers may wait for the reintroduction of interest rate subsidies and, if so, the future for auto sales is not encouraging. In any event, the curtailed production schedules for the second half of 1982 suggest that the auto producers have shed some of their ingrained optimism. Even allowing for the fact that inventories usually decrease during the second half of the year, that the automakers expect to produce only 2.4 million units during the second half of 1982 suggests that they do not expect their second half sales to exceed the "depressed" levels of the second half of 1981.

On a brighter note, U.S. auto manufacturers seem to have found ways to regain and/or maintain profitability despite the gloomy sales figures. Recent reports indicate that GM showed a $560 million profit in the second quarter despite declines in the sales of cars and trucks. Higher prices and cost-cutting measures contributed greatly. Ford was able to report second quarter net income of $205 million due to sharp cost reduction schemes and Chrysler profits totaled $107 million then. But some of these earnings reflected sales of assets and other dealings rather than gains from producing and selling vehicles. Nevertheless, the current recession clearly is having some favorable effects on automakers by forcing them to become more efficient.

1982 BUDGET UPDATE

As we went to press with this week's *Research Reports*, the Federal Government's actual receipts and outlays for the month of June became available. We have incorporated this information in the accompanying table, which is similar to tables we published on April 26 and May 31. In the table we show the actual receipts and outlays for the first 9 months of the fiscal year, and what they will have to be during the remaining 3 months of the fiscal year, if they are to equal earlier budget projections.

The data through June suggest that the deficit for fiscal 1982 is likely to be approximately $100 billion, which is roughly what President Reagan projected in his budget message to Congress last February and what has since been projected by the Office of Management and Budget (OMB). New OMB projections are expected to appear shortly, but they are not expected to significantly alter the deficit projected earlier.

The projections used in this table are those published last April. The overall deficit projected then seems likely to prove close to the mark, much closer in fact than the projections of the Congressional Budget Office (CBO), which expected the fiscal 1982 deficit to total as much as $117 billion as recently as last May, or of some private analysts, such as Michael K. Evans who, also last May, forecast a $135 billion Federal deficit for fiscal 1982. Nevertheless, the press continues to characterize the administration's projections as "overoptimistic" and other estimates, CBO's in particular, as "more realistic."

THE FEDERAL BUDGET FOR FISCAL 1982
(Billions of Dollars)

	Actual		Projected*		Total
Receipts	*Oct.-Jun.*	*Percent Change†*	*July-Sept.*	*Percent Change†*	*Fiscal Year***
Individual inc. taxes	$220.7	+5.8	$80.7	+1.2	$298.9
Corporate inc. taxes	42.0	−14.5	9.6	−20.2	51.6
Other	205.8	+9.4	72.1	+12.5	277.9
Total	$418.5	+5.1	$159.9	+4.3	$628.4
Outlays					
National defense	$138.3	+17.7	$49.3	+16.4	$187.6
All other	404.6	+7.1	136.7	+14.3	541.3
Total	$542.1	+9.6	$186.0	+14.8	$728.9
Deficit	−$74.5	+50.7	−$26.1	+204.7	−$100.5
Memo: 1981 Deficit	−$49.4	–	−$8.6	–	$57.5

* Total for year less actual for first 9 months.
† Percent change from corresponding period of Fiscal 1981.
** From *Current Budget Estimates*, April 1982.

An accurate forecast of the Federal budget deficit will always probably contain a large element of "dumb luck." As the table suggests, both receipts and outlays are likely to be lower than forecast by OMB last April.

Income tax receipts during the last quarter of the fiscal year may come close to those shown in the table. Comparisons of income tax receipts with a year earlier are likely to deteriorate as a result of cuts in withholding taxes and diminished corporate profits. To date, withholding tax receipts have fallen well below expectations as a result of the continued recession, but this has been offset by large unanticipated increases in other income tax receipts (see *Research Reports* for July 5). However, the other tax receipts during the July-September period are unlikely to total the $72.1 billion shown in the table, particularly inasmuch as receipts from the so-called windfall profits tax have been recently *behind* year-earlier levels.

On the spending side, outlays for national defense seem likely to continue about as expected. Increased outlays are expected for some items such as crop support and interest, but the abatement of general price increases will continue to be reflected in budget savings. This July's cost of living increase for Social Security beneficiaries, 7.6 percent, is well below the increase required to bring non-defense outlays up to the total projected for the year. It seems unlikely that the growth of non-defense outlays will double to 14.3 percent during the last quarter of the fiscal year, from 7.1 percent during the first three quarters.

PRICE OF GOLD

	1981	*1982*	
	Jul. 30	*Jul. 22*	*Jul. 29*
Final fixing in London	$402.25	$353.00	$342.50

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