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ISSUES AT THE SUMMIT

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CONGRESS OF THE UNITED STATES

together with

ADDITIONAL AND SUPPLEMENTARY VIEWS

MAY 4, 1977

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LETTER OF TRANSMITTAL

MAY 4, 1977.

To the Members of the Joint Economic Committee:

Transmitted herewith for the use of members of the Joint Economic Committee and other Members of Congress is a report of the Joint Economic Committee entitled "Issues at the Summit."

The report is based on mid-April hearings involving an outstanding panel of witnesses including representatives from Japan, Germany, Great Britain, the United Nations Conference on Trade and Development, along with American spokesmen for business and labor. It is intended to provide guidance to the President in respect to issues that he will be dealing with in the forthcoming summit meetings with foreign heads of State.

Sincerely,

RICHARD BOLLING,
Chairman, Joint Economic Committee.

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ISSUES AT THE SUMMIT*

On May 7, 1977, President Carter will meet with the heads of state of six other leading industrial countries and the President of the Commission of the European Communities to discuss economic issues that confront all of these nations. While no representative of the oil producing or the non-oil-producing developing countries will be present at the meeting, the actions and requests of these nations have placed several issues on the agenda of the summit and will continue to have a major impact on the industrial economies throughout the foreseeable future. Moreover, meetings with both oil exporters and developing countries will occur shortly after the London summit conference.

On the basis of hearings conducted on April 20 through April 22, 1977, the Joint Economic Committee offers the President before his departure its views on some of the issues that he will be discussing with foreign leaders. In an attempt to include all relevant perspectives in our hearings, we invited not just Americans to testify but several prominent foreigners as well. These individuals from other countries included one of the five members of the Council of Economic Experts advising the German Government, a respected Japanese economist, an advocate of the proposals advanced by the United Nations Conference on

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* Senator Roth states, "Due to the press of Senate business, I have not been able to give this report the close attention it deserves, and thus I am not in a position either to endorse or to dissent from the report's findings and conclusions."

Trade and Development (UNCTAD), and an official of the Commonwealth Secretariat. The schedule of our hearings and a complete list of witnesses is appended to this report.

We offer our recommendations for President Carter's consideration and for possible discussion at the summit conference. They are also intended to provide a basis for congressional reflection on these international economic issues.

The recommendations are not intended to be the definitive statement on any of the issues. These questions are too complex to be answered neatly in a few sentences. We submit our views as sensible policy proposals for the United States or, in some cases, for industrialized nations as a group to consider. The United States would be guilty of arrogance if we were to go to the London summit meeting or any other international conference expecting policy decisions reached here to be accepted in toto by other countries. Witnesses at our hearings stressed the desirability, indeed the necessity, of consultations among the major advanced and developing countries before adopting and announcing major new policy initiatives if we are to find willing cooperation and support.

Growth in the Industrial World

The leading industrial countries should commit themselves to agreed growth rate targets and to the use of the policies necessary for assuring realization of these objectives. They should closely monitor current developments and modify stimulus programs as necessary. 1/

The deep world recession of 1974-75 and the sluggish recovery of the leading industrial countries have left most countries in the Organization for Economic Cooperation and Development (OECD) with historically high levels of unemployment. Slow growth in these leading economies has exacerbated the payments difficulties of both weaker OECD countries and the developing world. As a result, protectionist sentiment has been on the rise throughout the industrialized world.

Unemployment, payments imbalances, and the dangers of a trade war would all be reduced by a satisfactory rate of expansion in the industrial countries. The key to economic expansion lies with the stronger economies -- those of Japan, Germany, and the United States.

In Japan, the modest economic recovery that began in 1975 continued through part of 1976. Real GNP that had actually fallen in 1975 grew by 5.7 percent in 1976. The Japanese trade and payments position remained strong. In 1976, Japan recorded an $11.2 billion trade surplus, a $4.7 billion current account surplus, and continued to add to its reserves.

There were still, however, a number of trouble spots. Consumer prices in Japan increased 9.4 percent, more rapidly than in most other industrial countries. The unemployment rate rose slightly to 2 percent of the labor force. And by the end of 1976, the economy had stalled.

In response to domestic pressures for renewed growth and international pressures to increase the level of Japanese imports, the Fukuda Administration has adopted a three-step stimulus package. In fiscal year 1977

(the Japanese fiscal year runs from April 1 to March 31), the Fukuda Administration plans to increase spending on public works by $2.4 billion, decrease taxes by $2.3 billion, and lower the discount rate substantially.

The Fukuda stimulus package is based on the Japanese Government's target of 6.7 percent growth in 1977. Most economists, however, suspect that the growth rate will be lower -- around 6 percent. The Japan Economic Research Council, a private research group, is even less optimistic. In a recent study, the Council has projected a 5.1 percent growth rate for 1977, with private fixed investment, inventory investment, and personal consumption all growing at rates below the Government's projections.

German economic performance in 1976 was the envy of the Western world. Real GNP grew at more than 5 percent and consumer prices increased by only 4.5 percent. The German trade and payments position is very strong. In 1976 Germany achieved a trade surplus of slightly more than $14 billion despite a 14 percent increase in the value of the German mark relative to other currencies. Unemployment, however, remained a serious problem. Despite the relatively rapid growth of the German economy, the unemployment rate fell by only one-tenth of one percent to 3.7 percent of the labor force (figures adjusted for U.S. concepts). More than 1-1/4 million Germans are still out of work.

In early 1977, the German Government indicated that it would increase spending in public works by $5 billion. In late March, the German Government added $1.7 billion to its proposed package and specifically labeled the change as an attempt to respond to

President Carter's request for greater German stimulus.

The German Government foresees a relatively bright year with the economy growing at over 5 percent, consumer prices rising by only 3.5 percent, and exports growing at between 8 and 10 percent. Some forecasts put the German trade surplus in 1977 as high as $18 billion despite the expectations of further appreciation in the value of the mark. Not all the forecasts are so confident of German growth. For instance, the OECD foresees real growth in Germany hovering around 3.5 percent. If the OECD forecast proves to be correct, there would be ample room for further German fiscal stimulus.

For the United States, 1976 brought rather mixed economic results. GNP did grow by 6.2 percent and the rate of increase in consumer prices fell more than two full percentage points from 7.3 to 4.8 percent. Although unemployment fell to 7.7 percent for all of 1976, it was higher (7.9 percent) at the end of 1976 than it had been in the first quarter (7.6 percent). Economic growth at an annual rate of 9.2 percent in the first quarter of 1976 slowed in the rest of the year to an annual rate of 3.6 percent. In sharp contrast to Germany and Japan, the United States experienced a $9 billion trade deficit and a $0.6 billion current account negative balance.

Reflecting concern over the slowed economy and high rates of unemployment, the Carter Administration proposed a two-year, $30 billion stimulus package that mixed tax reductions with spending for public works and public service employment. Early 1977, however, brought more rapid rates of both

growth and inflation than had been expected. Despite the exceptionally cold weather in January, GNP grew at an annual rate of 5.2 percent in the first quarter. Industrial production rose by 1.4 percent in March, the biggest monthly increase since August 1975. Retail sales did slump by 2.1 percent in January, but grew 2.7 percent in February and an additional 2.4 percent in March. At the same time, wholesale prices rose sharply in February and March.

In response to the good news about growth and the bad news about inflation, the Carter Administration withdrew the bulk of its tax proposals. The result was virtually to halve the size of the stimulus package and concentrate its impact on 1978.

In its Annual Report, the Joint Economic Committee endorsed a real growth rate of 6 percent and agreed that a fiscal stimulus package in 1977 would substantially improve the prospects for economic growth. The Carter Administration had also drafted their original stimulus plan on the basis of achieving 6 percent real growth. Reflecting the withdrawal of the tax rebate proposal and a reduction in pace of Federal spending, the Administration now expects real growth in 1977 of only 4.9 percent. The recently announced energy plan of the Carter Administration may reduce the growth rate even further. We regret the impact that this reduction in the U.S. growth rate target is likely to have on domestic employment and on growth in other countries.

Despite modest recoveries from the recent recession, Japan, Germany, and the United States have made only limited moves toward fiscal stimulus. In part, this action reflects official expectations of relatively

high levels of economic growth in the year ahead. But it also reflects a broad-based apprehension about renewed inflation. Especially in Germany, but also in Japan and the United States, pressures for economic stimulation have been met by objections that additional stimulus would accelerate the rate of price increase. Inflation, it was argued, would increase business fears and further reduce already low levels of private investment in plant and equipment. In other words, additional governmental action would simply be self-defeating.

Fears of inflation, however, are probably exaggerated. High levels of unused capacity and unemployment suggest that there is little danger of additional inflation resulting from fiscal stimulus. Particularly in the case of the United States, the sudden jump in the Wholesale Price Index is mostly made up of increases in energy costs and a rise in agricultural prices caused by bad weather.

The danger for the world economy is that the three stronger industrial countries will all fall short of their targeted growth rates. If that should happen, not only will their own economies stagnate, but the payments position of the developing world and weaker industrial countries will become more serious.

1/ Senator Humphrey states: "I believe it is essential for the leading industrial nations to establish growth targets that will be sufficient to reduce the unacceptably high rates of unemployment which plague our economies. The restoration of full employment with relative price stability must be the first priority for our coordinated economic policies."

Structural Unemployment

All of the industrial countries are suffering from high levels of structural unemployment. As a first step, the problem of youth unemployment should be explored at an OECD-wide conference to be held in the fall of 1977.

As the industrial structures of the developed countries have become more similar, so have the economic problems -- persistent inflation, falling levels of investment, and high overall rates of unemployment. Throughout the industrial world there are large pockets of unemployment that are structural in nature, particularly among women, minorities, and young people. This problem does not respond readily to fiscal stimulus or eased monetary policy. There is one unemployment problem common to all the developed countries the severity of which demands immediate attention -- jobs for youth. Senator Humphrey and 18 other United States Senators have joined in sending a letter to President Carter calling for an OECD-wide conference on youth unemployment. Such an OECD conference could provide fresh impetus to reduce structural unemployment.

Trade Policy

<u>The December 31, 1977, target date for completion of the current General Agreement on Tariffs and Trade (GATT) negotiations should be extended. Congress and the Executive should cooperate in avoiding the erection of trade barriers and in assuring most-favored-nation access to U.S. markets. The OECD pledge against resorting to trade restrictions should be renewed.</u>

The Trade Act passed in December 1974 authorized the President to enter into a new round of trade negotiations with the objective of lowering tariff and nontariff barriers to trade in agricultural and industrial products. The first tasks for U.S. negotiators, once authorized to participate in what has come to be termed the Tokyo Round, were to agree with the representatives of other countries on how the multitude of individual issues was to be segregated for discussion purposes and on the priority assigned to each group of questions. Much technical preparation has been completed, including exchanges of tariff schedules, discussion of the merits and deficiencies of different proposed rules for reducing tariffs, and the elements of new codes of conduct regarding nontariff trade barriers. As the 1976 elections in the United States, Japan, and Germany approached, both American and foreign negotiators refrained from engaging in substantive negotiations on policy because neither could be confident that any agreement that was reached would be accepted by new political leaders.

During the Rambouillet summit meeting in November 1975, the objective of concluding the Tokyo Round of trade negotiations by the end of 1977 was accepted by the participating countries. This objective was reaffirmed at the Puerto Rico summit in June 1976. Given the limited progress, largely of a technical nature, that has been achieved to date and the need for the Carter Administration to formulate a comprehensive trade policy before the negotiators can begin to grapple with substantive issues, extending the deadline is appropriate.

The choice is one of concluding the negotiations by the end of this year and accepting a limited set of gains or of extending the negotiations within the January 3, 1980, deadline specified in the Trade Act of 1974 and attempting to achieve broader agreement as anticipated by the Act and the 1973 Tokyo Declaration. Significant progress in reducing tariff and nontariff trade barriers and in liberalizing agricultural trade, a chief U.S. interest, requires that the discussions continue beyond the end of 1977. Therefore, the previous target date should be set aside. In its place we should seek to establish a series of interim deadlines keyed to accomplishing each major step in the negotiations.

A number of U.S. domestic industries have appealed for relief from import competition, among them the shoe and color television industries. In both of these cases the International Trade Commission found that imports were in fact a source of injury. In the shoe case the Commission recommended imposition of a tariff-quota, and in the TV case a substantially increased tariff. President Carter rejected the Commission's

recommendation regarding shoes and asked the Special Representative for Trade Negotiations to conclude orderly marketing agreements with major producing countries that would reduce the volume of imports. Perhaps a similar solution will be sought regarding color televisions, especially since the Japanese Government has indicated its willingness to enter into such an agreement.

The President's decision on shoes has avoided the immediate imposition of a higher tariff on imports. But his preference for orderly marketing agreements has its disadvantages. Such agreements deprive producing countries of their right under the General Agreement on Tariffs and Trade (GATT) to demand an offsetting reduction in U.S. duties on other imports or to retaliate by imposing higher tariffs on American exports. From this country's point of view, therefore, orderly marketing agreements are apparently less costly, since we need not compensate foreign countries to account for the jobs and income lost through reduced exports to the United States.

Slow economic growth and high levels of overall unemployment have made it more difficult for workers and individual firms to adjust to rising levels of imports of shoes and television sets. A voluntary agreement may make it easier for the American economy to adapt now. But there are serious domestic costs. The Government collects no tariff revenues, and quantitative limits on imports raise prices to consumers. Purchasers of low-priced textiles, apparel, and shoes -- the type most directly affected by orderly market restraints -- are generally of modest incomes.

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An orderly marketing agreement to be effective requires the establishment of a global cartel in the particular product. Although these agreements are not intended to be permanent, once established they are extremely persistent and difficult to dismantle, as the history of orderly marketing agreements in fibers and textiles illustrates. Thus, consumers in importing nations as well as foreign workers who would have produced exports can suffer the consequences of such agreements for years, even decades.

The conclusion of additional orderly marketing agreements would perpetuate the trend toward bilateral solution of trade problems and further undermine the GATT. Since these understandings are generally concluded bilaterally, excluded third countries have little opportunity to represent their interests. Such agreements now exist in fibers and textiles, specialty steels, and a number of products the Japanese export to Europe, including steel, ball bearings, automobiles, certain electronic products, and ships. If this trend continues, the GATT will become so riddled with exceptions that it will no longer be a meaningful agreement.

The New York Customs Court recently decided that by failing to levy certain excise taxes on color television sets exported to the United States, the Japanese Government was subsidizing their sale to this country. The steel industry has brought a similar case regarding the application of the European Communities' value-added tax to steel exports to the United States.

The Court made its decision although it is the general practice of nations not to levy

excise taxes on exports and although non-application is sanctioned by the GATT. Indeed, this is the general practice followed by individual States and by the Federal Government. For example, the Federal excise tax on liquor is not applied to exports. The Common Market also does not apply its internal value-added tax to items that are sold to residents of nonmember countries.

This issue arises because the United States depends largely upon corporate and individual income taxes as the source of Federal revenues, while the European Communities rely upon the value-added tax. It can be resolved in a fashion that does not produce the seriously adverse consequences on trade flows that could conceivably result. The United States could modify its tax system, appellate courts could determine that nonapplication of excise taxes to exports does not constitute a subsidy, or GATT rules could be changed to permit nonapplication of corporate income as well as excise taxes on exported goods.

Trade with developing countries raises a different set of issues. The witnesses testifying, both spokesmen for developing countries and American economists, agreed without exception that one of the most important actions this country can take to help non-oil-producing countries counter the impact of high energy prices and to assist these nations in maintaining reasonable rates of growth is to keep our markets open to imports of their manufactured goods, as well as primary products. At the beginning of 1976 the United States implemented a Generalized System of Preferences (GSP) to assist developing countries in increasing their exports of manufactured goods to this nation. This system confers important benefits, particularly for nations that are

struggling to diversify their exports by selling manufactured goods abroad. For this reason, a system of preferences ought to be maintained. However, across-the-board tariff reductions would in the long run provide greater benefits to these countries. Hence, further expansion of preferences should be carefully examined.

Advanced developing countries and selected industries elsewhere in the Southern Hemisphere are becoming technologically competitive and soon will no longer require the benefit of preferences. These countries and industries should be assured continued access to U.S. markets on at least a most-favored-nation (MFN) basis. Negotiation of additional tariff reductions on an MFN basis can reduce or eliminate the obstacles industrial countries have raised against the processing of raw materials and manufacturing abroad.

Energy Policy

To reduce the pressure for higher world oil prices and to bring U.S. policies into agreement with the objectives of the International Energy Agency, Congress should act promptly to carry out the President's request to cut U.S. energy consumption and to develop domestic energy resources.

High energy costs remain the single most difficult economic problem for the industrialized countries. Quadrupling of oil prices in 1973, coupled with the supply disruptions of the Arab oil embargo, was a major cause of the economic recession in

1974-75. With recovery, demand for energy, and particularly oil imports, has risen again in all industrialized countries, continuing to aggravate the problem of payments imbalances.

In December 1976 the Organization of Petroleum Exporting Countries (OPEC) voted a 10 percent price increase. Saudi Arabia and the United Arab Emirates, however, split with the rest of the cartel by agreeing to hold their price increases to 5 percent and by unilaterally raising their own crude production to meet increased world oil demand. Whether motivated primarily by a desire for intra-OPEC leadership or a wish to bring pressure for peace in the Middle East, these two countries have shown serious consideration for the acute strains of higher oil costs on the world economy and deserve recognition for their responsible action. At the next OPEC meeting in Stockholm this summer, Kuwait and Iran have indicated they too may forgo a further price increase and produce a three-tier price system. The industrialized countries should continue to seek ways to encourage OPEC members to show restraint in future price increases.

The International Energy Agency (IEA) was formed following the 1974 oil price shock to bring the industrialized consuming nations together in a common front to deal with the oil producers. The IEA has succeeded in developing an agreement to share available resources in the event of emergency supply disruptions. It has further sought to promote cooperation in conservation, research, and development, and to consider joint guarantees for energy development schemes. According to the IEA evaluation, the United States has done substantially less well than Japan and most of Europe in its

conservation efforts. Lack of commitment in the United States to a serious energy program has been a major stumbling block to further IEA programs.

On April 20, President Carter announced a national energy program with stringent measures to cut domestic energy consumption over the next five years. While it is yet too soon to comment on the specifics of this program, we heartily endorse the President's strong leadership in announcing this tough program. Sharp reductions in the growth of U.S demand for oil imports are essential if we are to limit OPEC power to raise oil prices further. At the same time, the United States must move ahead on its program of stockpiling oil to reduce the potential impact of supply disruptions. In considering the President's program, we must give careful attention to minimizing the macroeconomic impact of higher energy costs. Appropriate measures must not be too stringent or phased in too rapidly lest they upset economic recovery at home and damage the world economy.

Exchange Rate Intervention and Adjustment

> The International Monetary Fund should promptly develop guidelines regarding market intervention and other government activities that influence exchange rates. Official intervention in exchange markets should be discouraged except to curb disorderly conditions. Moreover, to promote global balance-of-payments adjustment, the industrial countries with strong currencies should not resist pressures in exchange markets tending to raise the value of their currencies.

In contrast to 1976, self-interested intervention in exchange markets to manipulate relative competitive positions is not presently an issue among the major industrial powers. However, given continuing high unemployment rates and increasingly serious trade issues, the principle of refraining from the management of exchange rates to promote exports should be reaffirmed.

The individual member countries of the IMF are now approving amendments to the Fund Articles and a one-third increase in quotas. The Congress endorsed the amendments and quota increase in 1976. The ratification process should be completed by mid-1977.

The revised Article IV says, "The Fund shall exercise firm surveillance over the exchange rate policies of members, and shall adopt specific principles for the guidance of all members with respect to these policies." Recent policy of U.S. monetary authorities has been to avoid intervening in exchange

markets except as necessary from time to time to counter disorderly conditions. A manifestation of this policy is the new Foreign Currency Directive adopted by the Federal Reserve System on December 28, 1976, which states, "System operations in foreign currencies shall generally be directed at countering disorderly market conditions." The Joint Economic Committee has for some years maintained that disorderly conditions in exchange markets should be the sole grounds for intervention by U.S. monetary authorities and has urged U.S. officials to persuade the authorities of other leading industrial countries to adopt a similar policy.

In October 1976, the Subcommittee on International Economics conducted a hearing on guidelines for exchange market intervention. The purpose of this hearing was to investigate whether other industrial countries were intervening in exchange markets to hold down the external value of their currencies in order to expand exports. Of particular concern were Japan and West Germany, since both have strong export positions and both had occasionally intervened in exchange markets to prevent their currencies from appreciating. The extent of exchange market intervention by these two countries and the reasons for such intervention could not be clearly determined. However, it currently appears that if either nation had previously intervened in exchange markets on grounds that were not consistent with the revised Article IV, such practices have now been curtailed, if not eliminated.

Under the revised Articles of Agreement, IMF members shall undertake an obligation to "avoid manipulating exchange rates or the international monetary system in order to

prevent effective balance-of-payments adjustment or to gain an unfair competitive advantage over other members." Agreement to refrain from these practices is welcome, and the IMF should promptly establish guidelines or a set of operating procedures that will ensure against manipulation of exchange rates through market intervention, domestic monetary policy, tariffs, controls over capital movements, or any other governmental action that can affect exchange rates.

The strong currency countries can and should help deficit nations undertake the adjustments necessary to reduce their external payments drain. As discussed above, industrial nations can keep their markets open to imports of manufactured products from developing countries. The multilateral development banks, as is noted in the discussion below, can help finance the exploitation of new energy sources and encourage the growth of efficient export and import-competing industries. As a third factor in promoting desirable adjustments to reduce payments deficits, as distinct from deflation or protectionism, strong currency countries -- particularly Germany and Japan -- can choose not to resist but instead accept pressures in exchange markets tending to raise the exchange value of their currencies.

The witnesses from Germany and Japan endorsed such action. Both of these countries in 1976 accrued significant trade and current-account surpluses. These surpluses add to the financial strains already imposed upon weaker countries by high energy prices. Japan and Germany should follow the example of the United States in reducing their trade and current-account surpluses and should let the exchange value

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of their currencies rise whenever market transactions tend to push them upwards. To the extent that current-account surpluses persist, these countries should lend readily to deficit nations through commercial channels and via participation in the International Monetary Fund and contributions to the multilateral development banks.

Balance-of-Payments Financing

> Even with the increase in quotas due to be approved this year, the International Monetary Fund's pool of lendable currencies could soon be depleted. Strong currency countries, including the United States, should contribute additional resources to the Fund that will be available to all members under conditions the IMF establishes.

Total payments deficits of non-oil-developing and weak industrial countries in 1977 will total between $30 and $40 billion (Table 1). These deficits come on top of sizable deficits for the last four years. At the same time, commercial bank lending to these countries may stop increasing and could even decline somewhat this year. Therefore an increasing burden is likely to be placed on the IMF to provide balance-of-payments financing and to enable borrowers to avoid deflationary or protectionist reactions to their difficulties. How these continuing payments are to be financed will be a subject of discussion at the London summit conference.

TABLE 1: Current-account balances

(Billions of U.S. dollars)

Group of countries	1973	1974	1975	1976[1]	1977[2]
OECD	2½	-33	-6½	-23	-25
OPEC	3½	70½	39½	41	45
Non-oil developing countries	-2½	-21	-29½	-20	-22
Other countries[3]	-4	-9½	-15½	-12	-14
Unexplained discrepancy	½	-7	12	14	16

[1]Partly estimated.
[2]Projection
[3]Sino-Soviet area, South Africa, Israel, Cyprus, Malta, and Yugoslavia.

Sources: Department of the Treasury, Organization for Economic Cooperation and Development (OECD), and Council of Economic Advisers

The Fund currently has about $4 billion worth of lendable hard currencies. The quota increase due to be approved in a few months will add approximately $5 billion to usable IMF resources. Last year the Fund lent about $8 billion, up from $5 billion in 1975. Since drawings are likely to increase in 1977, available resources plus loan repayments would permit the IMF to function for only about 18 months. Additional funds totaling about $3 billion are currently available through the IMF's General Arrangements to Borrow (GAB). But this supplementary facility is available to only the ten major industrial countries, and it too could soon be depleted. More of a cushion is necessary.

During the 94th Congress, the Executive submitted for legislative endorsement a proposed $25 billion OECD Financial Support Fund. The congressional reaction to this proposal was cool. Although hearings were held in the Senate, the legislation was never reported to the Senate floor. No action was taken in the House of Representatives. This proposal, along with all other pending legislation, died with the conclusion of the 94th Congress.

There is little reason to expect that the OECD Financial Support Fund proposal would fare better in this Congress if resubmitted. Indeed, this proposal was fashioned primarily in reaction to the quadrupling of oil prices, and changes in conditions since that time have made the proposed facility less useful than it might have been earlier. The problem of paying for oil imports is now recognized as an important, but certainly not the only, source of international payments disequilibria. Inflation, business cycle variations, and fluctuations in commodity

prices are also contributing causes. Payments financing should be available to meet all of these difficulties equally.

Lending under the OECD Financial Support Fund was to be conditional on the borrowing nations' efforts to reduce energy consumption and to develop alternative supplies. The conditions attached to loans for financing payments deficits should also include an IMF-type requirement that the borrower adopt appropriate macroeconomic policies. The Fund's staff is experienced and well-qualified to establish the conditions associated with balance-of-payments loans and to enforce these requirements. To give another institution authority to engage in balance-of-payments financing and require it to assemble a staff to perform the same functions as the IMF would entail a wasteful and possibly disruptive duplication of effort. The International Monetary Fund is the appropriate institution to mobilize additional resources for official financing of payments deficits, to establish the conditions under which member countries may utilize these funds, and to disburse them.

How can IMF resources be expanded? Another quota increase would have the advantage of enlarging the potential drawing rights of all Fund members and should be considered. But it would suffer from the disadvantage that many of the currencies paid in as additional quota subscriptions are not readily lendable. Moreover, quota expansions require two or three years to negotiate and implement. The existing GAB is limited in that several of the countries that were potential lenders when the mechanism was established currently have weak external payments positions and are consequently no longer able to lend. A more suitable

supplementary source of resources for the IMF would include strong industrial countries and surplus oil-producing nations as contributors and would provide funds that could be lent to any Fund member for periods of up to two or three years. The conferees at the London summit should endorse the immediate creation of such a super-GAB.

In the last two years, the International Monetary Fund has lent vastly more through its regular resources than previously. OECD countries -- like the United Kingdom, Italy, and Portugal -- have borrowed from it both under the Oil Facility and the regular credit tranches. The number of developing countries turning to the Fund for balance-of-payments assistance, both under regular credit programs and those designed to meet their particular problems, like the Compensatory Financing Facility, is likely to grow in the immediate future.

While commercial banks were able to play an important role in financing deficits in the first years following the oil price increases, there is now growing concern about how much they can prudently further increase their exposure. At the end of 1976, approximately $80 billion was owed by non-OPEC developing countries to all commercial banks; overall external debt of non-oil-developing countries was estimated at $180 billion. While several developing countries are currently seeking rescheduling of their credits, a consensus of both public and private sources is that there is no serious prospect of default at this time.

Federal Reserve Board Chairman Burns has suggested that the International Monetary Fund play a greater role in both monitoring commercial bank credits to individual

countries and in assisting these countries to formulate appropriate stabilization policies. While there may be some disadvantages in putting all of the responsibility in one institution, this proposal should be explored thoroughly.

Increased resources for the IMF and suggested expansion of its role as guide for commercial bank lending to developing countries has focused attention on the kind of policies that the IMF pursues to promote economic stabilization. IMF programs have traditionally been short term (a year to 18 months) and have focused on bringing about balance-of-payments adjustment.

It is becoming evident that the adjustment process may be more complex than initially perceived. Sometimes inflation must be curbed, new energy sources must be developed and conservation implemented, recession must be combatted, or realistic exchange rates must be adopted. At other times structural adjustment in a particular sector may be necessary. The Extended Fund Facility was set up for the purpose of financing structural adjustments requiring several years to complete.

With the increasing activity of the Fund, questions have been raised about whether the same standards can, or should, be applied to all potential borrowers. Fund policies may have been too restrictive in some cases and too lenient in others. The Fund should reexamine the criteria behind the policies it employs. Within the confines of available resources, it should seek to pursue policies that are not excessively deflationary. However, the IMF should only finance problems that have foreseeable solutions.

Achieving a More Equitable Economic Order

Three weeks after the London summit, the industrialized and developing countries will meet at another session of the Conference on International Economic Cooperation (CIEC). CIEC has been one of the principal forums for discussing a broad array of issues raised by the developing countries since 1974.

The developing countries have born a disproportionate burden of current-account deficits resulting from the quadrupling of oil prices and the subsequent slowdown in the industrial economies. Efforts of the strong industrial countries to reflate their economies, to conserve energy, to curb trade surpluses, and to refrain from imposing protectionist trade barriers will benefit the poor countries.

Since OPEC raised prices, discussions between industrial nations and developing countries have become focused on demands of the poor for a new international economic order that would distribute the benefits of economic growth more equitably. While there is general agreement that some greater equity should be achieved, there is little agreement among poor countries on exactly how such a restructuring of the world economy might be achieved. The developed countries, on the other hand, have not been able to propose measures to assist the poor countries in the way that satisfies the latter group. Over the last three years, meetings in numerous forums on these subjects have deteriorated into rhetorical posturing and broken down over specifics.

Despite the seeming repetitiveness and lack of accomplishment in this "North-South"

dialogue, significant changes in economic policy and institutions have been initiated by the industrialized countries to benefit the poor nations. These initiatives are (a) expansion of the IMF Compensatory Financing Facility used to offset shortfalls in export earnings due to commodity price fluctuations; (b) establishment of the IMF Trust Fund to subsidize balance-of-payments loans to the poorest countries with the proceeds of IMF gold sales; (c) a shift to a greater willingness on the part of the United States to negotiate commodity price stabilization agreements; (d) establishment of a compensatory financing facility under the Lome Convention between members of the European Communities and countries in their former colonial areas; and (e) extension of trade preferences for imports of manufactured goods from developing countries by the United States, the European Communities, Japan, and Australia.

On the part of the developing countries, the discussion has produced some more realistic redefinition of the issues. For example, demands for generalized debt relief have largely been dropped. The Group of 24 communique issued at the IMF meetings in Manila in October 1976 reflected the concerns of the more advanced developing countries about maintaining their own access to capital markets and did not demand a general debt moratorium. These countries, nevertheless, do continue to be concerned with the need for debt relief for the poorest nations.

At the summit the industrial countries will be considering what they can and should do for developing nations. Some of the demands raised under the new international economic order -- indexation of raw material prices or a common fund to stabilize the prices of

unspecified commodities, for example -- are clearly not in our interest nor that of a viable international economic system. Other demands of developing countries may make greater economic sense, such as aid transfers, but they require budget commitments within the United States that are difficult, given competing demands. Moreover, the developing countries must themselves adopt appropriate domestic economic policies to be able to take advantage of opportunities when they arise.

In considering remedies to problems the poor countries face, we should seek solutions that mutually benefit both the industrialized and developing nations. Only if we can create a healthy and growing world economy will we be able to accommodate the needs for greater equity of those who have been disadvantaged. Probably the most important single benefit to developing countries would come from the expansion of trade mentioned above.

<u>Commodities</u>

> <u>To protect poor countries from sharp fluctuations in export earnings, the United States should continue to consider, on a case-by-case basis, commodity price stabilization agreements, additional needs for compensatory financing, and the adequacy of resources for diversifying exports. In discussing proposals for joint funding of buffer stocks, the United States should not agree to commit funds unrelated to the establishment of specific commodity agreements or to any attempt to raise prices above market trends.</u>

Commodity agreements and the stabilization of the export receipts of developing countries in order to promote uninterrupted growth remains a key issue in the North-South dialogue. The developing countries want to reverse the decline in the terms of trade of raw materials that they have experienced; they see agreements to stabilize earnings in these commodities as critical to achieving this goal. The Integrated Commodity Program proposed by the United Nations Conference on Trade and Development (UNCTAD) would set up a common fund to finance buffer stocks for a core of 18 commodities as they are negotiated.

With a growing recognition of the need for stable export earnings to assure continuing development, the United States has been willing to consider commodity price stabilization agreements on a case-by-case basis. Over the last year, the United States

Government signed and ratified agreements in coffee and tin and indicated its interest in participating in the pending cocoa agreement if specific price levels are renegotiated. We are currently participating in several UNCTAD discussions for other commodity agreements.

Commodity agreements to stabilize prices around an underlying trend could facilitate planning both in the developed and the developing countries and help control inflation. Identifying and agreeing upon this underlying trend of market equilibrium prices, however, is extremely difficult, and there are added problems in policing any commodity arrangement. On the other hand, agreements that fix prices at levels above the long-run market-clearing equilibrium, or that seek to transfer resources by maintaining artifically high prices would not be successful in providing the development benefits sought by poor countries. Such agreements would lead to substitution of alternative products, uneconomic investments, and threats of politically motivated trade restraints.

Because of the difficulties in negotiating individual commodity agreements, the United States has favored stabilizing export earnings rather than prices. The IMF Compensatory Financing Facility was expanded for this end. The United States has also recognized the need to find individual solutions for particular commodities. In some cases, chronic oversupply has led to a declining long-term price trend; then diversification into other crops and manufactured exports is the only way to stabilize export earnings. In other instances, the difficulty of storing

agricultural commodities makes buffer stocks inappropriate.

When and if suitable stabilization agreements that benefit both producers and consumers have been negotiated, adequate funding will probably be forthcoming. Since joint financing of several stocks could be more efficient than independent financing, such possibilities should be explored as soon as enough agreements have been reached. Attempting to appropriate monies for a common fund before concluding the individual agreements would unnecessarily complicate commodity price stabilization negotiations.

Multilateral Assistance

The multilateral development banks should assist the developing countries' adjustment to higher energy costs by financing projects to exploit domestic energy resources and to create efficient export and import-competing industries. The United States should eliminate the arrearages in its pledged contributions to the multilateral development banks and should authorize a $2.4 billion contribution to the Fifth Replenishment of the International Development Association.

The poor countries need aid at concessional terms. According to the World Bank, per capita annual incomes for the 30 poorest countries still average less than $160 while those in industrialized countries average over $5,000. Without transfers of real resources financed by concessional aid from the industrialized nations, few developing

countries can look forward to steady economic growth, since they are not yet able to rely entirely on private capital flows and the benefits of trade.

Higher oil costs severely aggravated the payments deficits of the developing countries. These countries were initially able to forestall necessary adjustments by spending their reserves, borrowing heavily in the private capital markets, and drawing on the emergency programs of the International Monetary Fund. Because many of these countries are nearing their borrowing limits and their deficits are expected to persist, serious attention needs to be given to how these countries can meet higher import costs without relinquishing the goal of continuing economic growth.

The multilateral banks can play an important role in assisting the developing countries' adjustment to higher import costs. In close cooperation with the International Monetary Fund, the development banks should provide financing to foster efficient export- and import-competing industries. They should also seek ways to help poor countries develop competitive domestic energy resources and thereby reduce energy imports.

If the multilateral development banks are to continue helping the poor nations grow and encourage constructive adjustments to payments difficulties, they will need additional capital contributions. The Inter-American Development Bank agreed upon its capital increase last year and the World Bank and the Asian Development Bank are currently seeking capital increases from donor countries. The Fifth Replenishment of the International Development Association (IDA V), agreed to in March 1977, will provide

$7.6 billion over the next three years in concessional assistance for the very poorest nations. Congress should move quickly to appropriate funds for IDA V and for the agreed capital expansions.

Even with these increased resources, all the development banks must give continuous scrutiny to the quality of the projects that they fund as available resources -- even though seemingly large -- will fall short of the needs of the poorest countries. In addition, attention must be given to ensure that the recipient countries not only meet necessary criteria of creditworthiness, but that they pursue domestic policies generally supportive of the goals of growth, equity, and the improvement of the human condition that underlie our humanitarian support of development efforts.

Support of the International Development Association (IDA) -- the soft loan window of the World Bank -- is particularly important to demonstrate the seriousness of the U.S. commitment to help the Third World. In the past several years, Congress has been slow in providing funds for IDA; in fiscal year 1976 we actually fell behind on our commitment to IDA under the Fourth Replenishment by not appropriating the full amount authorized. Although our portion of the Fifth Replenishment Agreement appears large, as it must be if IDA is to maintain the real value of its ongoing lending, our percentage share continues to decline. While meeting our remaining commitments under the Fourth Replenishment, the United States should strive to commit new funds in step with other donors.

OPEC Participation

The industrial countries should encourage the OPEC countries with large financial reserves to participate more fully in the international lending institutions. OPEC and multilateral development bank aid programs should be coordinated in order to maximize the effective use of available resources.

The OPEC nations have increasingly participated in funding the development banks through contributions and purchases of bonds. This year the oil producers have pledged modest contributions to IDA V. The OPEC nations with financial surpluses however should be encouraged to play an even larger role in the IMF and the multilateral development banks. As mentioned above, these countries should be encouraged to contribute to any expanded super-GAB facility that is approved.

OPEC donors should also be asked to join with the OECD Development Assistance Committee in coordinating aid projects. Whenever suitable, projects should be financed jointly among private investors, the development banks, and OPEC aid institutions.

ADDITIONAL VIEWS OF SENATOR JACOB K. JAVITS

In general this report is well written and contains constructive suggestions for guiding the Administration at the forthcoming May 1977 Summit Conference. I wish particularly to emphasize the recommendations on structural unemployment, the pledge against resorting to trade restrictions, guidelines regarding market intervention, strengthening the resources of the International Monetary Fund (IMF) and the multilateral development banks, and encouraging greater participation of surplus OPEC countries in the international lending institutions.

The first recommendation of the Report, that "The leading industrial countries should commit themselves to agreed growth rate targets and to the use of policies necessary for assuring the realization of these objectives," reflects an unrealistic view of the situation. In my view, the governments of other industrialized countries such as Germany and Japan are not in a position to -- and are highly unlikely to -- take this rigid a view of committing themselves to specific economic growth rate targets.

At the present time the OECD and the Working Party Three afford excellent forums for Cabinet and Sub-Cabinet level coordination of domestic economic policy actions by the OECD member countries. However, I believe that international interdependence has reached the level where activities of this kind must be carried on at the highest political level.

Several references are made in the report to the need to promote freer trade and to encourage trade as an instrument of economic development, and I agree with the recommendations incorporated in these analyses. But, I believe that the role of private enterprise in international development and in the development of the less developed countries is consistently understated and underemphasized.

The national development plans of less developed countries continually rely on large infusions of private capital. These infusions in turn depend on what has now become an extraordinarily sophisticated and efficient worldwide mechanism for transferring funds, resources and technology vast distances in order to produce and to employ persons all over the world. The LDC critics of multinational corporations and international banking activities are often, as citizens of the world, major beneficiaries of that system.

While I do not believe that competition condones the alleged malefeasance of some international corporations, the fact is that roads, harbors, health care supplies, communications equipment, educational materials, and billions of dollars of other goods and services have found their way to the LDC's through their activities. The thrust of our foreign economic policy, therefore, should be to develop incentives for further liberalizing trade patterns with the LDC's as an integral aspect of our policies towards those countries.

In my view, the issues raised by the call for a New International Economic Order form the key economic -- and therefore, political -- world issues of the coming decade or

decades. Therefore, policy must aim at providing the incentives for private sector growth in such a way as to "internationalize" the mentality of U.S. business -- large and small.

I have some misgivings over one aspect of the report's analysis. While I agree with the fact that the International Monetary Fund is the appropriate institution for mobilizing additional resources for official funding of payments deficits, I do not agree with the implication of the report that the United States should abandon the proposal for the $25 billion OECD financial support facility. Although, as the report points out, the reception to that proposal in the United States Congress has been cool, the fact is that other OECD countries have enacted or have in place legislation authorizing participation in such a facility.

The need for flexibility in coping with the balance of payments difficulties of both the less developed countries and the weaker industrial countries requires that different financial institutions with different capabilities be put in place, much as business itself has developed new forms of enterprise to deal with the opportunities of world trade. The new, so-called Witteveen Facility proposal recently taken up at the Interim Committee Meeting of the International Monetary Fund, has some practical advantages over the OECD financial support facility, and my views are not meant to recommend a substitute of the latter for the former. However, the OECD facility represents an agreement which has already found considerable acceptance and which would implement the principle that oil payments imbalances between OPEC and the world's industrialized countries can be resolved by

SUPPLEMENTARY VIEWS OF REPRESENTATIVE CLARENCE J. BROWN REPRESENTATIVE GARRY BROWN AND REPRESENTATIVE JOHN H. ROUSSELOT

While we agree with several of the recommendations in the Committee Report, there are others to which we take exception.

The first is the recommendation that "The leading industrial countries should commit themselves to agreed growth rate targets and to the use of the policies necessary for assuring realization of these objectives."

What the Committee really means by this is something less innocuous. The recommendation should be translated to read, "Japan and Germany should be pressured into deficit spending and faster money creation in order to eliminate their current account surpluses. They should expand their economies more rapidly to encourage imports, in order to help stimulate the economies of the rest of the world by running balance-of-payments deficits."

Should We Pressure Germany and Japan?

We feel that the governments of Germany and Japan know far better than anyone else just how far they can go in expanding their economies before they run into socially and economically unacceptable inflation, with its attendant risk of recession and unemployment. It is not our place to make such a recommendation.

Could Such Pressure Help?

Even assuming that Germany and Japan were willing to try to reduce their current account balances by $5 billion each, would it help the worldwide economic recovery? No. The size of the impact must be minor.

German trade is roughly $100 billion of imports or exports a year, out of a gross national product (GNP) which will approach $500 billion this year. Thus, one-fifth of German spending is for imports. To get an extra $5 billion increase in imports, in addition to what is expected to occur, German GNP must grow by an extra $25 billion this year above the amount anticipated. The amount anticipated is already about $25 billion (5 percent of $500 billion). If Germany needs to grow by another $25 billion, that implies a doubling of her real growth rate to 10 percent per year. What fiscal or monetary policy could work that kind of miracle?

Japan, which has let the yen rise sharply for months, and which is not expected to have a current account surplus in 1977, is surely not guilty of misbehavior. Nonetheless, it is being urged to run a deficit of a few billion, say $5 billion, to help the Third World. Japan's imports are only about one-eighth of a GNP of nearly $600 billion, so that Japan would have to add an extra $40 billion to GNP to bring about an extra $5 billion in imports. Coincidentally, Japan is already growing by about $40 billion a year, or at a rate of 6 percent. Thus, like Germany, it would have to double its growth rate to provide a $5 billion deficit for the benefit of other countries.

Suppose that these countries could, in fact, return to fixed exchange rates, double their growth rates, and cause a $5 billion reduction in Germany's current account surplus, and a $5 billion current account deficit for Japan. Would this help?

Germany's $5 billion would be only one-tenth of one percent of the Free World's GNP of $5 trillion. Adding Japan, we get an increase in demand of two-tenths of one percent. This is truly negligible. Furthermore, most of that will flow to their major trading partners, the United States, Britain, France and Italy. Two of these, Britain and Italy, will simply use part of the money to repay debt while maintaining their austerity programs. This proposal does next to nothing for the Third World.

The Impact on Borrowers in the Third World

As implied above,Germany and Japan can be expected to run an actual payments deficit only under fixed exchange rates. There are a vast number of conceptual problems in saying that a country can run a balance of payments deficit while on floating exchange rates. (While both the German and Japanese floats have been "managed," both the mark and the yen have been allowed to rise significantly over the past year or more.)

Over the past year, both nations' current account surpluses were largely offset by capital account deficits (lending abroad). That is how the balance of payments balances under floating rates.

The implication of the Committee's recommendation that Japan and Germany continue with floating exchange rates <u>and</u>

eliminate or reverse their current account surpluses is that they ought to eliminate or reverse their capital account deficits -- that they should stop lending and start borrowing! Such a policy might aid those Third World nations which would furnish exports to Germany and Japan. However, it would injure those which are deepest in debt and need to restructure or renegotiate their loans. These countries do not want to see an end to German and Japanese lending. Still less do they want to compete with German and Japanese borrowing! This problem was not dealt with during the hearings.

Exchange Rate Adjustments

Later in the report, the Committee recommends that "industrial countries with strong currencies should not resist pressures in exchange markets tending to raise the value of their currencies." We agree. However, the Committee is implying that Japan and Germany have held down the values of the yen and the mark, and that this has contributed to their current account surpluses.

In recent years, both the yen and the mark have risen substantially, with no noticeable impact on the current account balances of either country.

The mark has risen more than 10 percent with respect to the dollar since the beginning of 1976. The yen has risen more than 7 percent. Germany is participating in the EEC currency snake, or joint float. This has somewhat curtailed the free movement of the mark. Nonetheless, substantial increases have been realized.

It is the conclusion of many international trade theorists that devaluations and revaluations have no permanent impact on a country's trade balance.

Old style devaluation theory stated that devaluations could help a country's trade balance, as follows:

"Suppose Britain devalues the pound by 10 percent, and that all British products continue to sell at the same number of pounds as before the devaluation. Then the price of imported wheat in terms of pounds goes up 10 percent, discouraging wheat imports, and British steel looks 10 percent cheaper to foreigners in terms of their own currencies, encouraging British exports of steel. If the effect is strong enough, Britain's trade deficit shrinks. (All this assumes fixed exchange rates, of course, such as under the Bretton Woods system.)"

Modern devaluation theory says:

"That is a nice first step, but will Britain's pound price of wheat and steel stay constant, or of any other product either?" The answer is "no."

British steel was always sold partly in Britain and partly abroad. It could have been sold entirely abroad, but since the British price equaled the world price, some was sold at home. Now, however, foreign steel is selling for 10 percent more, in terms of pounds, overseas. If any steel is to be sold in Britain, the pound price of steel must rise 10 percent, or all of it will be exported.

Similarly, foreign and British producers of wheat would charge the world price, which

enables them to command the same purchasing power over foreign (and domestic) steel (i.e., all other products) as before. That is, wheat would sell for 10 percent more in terms of pounds after devaluation.

This rise in the pound price of all trade<u>able</u> goods (whether actually trad<u>ed</u> or not) <u>is</u> followed by an equal rise in the price of British haircuts and other non-tradeable goods. Why? Because nothing has changed the <u>real</u> costs of haircuts versus wheat versus steel, or the public's view of them. If people tried to shift purchases away from the now more expensive steel and wheat into haircuts, the price of haircuts would rise until it was back at the same relative price, compared to steel and wheat, as before.

The conclusion is that devaluation of "x" percent does not permanently alter the trade balance. It simply reflects a simultaneous inflation of "x" percent, <u>or triggers one</u>. On the other hand, a rise in the value of a currency of "x" percent reflects a reduction of "x" percent in the rate of inflation, or helps to bring it about.

The Committee's recommendation is not going to produce the results it assumes.

<u>Commodity Price Agreements</u>

The Committee recommends that "To protect poor countries from sharp fluctuations in export earnings, the United States should continue to consider... commodity price stabilization agreements."

This is a plan to help the Third World indirectly, instead of directly through grants, loans, or freer trade.

The neediest of the Third World countries will need grants to get them through the energy crisis. Those among them and those among the more developed Third World nations with sound plans for permanent growth and adjustment, deserve to be able to get loans to tide them over, either from private banks or from an expanded International Monetary Fund (IMF) or International Bank for Reconstruction and Development.

However, we are now being asked to create a price support program for commodities as part of a long-run solution. As several witnesses noted, this will not bring about efficient development or industrialization of the Third World. It will only create increased dependence on one or two commodities for countries which are already too dependent on this type of production. It would tie up their resources producing commodities for storage instead of valuable goods for trade.

The alternatives of grants, lower tariffs, private investment and multinational lending are to be preferred to commodity price fixing plans.

If commodity stabilization funds are necessary, one should be established for each commodity, as President Carter suggested in his address on Latin America. If one fund were to be established for all commodities, as the Third World has proposed, the various Third World countries would be tied up in knots for years bargaining over how much of the fund would go to support each commodity, and what the support price should be. For

example, Third World nations heavily dependent on coffee production and tin imports would want a large coffee fund with a high support price, and a low tin fund with a low support price, while tin producers who import coffee would want the converse.

Efforts at Self-Help

The implication of some of the witnesses that the developed world has exploited and suppressed the Third World has to be challenged. The United States is more than 90 percent self-sufficient. We import or export less than 10 percent of our GNP. And, what we import, we pay for with exports. We do not seize products, or conduct trade, at gunpoint.

Therefore, we feel it proper to ask the question, "What has the Third World done to help itself?"

Some of these countries have welcomed foreign investment. Some have not.

Some of them have removed exchange rate and foreign exchange controls. Some still stifle their own financial markets.

Some of them have low tax rates and never threaten to nationalize industries. Some scare private help away through threats and political instability.

Some of them allow investment in a normal, honest fashion. Others impose enormous taxes on business in the form of red tape and bribe-taking, which costs multinational companies money and gets them into political trouble at home.

One of the witnesses remarked that "governments feel that it is their business in some measure to choose the pattern of political-economic organization." That is true, provided they are willing to take the consequences. If their political-economic form of organization discourages self-help and private assistance, do they have as much of a claim on foreign sympathy as do those countries which seek private development and encourage self-help?

We should not forget that the Government of the United States is also free to choose its pattern of "political-economic organization." The United States has every right to decide that its own "pattern" is best served by favoring nations which have encouraged their own development and sought after private investment before applying to the U.S. Treasury, over those which have made a bee-line for the money of American taxpayers.

Mrs. Anne Krueger testified that, "No matter what the external environment, or the level of resource transfer, anything that represents a genuine step forward in raising productivity and living standards of the people is going to require at least 90 percent of the inputs from domestic efforts."

We concur, and we are more than willing to help, in as efficient a manner as possible, those nations which share that view.

SUPPLEMENTARY VIEWS OF SENATOR ORRIN G. HATCH

I support the reservations expressed in the Supplementary views of Rep. Clarence G. Brown, Rep. Garry Grown, and Rep. John H. Rousselot, and I would like to express some additional concerns.

It seems to me that implicitly the Committee Report is recommending world inflation and international price-fixing. Both would, of course, increase the economic misallocation of the world's resources and lessen human welfare.

The scheme to establish price supports for Third World commodities will cause a wasteful misallocation of their scarce resources into the overproduction of the price supported commodities at the expense of their economic development.

The scheme to reflate the domestic economies of the United States, Germany, and Japan will turn these net suppliers of international loans into net borrowers of international loans. To dump the United States, Germany, and Japan into the already crowded international market for loans will only make the financial situation of Third World, large debtor countries more difficult.

Already Italy and Britain have trade deficits and to cover them they have to compete against Third World countries for international loans. If we pressure Germany and Japan out of their trade surpluses and into trade deficits, they also will have to compete against Third World countries for international loans. Every country cannot be a debtor country. The economically

underdeveloped Third World countries need to be debtor countries, because they need to import investment. Therefore, come countries elsewhere must have trade surpluses in order to be able to supply loans.

Germany and Japan cannot simultaneously have trade deficits and supply loans except by transferring their foreign exchange holdings as gifts to the Third World. This would require flexible exchange rates to be abandoned and the German and Japanese central banks to peg the foreign exchange rates of the mark and yen. Otherwise, the exchange rates of the mark and the yen would move, until the payments deficits were eliminated.

If Third World countries want grants, they should ask for them outright instead of concocting inefficient schemes that will reduce their economic development prospects. Our response to these requests must be based on their economic merit and not on any alleged moral compulsion. We have no obligation to lands whose economic opportunities are largely foreclosed by the nature of their political and economic systems and by the absence of extensive and secure private rights to property. We have no obligation to subsidize lands whose only elite is the government class that rules.

On the other hand, those countries that seek to extend economic opportunity to their citizens, rather than restrict it to government, will find that the opportunities created by the energies of private people will generate helpful investment and support from people abroad.

HEARINGS ON ISSUES AT THE SUMMIT

GROWTH, TRADE AND ENERGY
April 20, 1977

GERASSIMOS ARSENIS
Director, New York Office of UNCTAD

ARMIN GUTOWSKI
Member, German Council of Economic Experts, Frankfurt am Main, Germany

SABURO OKITA
Special Advisor, International Development Center of Japan, Tokyo

GEORGE POULIN
Vice-President-elect, International Association of Machinists and Aerospace Workers, Washington, D.C.

ROBERT V. ROOSA
Partner, Brown Brothers Harriman and Company, New York

J. ROBERT SCHAETZEL
Consultant and Writer, Washington, D.C., Former U.S. Ambassador to the European Communities

BALANCE-OF-PAYMENTS FINANCING AND ADJUSTMENT
April 21, 1977

RICHARD S. ECKAUS
Professor of Economics, Massachusetts Institute of Technology

PETER B. KENEN
Professor of Economics and International Finance, Princeton University

WILLIAM J. McDONOUGH
Executive Vice-President, First National Bank of Chicago

ISSUES IN NORTH-SOUTH DIALOGUE
April 22, 1977

LAWRENCE S. KRAUSE
Senior Fellow, Brookings Institution, Washington, D.C.

ANNE O. KRUEGER
Professor of Economics, University of Minnesota, Minneapolis

JOHN P. LEWIS
Professor of Economics and International Affairs, Woodrow Wilson School, Princeton University

SRIDATH S. RAMPHAL
Secretary-General, Commonwealth Secretariat, London

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