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World trade collapse sets the stage for trade war

by David Goldman

It might be said in defense of the disastrous 1929 Hawley-Smoot tariff, that its framers were fighting for a greater share of a world trade volume then still at relatively high levels. Secretary of State George Shultz, Trade Representative Clayton Yeutter, and their correspondent trade-warriors on the European side, have no such excuse. Their policies have already collapsed world trade, and their emulation of Hawley-Smoot merely uses the trade collapse for political provocation.

The scale of the present disaster may be summarized in the following comparison:

During the world economy's last period of growth, between 1973 and 1979, total world trade *tripled*, from $523 billion to $1.5 trillion. Higher oil prices accounted for only $70 billion of this growth; in contrast, the exports of industrial nations rose from $387 billion to $1,074 billion. In periods of growth, world trade grows much faster than economic growth as such, because the introduction of new technologies makes the world division of labor more complex.

That was during the 1970s, when the United States still produced 140 million tons of steel per year. Now, we produce fewer than 70 million tons of steel, and world trade is *lower* in absolute terms than it was in 1981.

In 1980, all the world's nations exported a grand total of $1.9 trillion in physical goods. By 1983, the volume had fallen to $1.67 trillion, or about 12% less than the 1980 total. At the height of the supposed "recovery," in 1985, world exports were only $1.72 trillion, still 10% lower than the 1980 level. During the 1975-80 period, world trade had *grown* by 5% a year.

The true position of world trade is even worse than the numbers show. To start with, American imports rose from a total of $256 billion in 1980, to $361 billion in 1985. These imports, bought at 40% to 70% below American producer prices, merely replaced production capacity we lost at home. In other words, the increase in U.S. imports reflects, not economic growth, but decay. Total world trade in 1985 minus the $104 billion increase in U.S. imports was only $1.663 trillion, lower than the supposed nadir of international trade in 1983, when exports fell to $1.667 trillion.

Discounting the bloating of America's import bill, the fall in international trade since 1980 amounts to 19%—not quite as bad as the worst of the 1930s, but grim by any historical standards.

In fact, American imports grew from a steady 14% of total world imports between 1977 and 1981, to 19% of the total in 1986, corresponding to the collapse of American industrial capacity. In absolute terms, American imports more than tripled between 1977 and 1986, from $120 billion per year, to $380 billion per year.

During the same period, the United States lost:

- Half of its steel production;
- More than half of its non-ferrous metals production;
- Half of all construction expenditures for economic infrastructure;
- Nine-tenths of its expenditures for utilities construction;
- A fifth of its automobile output;
- A fifth of housing construction;
- More than half of farm-equipment production;
- More than half of machine-tool capacity.

And so forth. What this country can no longer produce, it imports from abroad.

Not only has the volume of world trade declined; as in 1930s, prices in world trade have collapsed along with volume. The International Monetary Fund's comprehensive in-

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dex for commodity prices, which sets the 1980 value at 100, stood at less than 70 as of October 1986. That is, commodity prices have dropped by more than 30% since 1980, comparable to the worst of the 1929-35 period.

The end of the subsidy

American imports now amount to 20% of total domestic physical consumption, and 25% of new capital goods purchases. The financing of the subsidy depended upon two factors:

1) The enormous increase in the dollar's value between 1978 and 1984, when it rose from DM 1.80 at its low point to DM 3.30 at its peak. This permitted the United States to purchase foreign goods at 40% below the comparable cost of production.

2) The evolution of a captive "dollar bloc," comparable to the colonial "sterling bloc" of the 1930s, which then permitted Great Britain to purchase raw materials with a pound valued at artificially high levels with respect to the Empire, despite the pound's falling value against other industrial nations' currencies.

Of course, the dollar's fall to the neighborhood of DM 1.90 in the past several weeks underscores the difficulty of maintaining purchases from Japan and West Germany under present conditions. The enormous increase in the U.S. trade deficit, from about $150 billion in 1985 to an annual rate of $230 billion in November 1986, reflects not so much an increase of purchases, as the higher cost of these purchases.

However, as the Dallas Federal Reserve has pointed out, the dollar has fallen only by 6.4% against the average of its trading partners' currencies, and the weighted average of the fall is less than 10%—compared to the 40% declines against the German mark and the Japanese yen. That is because the "dollar bloc," including Taiwan, South Korea, Brazil, and other important developing-sector trading partners of the United States, has kept its currencies falling with the dollar.

That has led to some remarkable financial distortions, including the accumulation by Taiwan of $25 billion of U.S. Treasury securities since January 1986. That reflects speculative purchases of the Taiwan dollar, which has lost so much value against the Japanese yen that it will soon have to leave the "dollar bloc."

In Ibero-America, exporters have had to accept prices for their manufactured goods at 70% below comparable U.S. cost of production, at the expense of 10% to 20% reductions in living standards each year, according to a study performed by *EIR* for our spring 1986 *Quarterly Economic Report*. This decline was measured between 1981 and 1983, based on comparison of price and unit data for a group of 35 major commodities. Surprisingly, exports of raw materials from Ibero-America to the United States declined, while exports of manufactured products rose spectacularly. International Monetary Fund programs forced devaluations of those nations' currencies against the dollar, producing declines in the export prices of their manufactured goods even larger than the fall in the prices for their commodities listed on international exchanges.

TABLE 1
Sources of U.S. imports
(percent)

	1980	1983	1985
Industrial nations	49	57	65
Developing nations	51	43	35

The problem is that the dollar-bloc countries do not have sufficient economic weight to provide the United States with the size of subsidy it requires.

Table 1 shows the increasing dependency of the United States on the industrial nations as sources of imports.

The fact that this marked shift took place during a period when developing-sector exports were to be had at a fraction of cost—at 70% less than 1980 prices, in the case of Ibero-America—underscores the point that America's industrial economy cannot exist without a subsidy from other industrial nations; the United States is too big, and the industrial sectors of the developing world too small, to carry the burden. All nations participated in this subsidy, but none so much as Japan.

The European data, in particular, underscore the miserable fraud involved in Yeutter's attacks on Western Europe. Yeutter's strike at selected European food exports was calculated to hit every European Community (EC) country, to score maximum political damage. According to European agriculture sources in Brussels, the list was drawn, "probably by U.S. Trade Representative Clayton Yeutter personally to hit select targets of European agriculture exports." According to estimates in Brussels, the tariff targets will mean loss of approximately $400 million per year to Europe. Hardest hit will be French exports, almost 50% of which are affected, including cognac and certain white wines; Danish canned ham; German white wines and cheese; and Dutch cheeses. According to the terms set Dec. 31 by Yeutter's office, if the European Community does not satisfy U.S. administration demands by Jan. 30, the prohibitive 200% tariff system will go into effect.

These measures are irrelevant to the U.S. trade problem from the beginning. The deeper problem is that the collapsing American dollar, and the $200 billion overhang of U.S. net foreign indebtedness, have shut off the means to finance the trade subsidy. The United States will begin to live on what it produces, that is, undergo the worst contraction of consumption in its history.