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POLITICAL ISSUES IN EXPORT POLICY

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As a speaker, I have seldom been given wider latitude in the selection of a topic. If my choice seems to take us far from the main fields of your professional interests and from market research, the predominating subject of this panel, my justifications are, first, that if I can make any contribution to a meeting of disciplined economists, it is apt to be in the field of my own interest and experience, and second, that market research which ignores the influences of our political environment lacks a measure of realism.

I would like to discuss two subjects of recent and current interest with which Cargill, as a grain exporter, has been involved. Each case concerns a major area of opportunity for the grain economy of the United States. And in each case, opportunity has been seriously jeopardized by political compromise which seems inherent in our system of determining national policy.

First of my two subjects is the recent series of negotiations with the Soviet Union for the sale of U. S. wheat. The important facts for our purposes are these:

Russia, normally a wheat exporter, last year was persuaded by a combination of unusual circumstances to seek wheat from the United States. It had suffered four successive harvests which had ranged from disappointing to disastrous. The 1963 harvest was one of the worst in its recent history. Grain production, especially wheat, dropped 25 percent. Unexpectedly, in the fall, Russia was also confronted by a substantial failure of the wheat crop in Western Europe, which normally supplies its East-European satellites.

The Soviets turned first to Canada, which always has been willing to sell wheat to Communist countries. It arranged for delivery of 200 million bushels of wheat and flour equivalent (valued at more than half a billion dollars) over a period of ten and a half months. Then, needing a source of supply for the winter months, when Canadian St. Lawrence ports are blocked by ice, the Russians turned to the United States. They sought for themselves and their satellites 4 million tons of wheat -- about 150 million bushels -- for shipment in January, February and March at prevailing world prices. For this they were willing to pay promptly in dollars.

Assuming the sales did not conflict with this country's assessment of Soviet intentions and capabilities in the Cold War, they offered a remarkable economic opportunity. The President shortly determined such sales did not conflict, but in fact strongly supported the national interest.

Secretary of the Treasury Dillon, in testimony before the Senate Banking and Currency Committee, noted three important benefits from the proposed sales to the nation as a whole: First, they would improve our balance of international payments -- $2.2 billion deficit in 1962 -- by $300 million; second, they would strengthen our gold position vis-a'-vis the Russians, and third, they would produce savings of $200 million in storage payments over a period of five years.

For the wheat economy, in chronic difficulty through most of the period since World War II, the Russian offer represented an immediate outlet for more than $250 million worth of wheat, a chance almost to double hard currency wheat exports over the average of the two preceding years and, perhaps most important, the possibility of an important new dollar market for the future -- if we chose to supply it.

All the Russians required was service. The same sort of service -- on delivery dates, price and selection of classes and qualities -- that we traditionally provide any foreign buyer with dollars to spend. But service is what they did not get. What they got, instead, was delay and more delay. The reasons for this, and the consequences, are worth noting.

First, there was a necessary delay, to which no one objected and which was brief in any case, while the President weighed the broad implications of the Russian offer. Then, however, came a whole series of unnecessary delays: (1) While the Administration sought public support for a decision it had already determined was in the national interest; (2) while the public struggled with baffling contradictions of the so-called Latta amendment; (3) while the Senate debated the wisdom of extending credit which the Russians did not seek and did not use, and (4) while the Administration groped for a solution to the demands of various maritime interests.

Let's consider what was involved in the two most troublesome issues -- the Latta amendment and the maritime problem.

The Latta amendment is a resolution adopted in 1961, at the time of the Berlin crisis, as part of that year's Agriculture Act. It expressed the sense of the House of Representatives that this country should not subsidize the sale of agricultural commodities to "unfriendly nations."

The Latta amendment reflects a basic misunderstanding of the function of the export subsidy. As you know, but many do not, the export subsidy is provided to enable U. S. wheat producers to take part in world trade. So long as this country supports the income of wheat producers by artificial domestic pricing, some adjustment to the realities of world competition is necessary. The export subsidy provides this adjustment. Its benefits flow to the wheat producer and the wheat economy in the form of a broader market. They do not flow in any sense to the foreign buyer who can, if he chooses, buy from other world suppliers at the lower world price.

If anything, the Latta amendment produces a result exactly contrary to the nation's need. Commodities for which export subsidies are required --

such as wheat and cotton -- are the very commodities in greatest surplus and, therefore, in greatest need of export outlets. To the extent we exclude them from East-West trade in favor of such others as corn and soybeans, which are not in great surplus and are competitive in world trade without subsidy, we penalize only ourselves.

However illogical the "subsidy-no subsidy" test may seem, many people willingly accept it. This is clear from letters we have received criticizing what the writers assumed to be a taxpayer subsidy to the Russians. Politicians -- many of whom surely are familiar with the real nature and purpose of the export subsidy -- exploited this misunderstanding, presumably because they either disagreed with the President's decision and could not attack it effectively on its merits, or because they wished to embarrass the Administration at any cost. The cost, in negotiations with the Russians, counted in several important weeks of delay.

The second major issue presented by the Russian sale involved the unprecedented requirement that U. S. flag ships, regardless of additional cost, be used for at least 50 percent of the total movement. Here, too, some background is necessary to understand how and with what results political leverage was employed.

The flag requirement was first suggested by President Kennedy in his announcement on October 9 that wheat shipments to the Soviet Bloc would be licensed. He added that shipments would be "carried in available American ships supplemented by ships of other countries as required." There continues to be disagreement about both the President's meaning and the source of his inspiration for the reference to U. S. ships. There had been no discussion of a flag requirement in our prior negotiations with the Soviet trade mission. We doubt that the President could have foreseen the consequences of his announcement, which were immediate. U. S. flag rates skyrocketed.

This could have been predicted by anyone familiar with the history of the U. S. tramp shipping industry. In recent years U. S. ships have been effectively priced out of the commodity trade by construction and manning costs much higher than those of their foreign competitors. To assist them, Congress passed, in 1934, the Cargo Preference Act. It requires that U. S. ships be used to transport at least half of any cargo for which our government has advanced (long term) credits or guaranteed the convertibility of currencies. Under this law, PL 480 sales of surplus grains have provided the principal source of grain cargoes for U. S. tramp ships since the program's inception a decade ago.

Because U. S. flag ships seldom can compete for commercial grain business, few have been built for the purpose since the Second World War. The bulk of our tramp fleet has engaged in other, more profitable business -- notably in the U. S. coastal and PL 480 trade. Thus, when the President announced that as much as 150 million bushels of wheat offered the Russians might be moved in U. S. flags, he greatly increased the cargo available, in theory at least, for a limited ship supply. The result, as I've said, was that U. S. flag rates broke sharply upward.

In the face of this the Russian buyers balked. They refused to pay a premium -- amounting to as much as 23 cents a bushel during the period of negotiations -- not required of any other buyer of U. S. wheat.

In the debate which followed the President's announcement, proponents of the U. S. flag requirement in the Russian trade argued that the Cargo Preference Act provided precedent. They chose to ignore two important facts: First, that we have never before applied this requirement to a commercial sale -- which, of course, was what the Russians sought -- even those involving short term credit guaranteed by the Export-Import Bank. Second, that even under Public Law 480, the United States government, not the foreign buyer, pays the premium for U. S. flags. Thus, the effective cost to the foreign buyer has been no more than the foreign flag rate.

For several weeks negotiations were stalled on this issue. President Kennedy's death in November complicated a settlement. The new administration was unwilling to withdraw a commitment which the maritime unions claimed they had had from the former president, even though it clearly frustrated sales the latter had determined were in the national interest.

Only after several weeks of delay in which it had long discussions with exporters, shipowners and maritime unions, did the Administration define its requirements: First, it limited the use of U. S. flags to 50 percent of the wheat sold. Second, it established a range of shipping rates deemed "fair and reasonable" and indicated waivers would be issued unless U. S. ships were offered within the range. (These changes brought the terms into line with those for PL 480 sales except -- and this is important -- our government did not offer to absorb the premium for U. S. flags.) Third, a procedure was worked out for canvassing the freight market to determine how much U. S. freight might be available for any particular shipment period. This last was important because it enabled the exporter to estimate his freight costs accurately before making an offer. It was generally assumed that a canvass would show no more than 30 percent of the total anticipated sales could be accommodated in available U. S. flag vessels. Finally, the Administration suggested that transactions could be handled on a delivered basis so that the exporter rather than the Soviet buying mission could arrange the freight.

Still this was not sufficient. The Russians adamantly refused to pay any premium or accept any terms not imposed on other commercial buyers of U. S. wheat. For a time it seemed that the whole transaction would founder. And, indeed, it might have, had not the Administration been determined to find a way to complete the trade.

As you know, a way was found. The key was durum. The Soviet buyers had little interest in durum but they were willing to accept it if it could help break the log-jam.

The importance of durum for this purpose lies in the fact that the export subsidy for this class -- unlike others -- is established on a bid basis for individual trades. Both major export sales to the Russians included large quantities of durum on which a subsidy, sufficient in amount to offset at least a portion of the anticipated freight premium was paid the exporter. In answer to the critics, the Administration indicated it would have been willing to accept subsidy bids at this higher level in connection with an export sale of durum in this quantity to any foreign buyer.

Once the sales were made and the contracts signed, it seemed our problems were behind us. But this was not to be. On February 16, maritime unions halted loading of all ships to Russia. They based their action on a waiver of the U. S. flag requirement issued to Continental Grain Company under rules the unions had previously accepted and on which both Cargill and Continental had based contract prices with the Russians.

The apparent reasons for the unions' action provide some insight into the problem we are considering here -- the political involvement of U.S. export policy. In the period after general agreement on the terms of the shipping requirement several things happened: First, there was Britain's announcement that it would offer long term credit to the Russians for purchase of industrial plant and machinery and, later, that same country's decision to sell buses to Cuba. These were followed by France's recognition and exchange of trade delegations with Red China. In these cases our government's objections were met with the bland assertion that our wheat sales to Russia provided precedent for almost anything our allies might wish to do in the trade field. It would seem that unions simply capitalized on growing public disillusionment with the Russian wheat sales to force acceptance of ground rules more to their liking.

This placed the Administration in a difficult position. It did not want to default on commitments to the Russians, yet it was unwilling to force performance by the unions in an election year. So, it simply acceded to the union's terms.

We are not sure even today what all these terms may have been. We know this much: First, that no further waivers were to be issued whether or not ships were available under the terms of the earlier announcement (on which our sales had been based). Second, the Administration would consider at a later time extending the requirement to all grains and to all Communist countries, including Yugoslavia, which is clearly outside the Soviet orbit. Judgment on these extensions will be made on the advice and counsel of a committee comprising government, shipowner and union representatives, but significantly not including representatives of American agriculture or agricultural industry.

We did the only thing we could under the circumstances except, perhaps, default on our contracts. We altered the contracts to accommodate ships unavailable or ineligible under the original rules and we absorbed the additional costs.

I have not discussed these aspects of the Russian sales at such length to gain your sympathy, but instead because they illustrate how vulnerable are our export opportunities to political opportunists.

In the case of the Latta amendment, by playing on public misunderstanding of the export subsidy, opponents of the Administration delayed negotiations for several weeks and created a reserve of public resentment which will make future negotiations very difficult. By the same token the maritime unions seized upon public misunderstanding and suspicion to secure commitments which gave them access to tonnage for which they would not otherwise be competitive. And, last, rather than face the issue squarely, the Administration first temporized and then applied a palliative -- the bid subsidy on durum.

The cost of our lack of resolute purpose after the President had approved the sales of wheat to the Soviet Bloc is difficult to measure. Certainly we lost sales of nearly 2 million tons of wheat worth more than $100 million to the wheat economy of this country. We may also have lost the opportunity to determine for ourselves in the future whether we will or will not sell wheat to the Soviet Bloc.

And for what good purpose? Certainly not to solve the problems of the U. S. tramp fleet, for the present policy is no solution at all. If the Soviet Bloc will not buy from the U. S. under these terms, surely no benefit will accrue to the U. S. maritime industry. Indeed, if advantage was gained from the political combat which surrounded the Russian wheat sale, it must be measured in gain to the combatants themselves, for there was certainly no advantage to the nation or its wheat economy.

In the beginning I suggested that there are two current issues which illustrate my thesis. The second concerns the current round of negotiations between the United States and the Common Market under the auspices of GATT. If anything, its consequences for agriculture are likely to be more harmful than those which will result from our mishandling of the Russian sales. The issue here is a basic conflict between the United States and the Common Market on agricultural trade policy. At stake is our best present dollar market for grain.

Here, too, some brief background may be helpful in understanding the issues. Historically, only France among the six Common Market members has been a producer of significant grain surpluses. The other five have been importers -- collectively, our industry's most important commercial customer, buying fully a third of our farm exports sold for dollars.

In the past, despite our transportation disadvantage, we have competed effectively with France for the grain requirements of these countries because of the efficiencies of our farmers and our internal handling system. As a result, France has had to limit its production in order to avoid costly surpluses.

Now, however, the situation is changed. France, a member of the Common Market, finds itself within the bounds of a customs union with five important grain deficit countries of Western Europe. When the common agricultural policy becomes fully effective, France will be able to ship grain to other members free of any duty. Exports from other countries, including the U. S., will continue subject to a variable levy which adjusts itself automatically from day to day to offset any change in the world market price.

France, completely protected from external competition, no longer need fear a buildup of costly surpluses. Instead, that nation can actively expand production by increasing price incentives and modernizing farms. To the extent it is successful, we will progressively be closed out of our best dollar market. This, essentially, is the issue for agriculture in the Geneva meetings.

In retrospect it appears that our initial acceptance of the variable levy -- or, at least, agreement to defer objections under the so-called "standstill agreement" was a disastrous mistake. The variable levy is completely effective against imports and, in its present form, structurally incompatible with a liberal trade policy. More important for our discussion today, it has shifted the focus of negotiations from tariffs, where we have a measure of flexibility under the Trade Act of 1962, to domestic farm policies, where our own long history of protectionism and our cumbersome system of policy-making leave us vulnerable.

This was apparent in our first attempts to deal with it in preparation for the Kennedy round. You will recall that the Secretary of Agriculture, in addresses here and in Europe, insisted that American farmers have the right to compete in European markets if we were to extend reciprocal rights to European manufacturers. He strongly endorsed liberal trade arrangements for both farm and industrial goods. His statements were widely acclaimed -- and rightfully sc -- in this country. Unfortunately, they were not as persuasive in Europe. Common Market officials pointed out that for more than 30 years, the United States has maintained farm price supports amounting to production incentives and has protected them against imports whenever necessary. They noted that laws authorizing import restrictions remain on our books and can be implemented whenever imports threaten price supported commodities. They were not impressed by the fact that these laws are now seldom invoked. Mr. Edgar Pisani, French Minister of Agriculture, implied that, with ten years of protected growth and modernization, French farmers won't require tariff protection either.

This playback must have been particularly embarrassing to the Administration, for it came at a time when the Secretary of Agriculture was before the Congress seeking extension of our domestic price support programs, expressly for the purpose of improving farm income. The Administration faced an uncomfortable choice: Either to reverse the direction of its domestic farm policy -- a difficult shift of gears -- or to move to politically more comfortable ground in its approach to the Common Market. It is regrettable, I think, that it chose the latter. Our objective became, and apparently is today, not liberal trade in the classic sense, but an international grain agreement -- or "arrangement" as some prefer to call it. We now seek guaranteed access to Western European markets by prearrangement rather than under a fixed tariff and international price competition.

To some this may sound appealing. Certainly it is more compatible with recent domestic farm policy for which members of both major parties bear heavy responsibility. But in practice, it also involves certain basic problems which have not been the subject of adequate public discussion.

Most important, international arrangements of the sort proposed would suspend completely effective price competition; indeed, this is their central purpose. If we accept access to Western Europe on this basis, we forego the opportunity of focusing the weight of our bargaining position in the Kennedy round in this most important issue -- the level of price incentives offered French farmers. If the result is higher price incentives and resulting production of surpluses -- as we suspect it must be -- our access agreement will be of doubtful value. This seems better understood in Europe than it is here. Dr. Sicco Mansholt, vice president of the Common Market commission, said recently, "It is nonsensical to suppose that quotas can guarantee continuing access to our market for exporting countries, if by a policy of high price supports we artificially stimulate our own production to the point where we meet, or even exceed, our own grain and dairy produce requirements". We in the U. S. know from experience the pressure costly surpluses can exert against imports.

Even if we were successful in extending an access agreement from time to time, we would face the prospect of competing with subsidized French surpluses in other world markets. This does not seem much of a bargain for the United States.

I suggested earlier that the Administration has another alternative. It involves recognition of certain practical limitations in dealing with the issue of world trade in grain:

First, because of government efforts to protect the income of producers, world trade in grain is and has been, for many years, detached from economic realities. Until this is changed there is little sense in talking about trade on the basis of comparative advantage.

Second, that needed change involves, both here and in Europe, more rational efforts to deal with income problems of producers.

Third, that these changes cannot be accomplished in a single stroke. Political realities clearly dictate progressive steps in this direction over a period of several years.

And, fourth, that neither the United States nor the countries of Western Europe will undertake these steps without assurance that others will also undertake them. The Secretary has aptly likened this aspect of the problem to disarmament.

If there is a genuine desire for a solution to the agriculture impasse with the Common Market -- and I believe there is both here and in Europe -- and if the practical limitations I've mentioned can be recognized and accepted then our objective should be not a quantitative access agreement but, instead, an agreement which will lead to progressive steps toward elimination of the principal impediments to trade. Obviously, they include our domestic programs of price support and supply control as well as the devices the Common Market proposes to protect its producers.

Happily, there seems to be a growing awareness of the opportunities this approach offers. Mrs. Helen Farnsworth has offered several very useful suggestions for implementing such an agreement under the auspices of GATT. More recently, the National Planning Association has endorsed the idea.

There is, of course, no assurance that we could persuade the Common Market to accept such a plan. I assure you, I do not for a moment underestimate the difficulty and complexity of such an undertaking. On the other hand, it should have appeal to Europeans lacking in other approaches. For one thing, it would defer the necessary downward adjustment of farm prices in Europe until after French and German elections in 1965. (It is worth noting that an attractive feature of the common agricultural policy from Germany's point of view was provision for establishing common target prices not in a single step but over a period of seven years.) Further, it provides a framework for bringing agricultural and industrial trade objectives into line. This is important both to European industrialists who recognize the danger of retaliation and to professional managers of the Common Market government who see agricultural protectionism as one of the most dangerous obstacles to full economic and political union.

Its importance to this country seems obvious: Under such an arrangement, the comparative efficiency of our farms should reflect itself in expanded foreign markets for years to come. Further, it would provide both compelling reason and opportunity to make important, long delayed reforms in domestic farm policy.

Whether these advantages will persuade those who control our trade policy is another matter, for it would necessarily involve admission that, however well price support programs may have served farmers in the past, they are now a serious handicap to efforts to maintain access to badly needed foreign markets. The record shows that this sort of admission does not come easily in our system.

It will be tragic if we turn our backs on this promising plan simply because it requires a shift in domestic farm policy -- all the more so because it is apparent that the shift is coming anyway. There no longer exists a farm bloc of sufficient strength to impose the cost of these programs on consumers and taxpayers year after year. This was apparent in the extraordinary efforts required this year to enact a wheat program.

It is not my purpose here today to imply that agriculture is somehow more deeply involved politically than it has been in the past. Instead it is to suggest that the nature of present issues -- involving arrangements that will determine our access to important dollar markets for years to come -- makes policy misjudgments based on political compromise much more costly. Our past mistakes in farm policy judgment could be corrected once they were recognized. This is not apt to be true of mistakes in dealings with the Soviet Bloc or the Common Market. Once these mistakes are made they may be forever beyond our power to correct. Unless strong support for the needs of export markets is heard -- before the fact -- in the councils of those who determine our farm policy, the fate of their constituents will almost certainly be shrinking opportunity.