Import, export prices reflect declining dollar and oversupply in 1985

After falling during the first three quarters of the year, import prices rose as the effects of the weakening dollar were finally felt; meanwhile, fierce competition and oversupply forced down U.S. export prices

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U.S. import prices, as measured by the BLS International Price Program, continued to fall in 1985, marking their third consecutive year of decline. The 1.1-percent decrease for the year followed a 1.5-percent drop in 1984. Most of the 1985 decline was registered in the first quarter, when import prices fell 2.3 percent. The dollar's depreciation moderated import price decreases in the second and third quarters, and contributed to a 1.8-percent price rise for imports during the fourth quarter. (See chart 1.)

During 1985, price increases for imports of finished goods and food could not offset declines for raw materials and intermediate goods. Prices rose 4.2 percent for machinery and transport equipment, 0.8 percent for miscellaneous manufactured goods, and 4.8 percent for food. Prices for beverages and tobacco also rose 3.3 percent for the year. However, decreases were recorded in the other four components of the all-import price index. Energy, intermediate goods, and crude material prices were down 6.0 percent, 2.5 percent, and 7.8 percent, respectively. The fats and oils index, which represents only 0.2 percent of the all-import index, plunged 56.0 percent. These declines are largely attributable to oversupplies of basic commodities, such as crude petroleum, rubber, steel, and certain nonferrous metals.

The U.S. dollar reached an all-time high in March 1985, and then began a gradual decline, falling 9 percent by September. In late September, the decline was accelerated after a group of the Nation's major trading partners agreed to intervene in the foreign exchange market to curb the dollar's strength. The immediate effect was a further 5.1-percent decline in the value of the dollar, bringing the total drop to 13.6 percent for the year.[1]

Product areas in which the major industrialized nations supply a large percentage of U.S. imports appeared particularly susceptible to last year's changes in exchange rates. For example, the machinery and transport equipment index, which accounted for nearly 40 percent of total imports in 1985, declined 1.3 percent in the first quarter of 1985. However, as the dollar began to fall, import prices rose modestly in the middle of the year, and then jumped 3.6 percent in the fourth quarter, the strongest quarterly advance in 4 years.

The dollar's decline did not immediately affect all import prices. Some suppliers deferred price increases to see if the dollar's downward trend would be sustained. In other cases, traders were bound to long-term supply contracts and thus could not adjust prices immediately. Also, the dollar re-

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mained strong against some currencies, especially those of Mexico and Latin America. For example, the Mexican peso depreciated 54.3 percent against the U.S. dollar in 1985.[2] Meanwhile, the currencies of Canada and some of the newly industrialized nations of the Far East depreciated slightly against the dollar last year. All of these factors contributed to the record $361 billion of foreign goods imported by the United States in 1985.[3] That was 6.0 percent greater than the previous record high set in 1984.

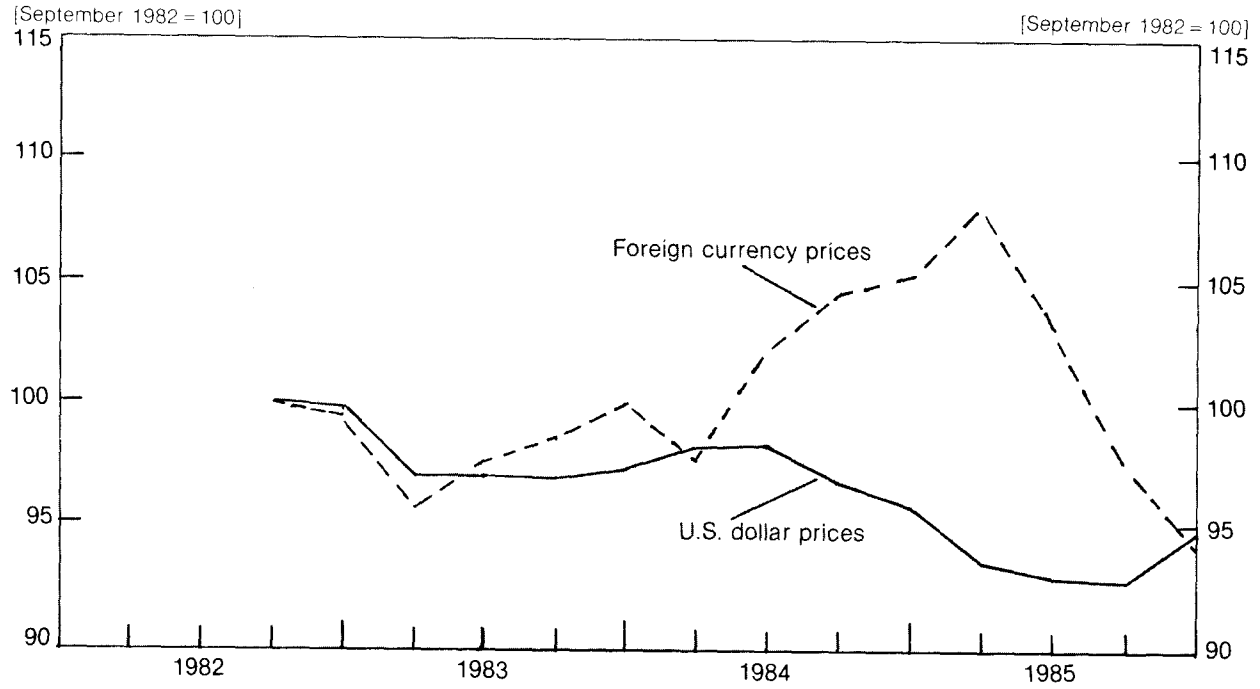
U.S. export prices declined in 1985 for the second year running. The 1.3-percent drop nearly matched the 1.4-percent decline observed in 1984. (See chart 2.) Major declines occured in the indexes for crude materials (−8.1 percent), energy (−3.1 percent), and agricultural products (−3.0 percent). The fats and oils index plummeted 31.4 percent but this index represents less than 1 percent of U.S. export trade. Declines of 1.2 percent, 1.1 percent, and 2.7 percent were registered for intermediate manufactured goods, chemicals, and beverages and tobacco. Moderating these declines were a 1.3-percent price increase for machinery and transport equipment and a 1.0-percent advance for miscellaneous manufactured goods.

Many of the same factors that caused import prices to decrease also held down export prices. Excess global stocks of food, crude materials, and fats and oils depressed prices for those commodities. The strong competition encountered by U.S. exporters, especially from producers in the Far East, kept any price increases to a minimum. Also, the strength of the U.S. dollar continued to have a dampening effect on export prices, despite the weakening during the last three quarters of the year. Although U.S. export prices dropped, the Nation's export volume was down in 1985. U.S. exporters shipped $213 billion in merchandise, or 2.2 percent less than the previous year's total.[4]

The Nation's merchandise trade deficit hit a record $148.5 billion in 1985,[5] 16 percent above the 1984 total. (See chart 3.) The largest U.S. merchandise trade deficit was held with Japan—$49.75 billion, up 35 percent from 1984. The Nation also had significant trade deficits with Canada, Taiwan, and West Germany of $22.2 billion, $13.1 billion, and $12.2 billion respectively.[6] In contrast, the United States continued to maintain a healthy trade surplus of $21.4 billion in the service sector.[7] Service trade includes income of U.S. foreign subsidiaries. The dollar's 1985 decline tended to push up earnings in this area.[8]

The strong dollar has been a major cause of the trade deficit. Although the real value of the trade-weighted dollar declined 13 percent between March and December 1985, at yearend it remained 32 percent higher than its July 1980 low.[9] (See chart 4.) Roughly one-third of the recent drop in the trade-weighted dollar followed the historic "Group of Five" meeting on September 22 in New York, at which

Chart 1. Quarterly indexes of U.S. dollar and foreign currency prices for U.S. imports, 1982-85



SOURCE: Bureau of Labor Statistics, based on data from the Bureau and from the Morgan Guaranty Trust Co.

Table 1. Changes in Import Price Indexes for selected categories of goods, December 1984–1985

SITC Category	Description	Percent change						
		Annual			Quarterly			
		Percentage of 1980 trade value	Dec. 1983 to Dec. 1984	Dec. 1984 to Dec. 1985	Dec. 1984 to March 1985	March 1985 to June 1985	June 1985 to Sept. 1985	Sept. 1985 to Dec. 1985
	All commodities [1]	100.000	−1.7	−1.1	−2.3	−0.5	−0.1	1.8
	All commodities, except fuels and related products	67.223	−1.0	0.9	−2.2	0.3	0.4	2.4
0	Food	6.554	−2.3	4.8	0.4	−1.7	−2.0	8.3
01	Meat	.977	−1.3	−0.8	−1.4	−9.4	2.0	8.8
06	Sugar, sugar preparations, and honey	.925	0.5	−5.6	−0.1	3.5	0.4	−9.1
07	Coffee, tea, cocoa	2.241	−2.0	10.6	−2.4	−1.8	−2.9	18.7
1	Beverages and tobacco	1.082	0.7	3.3	−0.2	0.6	0.6	2.3
2	Crude materials	4.275	−0.2	−7.8	−5.0	−0.4	−2.2	−0.3
23	Crude rubber including synthetic and reclaimed	.410	(2)	−12.6	−7.4	−1.5	−9.8	6.2
24	Wood	.865	−3.0	−4.4	−3.2	6.2	−5.0	−2.2
25	Pulp and waste paper	.708	15.2	−18.7	−9.9	−4.3	−4.5	−1.3
28	Metalliferous ores and metal scrap	1.465	(2)	−5.8	−5.4	−3.1	2.2	0.7
3	Fuels and related products	32.776	−3.0	−6.0	−2.7	−2.4	−1.4	0.4
33	Crude petroleum and petroleum products	30.653	−3.1	−4.8	−1.6	−2.6	−1.6	1.0
4	Fats and oils	.226	14.4	−56.0	−21.8	−14.7	−24.9	−12.2
5	Chemicals and related products	3.475	−2.4	−3.0	−1.4	−0.8	−0.4	−0.3
6	Intermediate manufactured products	13.520	−0.4	−2.5	−2.7	−0.5	0.9	−0.1
67	Iron and steel	3.127	3.5	−4.4	−2.2	−0.7	−0.8	−0.7
68	Nonferrous metals	3.123	−7.9	−7.9	−6.2	0.5	1.7	−3.9
7	Machinery and transport equipment	25.442	−1.2	4.2	−1.3	1.0	0.9	3.6
73	Metalworking machinery	.755	−6.1	9.1	−4.0	4.9	4.1	4.1
75	Office machines and automatic data processing equipment	1.217	−4.9	1.6	−2.8	0.2	1.0	3.8
76	Telecommunications, sound recording and reproducing equipment	2.785	−3.8	−3.0	−1.4	−1.3	−0.6	0.3
77	Electric machinery and equipment	3.396	−9.3	−3.6	−5.0	2.2	−3.0	2.3
78	Road vehicles and parts	10.887	1.6	5.8	0.2	0.5	0.5	4.5
8	Miscellaneous manufactured articles	9.794	−0.1	0.8	−3.0	1.0	1.6	1.2
84	Clothing	2.666	7.8	−2.9	−1.3	−2.0	0.4	0.0
85	Footwear	1.232	4.8	0.1	−3.6	−0.5	4.0	0.4
87	Professional, scientific, and controlling instruments and apparatus	.628	−4.8	10.2	−4.0	3.5	7.0	3.6
88	Photographic apparatus and supplies, optical goods, watches and clocks	1.162	0.8	3.9	−2.6	0.7	1.8	4.2
89	Miscellaneous manufactured articles, n.e.s.	3.286	−8.4	1.7	−5.3	4.4	1.3	1.6

[1] This category includes indexes in addition to those shown here. For all of the indexes available in each category, see *U.S. Import and Export Indexes*, USDL–86–38 (Bureau of Labor Statistics), January 30, 1986.

[2] Data not available.

n.e.s. = not elsewhere specified.

Japan, West Germany, the United Kingdom, and France agreed to cooperate in a plan to force down the value of the dollar through intervention in foreign exchange markets. As of December, however, this decline had not retarded U.S. imports or stimulated exports, as the record trade deficit showed.

Another reason for the large trade deficit has been the rapid industrialization of Far Eastern nations following in Japan's footsteps. Besides the massive trade deficit with Japan, the United States also ran large trade deficits with other nations in the Far East. The combined trade surplus of South Korea, Taiwan, Hong Kong, and Singapore with the United States reached an estimated $25 billion in 1985.[10] These nations are aggressively entering automobile, consumer electronics, and semiconductor markets.[11] This has led to lower prices for many of these goods on world markets.

The Latin American debt problem also had a negative effect on U.S. foreign trade in 1985. It is estimated that the region's total foreign debt will reach $360 billion for the year.[12] Brazil is most heavily in debt, owing $100 billion, with Mexico not far behind at $97 billion.[13] All the debtor nations need hard currency to repay loans from Western banks and The International Monetary Fund. In an effort to obtain the currency, these countries have curtailed imports, which has dramatically hurt U.S. export trade. U.S. exporters to Latin America are further hampered by the appreciation of the dollar against many of these nations' currencies.

Price developments discussed in this article are based on data from the BLS International Price Program. That program produces import and export price indexes based on the Standard Industrial Trade Classification scheme. Both indexes use a modified Laspeyres formula. Price data are collected for more than 14,000 products, and are not seasonally adjusted. Import price indexes are weighted by the 1980 Tariff Schedule of the United States Annotated (TSUSA). Export price indexes are weighted using the 1980 Schedule B

classification system of the U.S. Bureau of the Census. In addition, the International Price Program, in 1985, also started producing SIC-based indexes and Bureau of Economic Analysis "end-use" price indexes.

Import price developments

Energy. The decline in world energy prices continued to lower U.S. import prices. This was reflected in the price index for imported fuels and related products, which decreased 6.0 percent for the year after a 3-percent drop in 1984. This index comprises 32.78 percent of the all-import index. The crude petroleum index fell 3.8 percent and the natural gas index decreased 23.9 percent. (These two index movements represent prices through November 1985.)

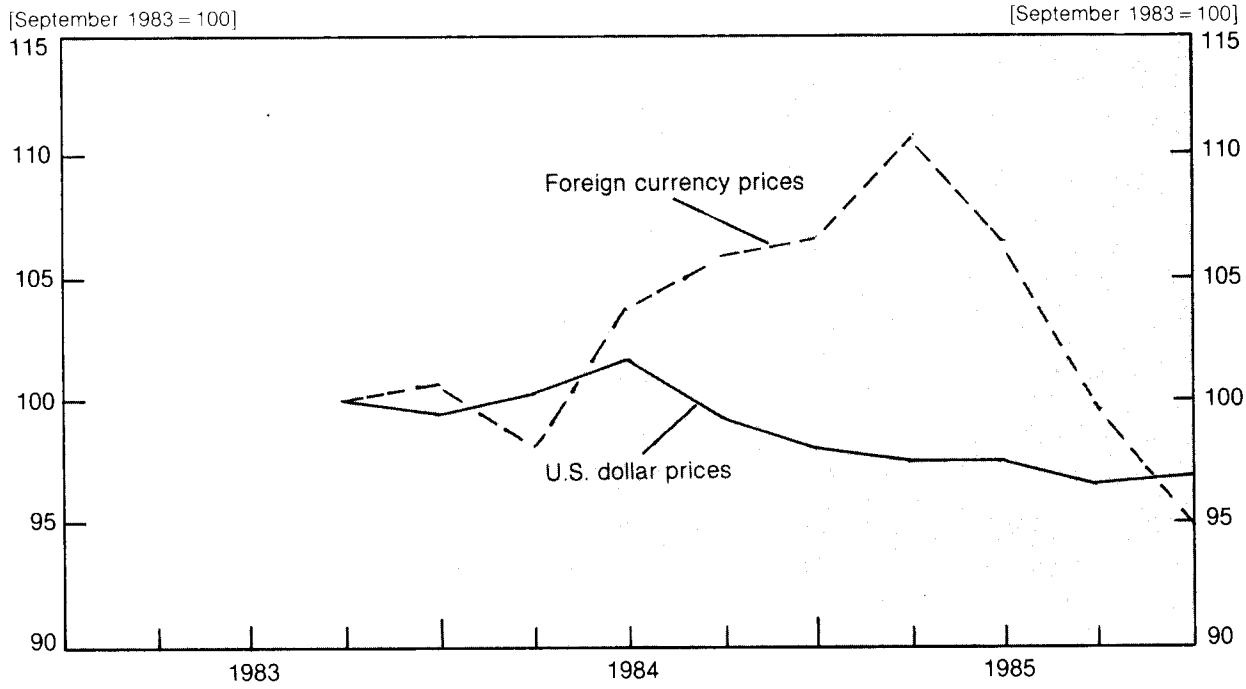
U.S. average monthly imports of crude oil and petroleum products declined 7 percent from their 1984 level, and 27 percent since August 1980.[14] (See chart 5.) Much of this decrease can be attributed to greater fuel efficiency in automobiles and a switch from crude oil to coal and natural gas by many industrial consumers.[15] The decline in U.S. crude oil imports has greatly affected many OPEC nations, especially Saudi Arabia. From 325 thousand barrels of crude oil a day in 1984, Saudi Arabian imports had declined to 167 thousand barrels a day by 1985. Total U.S. imports of OPEC crude oil in 1985 were 1,825 thousand barrels a day, down 11 percent from 1984 and 58 percent from 1980.[16]

Since 1982, the United States' major source of foreign crude and petroleum products has been non-OPEC producers. Imports of crude oil and petroleum products from these nations were 23 percent greater in 1985 than in 1980, but were down 5 percent from 1984 levels. The number of barrels of Canadian and Mexican crude imports increased during 1985, but imports of U.K. crude fell 22 percent over the year.[17]

In September, OPEC representatives met in Switzerland and decided to drop the cartel's official price 50 cents per barrel for heavy crude and 20 cents per barrel for medium crude. The cartel's previous official price of $26.50 a barrel for heavy crude had been $2 above the spot market price.[18] Saudi Arabia was the only OPEC member to actually sell heavy crude for that amount. As a result, in July, Saudi output hit its lowest production level in 20 years. For several years, the other OPEC members have routinely sold their crude at a discount or through barter agreements and so have captured potential Saudi Arabian sales.[19]

As of October 1, 1985, Saudi Arabia decided that it was no longer going to follow the cartel's official prices. In order to get production up, Saudi Arabia began the practice of "net-backing" prices. This involves the linking of crude oil prices to those of refined products. With Saudi Arabia cutting prices to some $2 below the official cartel price, that nation's production increased to 4.2 million barrels a day

Chart 2. Quarterly indexes of U.S. dollar and foreign currency prices for U.S. exports, 1983-85



SOURCE: Bureau of Labor Statistics, based on data from the Bureau and from the Morgan Guaranty Trust Co.

from 2 million barrels a day. At year's end, Sheik Yamani, the Saudi Arabian oil minister, announced plans to keep production at the higher levels even if it forced prices below $20 a barrel, which it did in January 1986.[20]

Most non-OPEC oil producing nations cut their prices for crude throughout 1985. In November, however, Mexico and two Canadian companies increased their prices for crude oil. Since 1983, Mexico had conformed to OPEC pricing and production policies. This situation existed until July 1985, when that country cut its prices for Isthmus light crude by $1.24 and for heavy crude by 77 cents a barrel.[21] But in November, Mexico responded to a firming up of oil prices and increased demand for light crudes by raising the price of its Isthmus light crude by 76 cents. In the same month, Canada's Imperial Oil Ltd. and Petro Canada raised their prices for Alberta 40-degree light crude oil by $1.58 and $1.20 respectively.[22] Throughout November, crude oil prices rose on the spot market as oil companies kept inventories low in expectation of price decreases in December or early 1986. At that time, the full impact of Saudi Arabia's increased production was expected to cause a glut of oil on the world market.

By December, U.S. stocks of heating oil for the winter season were at an all-time low. Because domestic refineries had extra capacity and foreign heating oil was available, there was no concern about a shortage in heating oil when seasonal demand picked up.[23] However, spot market prices for heating oil had increased in the last half of the year. In July, heating oil was selling on the spot market for $28.50/bbl, but by the end of November, the price had reached $38.50/bbl.[24] This resulted from high European demand, and the fact that the Europeans were offering a premium to refiners. In September, inventories were 18 million barrels below 1984 levels and just 13 million barrels above spot shortage levels.[25]

During the winter of 1984–85, U.S. natural gas use was 1.9 percent below the previous year's levels. The forecast for winter 1985–86 is for an increase in natural gas consumption in the 3-percent range, with a concomitant growth in imports of 0.04 trillion cubic feet.[26] Practically all of the increase in imports will be coming from Canada.

From 1975 to 1984, Canadian natural gas prices were set by the government. However, in November 1984, Canada started deregulating natural gas prices, with the wholesale price of natural gas in Toronto serving as the benchmark for sales to the United States. Prices fell as a result of the deregulation, and Canadian natural gas exports to this country increased.[27] Further deregulation in November 1985 was designed to help Canadian producers become price competitive with Western U.S. natural gas producers. According to Canadian law, an exporter cannot sell natural gas to the United States at prices below those offered to purchasers in neighboring provinces. Still, at a floor of $2.19 per thousand cubic feet, yearend 1985 prices were 26 percent less than the previous Toronto benchmark price.[28]

Table 2. Percent change in Export and Import Price Indexes by end-use category, December 1984–85

End-use category	Quarterly				Annual	
	Dec. 84 to March 85	March 85 to June 85	June 85 to Sept. 85	Sept. 85 to Dec. 85	Dec. 83 to Dec. 84	Dec. 84 to Dec. 85
Imports						
Food, feeds, and beverages	0.3	−1.7	−1.4	7.1	−2.1	4.1
Raw materials, except petroleum	−4.7	−0.5	−0.4	−1.6	−0.7	−7.1
Raw materials, durable	−3.8	0.1	−0.4	−1.2	−3.0	−5.3
Raw materials, nondurable	−5.7	−1.2	−0.4	−1.8	1.7	−8.8
Petroleum and petroleum products	−1.5	−2.7	−1.5	0.7	−2.7	−4.9
Capital goods, except auto.	−3.1	1.6	1.3	2.5	−3.5	2.2
Nonelectrical machinery	−2.6	1.3	3.2	3.3	−2.5	5.1
Automotive, including parts	0.2	0.5	0.5	4.7	1.3	5.9
Consumer goods	−1.6	−0.1	1.6	1.5	0.7	1.4
Consumer goods, durable	−1.5	0.0	2.0	1.9	−2.6	2.3
Manufactured, durable	−1.3	0.5	1.7	2.1	−1.8	3.0
Consumer goods, nondurable	−1.5	−0.5	1.4	0.8	5.1	0.1
Exports						
Food, feeds, and beverages	−1.8	−0.7	−5.8	1.7	−12.6	−6.6
Raw materials	−1.5	−0.4	−0.7	−0.3	−1.6	−2.9
Raw materials, durable	−0.8	−1.1	−0.5	−0.1	−4.5	−2.5
Raw materials, nondurable	−1.8	−0.1	−0.8	−0.4	−0.5	−3.1
Capital goods, except auto.	0.6	0.4	0.0	0.0	3.5	0.9
Automotive, including parts	0.9	1.2	0.1	1.0	1.7	3.3
Consumer goods	0.1	0.2	0.8	−0.2	1.2	0.9
Consumer goods, durable	−0.2	0.1	1.2	−0.4	0.4	0.7
Consumer goods, nondurable	0.6	0.4	0.2	0.0	2.0	1.2

Machinery and transport equipment. Prices for imported machinery and transportation equipment were up 4.2 percent in 1985, after slipping 1.2 percent in 1984. (See chart 6.) This index is heavily influenced by fluctuations in the value of the U.S. dollar. Much of the machinery and transportation equipment imported to the United States comes from Japan and West Germany, nations whose currencies appreciated against the dollar in 1985. The weakening of the dollar was reflected in the rise of the index through the last three quarters of the year.

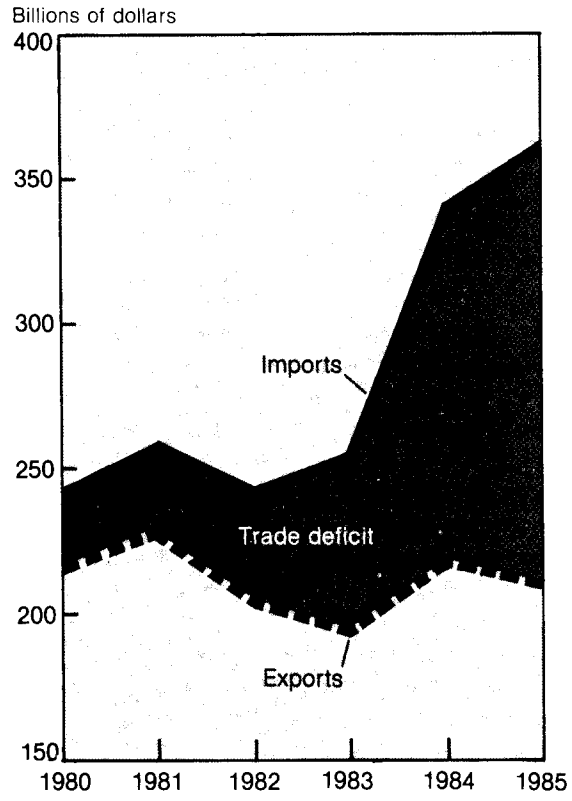
The index for imported machinery and transportation equipment represents 25 percent of the all-import index. In 1985, the value of these imports reached $141.7 billion, up from $123.1 billion the previous year.[29] As the U.S. economy continued to expand, albeit at a slower rate than in 1984, domestic demand for capital goods such as looms, lathes, pumps, and pistons, and for consumer items such as vehicles, video cassette recorders, and microwave ovens,

continued to grow. Much of this demand was met by imports. Indeed, import penetration in the U.S. machinery, electronics, and mechanical components markets has been growing steadily for more than a decade.[30]

Import penetration in the automobile industry also increased in 1985. Despite Detroit's big late summer sales campaign, both Japan and West Germany managed to capture larger shares of the domestic market. Overall, car and truck sales hit record highs, with total units sold reaching 15.7 million.[31] Of these, 74.3 percent were American made, 20.2 percent Japanese, and 3.8 percent German. Comparable 1984 shares were 76.5, 18.4, and 3.3 percent respectively.[32]

The ceiling on the voluntary restraint agreement covering Japanese auto exports to the United States was raised substantially in April of last year. From April 1984 to April 1985, Japanese manufacturers had limited auto shipments to the United States to 1.85 million units. In April 1985, however, they announced that they would raise the yearly limit to 2.3 million vehicles. As a result, Japanese auto shipments to this country as of October 1985 were 36 percent greater than comparable 1984 figures.[33] The yearend strengthening of the yen prompted Japanese producers to raise prices, but analysts doubt this will stem strong sales gains.[34]

Chart 3. Annual volume of U.S. exports and imports of merchandise, 1980-85



SOURCE: U.S. Department of Commerce.

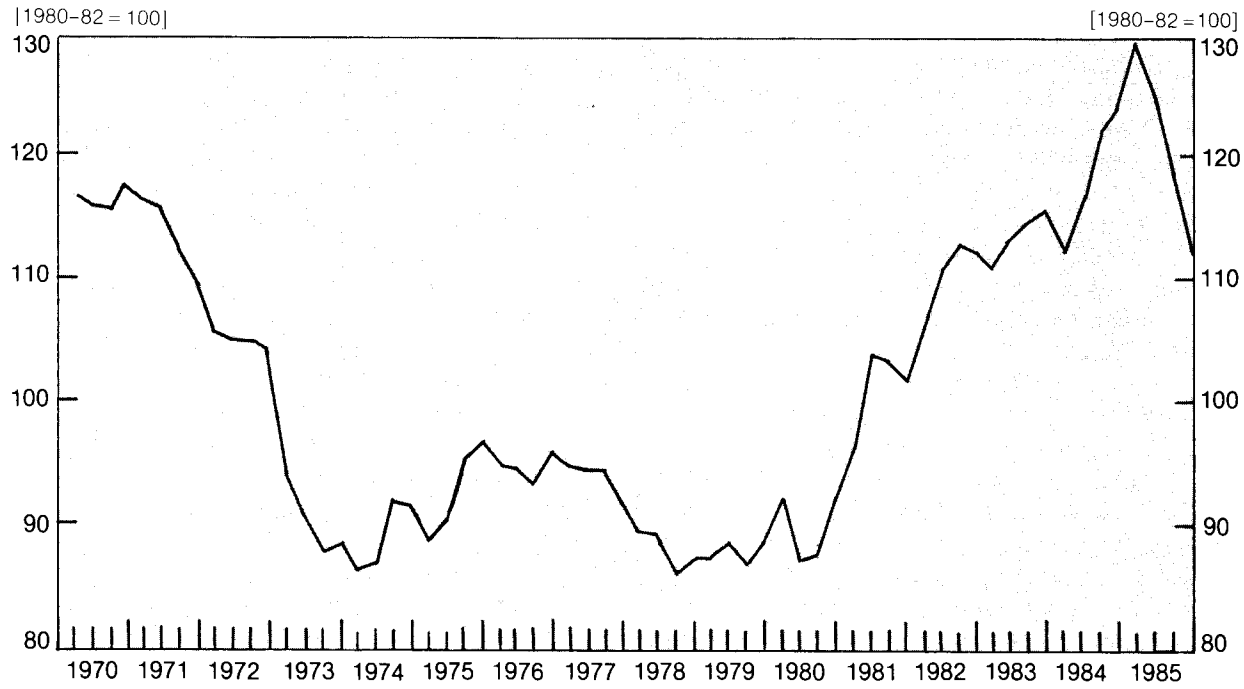
With fuel costs no longer rising rapidly, and disposable incomes increasing, U.S. demand for larger, more luxurious cars has risen in the last few years. The Japanese have altered their import product mix to reflect this change in tastes. With supply limited by the voluntary export restraints, Japanese auto makers have improved comfort and performance features in order to raise prices and profits.[35] This is not completely reflected in the automobile import index, which tracks a fixed basket of automotive styles and factors out price increases due to quality changes in the products priced. Thus the index advanced 6.1 percent for 1985, mirroring moderate price increases for comparable base models. Consumers, however, saw higher prices, and sportier cars, in dealer showrooms.

In recent years, domestic auto makers have responded to increased competition by cutting costs, modernizing plant and equipment, and forming joint ventures with their Japanese rivals. These joint ventures will provide U.S. manufacturers firsthand exposure to Japanese production, inventory, and managerial techniques which have made them leaders in small car production. In turn, the Japanese gain a solid foothold in the lucrative U.S. market. Should the U.S. Congress enact domestic content or import quota legislation, the Japanese will continue to profit from the estimated 1.2 million vehicles that the joint ventures will produce annually in this country by the end of the decade.

Electrical machinery and equipment imports decreased in volume and price last year. U.S. firms imported $18.2 billion worth of these goods in 1985, a 3.3-percent drop from 1984.[36] The import price index for this product group fell 3.6 percent for the year, continuing its downward trend.

Semiconductors constitute roughly 40 percent of the weight of this index. Spurred by increases in spending on personal computers, home electronics, aerospace, and defense in 1984, electronics components manufacturers here and abroad churned out millions of memory chips, transistors, rectifiers, and similar devices. Advances in technology and increasing economies of scale resulted in sizable per-unit cost savings for these products. The explosion in personal computer spending eased in 1985, however, leaving semiconductor supply far ahead of demand. This glut has depressed prices worldwide, causing the import price index for electrical components to fall 14.6 percent for 1985. The glut is expected to last well into 1986.[37] Prices for some specialty items and memory devices began rising late in 1985 as inventories were slowly depleted and buyers feared possible shortages in the spring.[38] In addition, Japanese firms raised their semiconductor prices late in 1985 in response to allegations by the U.S. industry that Japanese goods were being sold in this country at less than cost.[39] The yen's appreciation against the dollar in the fourth quarter also contributed to the price increases. These factors, however, were not enough to reverse the index's downward trend.

Chart 4. Index of the effective real exchange rate of the U.S. dollar, quarterly data, 1970-85



NOTE: Quarter is represented by data for the last month.
SOURCE: International Economics Department, Morgan Guaranty Trust Co.

Price increases were welcome news to U.S. chip makers. In recent years they have been operating under ever lower price ceilings imposed by the large volume of Japanese chips on world markets. For example, one estimate puts Japan in control of 90 percent of the world market for 256K dynamic RAM chips.[40] Domestic chip manufacturers suffered heavy losses and many plants were closed this past summer.[41]

Computer and automated data processing equipment sales growth slowed markedly in 1985, after 25-percent annual growth in the previous 3 years.[42] Some sectors of the market, such as personal computers, actually suffered sales declines.[43] A slowdown in capital spending by the manufacturing sector, which usually accounts for a third of computer sales, and uncertainty surrounding tax reform and its effect on investment contributed to the sales slump.[44] In addition, many of the computers already in use have not delivered promised increases in productivity, which has tended to slow investment in new equipment.[45] Overall, import prices rose 1.6 percent for the year. Prices rebounded modestly in the last half of the year as the dollar weakened against the currencies of our major suppliers, primarily the Japanese.

Prices of imported metalworking and machine tool equipment rose strongly in 1985, boosting the index for those goods 9.1 percent. Buyers stressed reliability, fast delivery, and good service among their reasons for selecting imports over domestic equipment.[46] Indeed, imports rose 23 percent over the first three quarters of the year, capturing over half the U.S. market.[47] Because Japan is America's main supplier of foreign made machine tools, the yearend strengthening of the yen increased prices substantially.

New orders placed with U.S. machine tool manufacturers declined 13.2 percent in 1985,[48] further evidence of the failure of the manufacturing sector to expand in line with the economy as a whole. The curtailing of Federal investment tax credits and the lengthening of depreciation schedules also has made domestic producers apprehensive, as they feel such changes could stall economic growth throughout industry.

Food. Prices for imported food rose 4.8 percent in 1985 after the previous year's decline of 2.3 percent. This index makes up roughly 6.6 percent of the all-import price index. Price increases for coffee, tea, and cocoa and for fruits and vegetables were offset by price declines for meat, sugar, and fish. In fiscal 1985, U.S. food imports were valued at $19.77 billion. Because of declining agricultural exports, the Nation's agricultural trade surplus shrank from $19.10 billion in fiscal 1984 to $11.42 billion in fiscal 1985.[49]

After three quarters of modest declines, imported coffee prices soared 26.4 percent in the last quarter of 1985. This resulted in a 16.7-percent increase in coffee prices for the year. However, U.S. coffee consumption was down from 1.99 cups per person per day in 1984 to 1.83 cups per day.

Last year was also the first year that more soft drinks were consumed than coffee.[50]

The International Coffee Organization (ICO), which is composed of both producing and consuming nations, had increased the export quotas for producing nations in 1984 to 61 million bags. These more liberal quotas may have resulted in the large glut of coffee on the market and an 8-percent reduction in coffee prices over the first three quarters of 1985. The 1984 ICO agreement was intended to keep coffee prices between $1.20 and $1.40 a pound,[51] but by September 1985 the price was down to $1.17 a pound.[52] This prompted the ICO to decrease the quota to 58.0 million bags.[53] This, and more importantly, news of a Brazilian drought in the summer of 1985 sent coffee prices soaring at the end of the year.

Tea prices were on a steep decline in 1985, as an exceptionally good 1984 harvest in Sri Lanka yielded plentiful supplies. Unfortunately, the 1985 Sri Lankan tea crop was of a poor quality because of heavy rains during the growing season. The 1985 harvest was predicted to be 208 million kilos, the smallest crop since 1960.[54] The shortfall in supply is expected to drive up the price of teas in 1986.

In fiscal 1985, the quantity of tea imported by the United States decreased 8 percent from the previous year's level.[55] Demand in this country centers upon the lower priced teas and herbal teas. Thus Argentina, a grower of lower priced teas, exports more of the commodity to the United States than do traditional suppliers such as Indonesia. Tea consumption in the United States declined 2 percent for the year, as cooler weather in the spring and a late summer reduced consumption of iced tea, the most popular form of the product consumed in this country.[56]

Cocoa prices were also down in 1985. The Ivory Coast, Brazil, Malaysia, Ecuador, and Indonesia all had harvests of record proportions during crop year 1984–85. Because of these developments and prospects of an equally large 1985–86 harvest, cocoa prices for the first three quarters of 1985 fell to $2,155 per ton from $2,342 per ton in calendar 1984.[57]

In 1985, prices for imported meat continued their decline. The meat import price index decreased 0.8 percent after the previous year's 1.3-percent drop. Although cow slaughter was down in 1985, the weights of U.S. cattle reached a record level.[58] This caused higher than expected domestic beef supplies, and thus sharp declines in imported meat prices, especially early in the year.[59] This situation was corrected by the fourth quarter of the year.

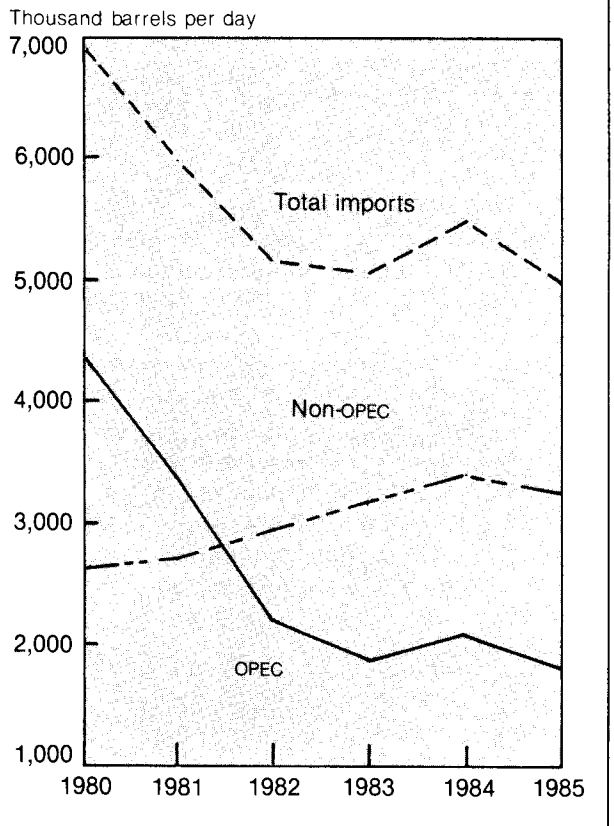
More beef exports come to this country than to any other. However, in recent years, meat imports have leveled off because of the strength of the U.S. Meat Import Law, a lowering of the amount of exportable beef worldwide, and agreements with foreign beef producers to reduce their exports to this country.[60] In 1985, the amount of meat imported into the United States increased only 4.0 percent.[61] Pork imports were 1,128 million pounds, up 15 percent from 1984.[62] Canada and Denmark should account for the greatest increase in pork exports to the United States.

Sugar and sweetener import prices decreased 5.6 percent in 1985. The United States imports one-third of all the sugar that it consumes.[63] The leading sugar exporters are Cuba, the European Community (EC), Australia, Brazil, and the Philippines. In recent years, there has been an oversupply of sugar on the world market. Much of the large buildup of sugar stocks can be traced to policies of the EC. Prior to 1977, the EC was a net importer of sugar, but because of increased production and export subsidies, the Community has now become a net sugar exporter.

U.S. demand for sugar has been decreasing in recent years as high fructose corn syrup (HFCS) and artificial sweeteners are substituted for sugar. Total domestic demand in 1985 is expected to be 8 million tons, 6 percent less than the amount consumed in 1984.[64] In 1981, the United States established quotas for imports of sugar, because their cheaper price was detrimental to domestic producers. The 1985 quota was reduced to 1.8 million tons from 2.5 million tons.

Miscellaneous manufactures. The import price index for

Chart 5. Annual U.S. imports of crude oil and petroleum products, total and for OPEC and non-OPEC sources, 1980-85



SOURCE: U.S. Department of Energy, Energy Information Administration.

miscellaneous manufactured articles rose 0.8 percent in 1985, having declined a scant 0.1 percent in 1984. A 2.9-percent decrease in clothing prices could not offset the increases recorded for footwear; professional, controlling, and scientific instruments; and photographic instruments and supplies.

The U.S. Congress passed a bill in late 1985 that would have restricted imports of textiles, apparel, and footwear. The bill was designed to maintain imports' share of the U.S. textile and apparel market at the level they would have held had the 1974 Multi-Fiber Arrangement been strictly enforced. It is estimated that Far East exporters have increased shipments to the United States 19 percent over the past 4 years.[65] The textile bill, which would have reduced imports by 40 percent, was vetoed by President Reagan in late December. Prior to the veto, however, some of the smaller foreign manufacturers were cutting prices to acquire a larger market share before the proposed quotas could take effect. Also, there were reports of overproduction by South Korean apparel manufacturers.

After several investigations, the U.S. International Trade Commission (ITC) ruled in June 1985 that the domestic footwear industry was being injured by imports of nonrubber footwear. The ITC recommended that the market share of imported footwear be reduced from 71 percent to 68 percent. Lower labor costs have helped foreign shoe manufacturers capture the major share of the U.S. market: the average hourly wage of a shoemaker is $6.71 in the United States, but in Brazil and Taiwan, both major shoe exporters, the averages are $0.85 and $0.91 per hour, respectively.[66] The import price index for footwear declined during the first two quarters of 1985 and then increased during the last half of the year. Prices for U.S. wetblue hides, the main source of shoeleather, began to rise at midyear, boosting the costs of world shoe production. However, the fluctuation in footwear prices resulted in only a 0.1-percent index increase in 1985.

Import prices for photographic apparatus and supplies, optical goods, and watches and clocks increased 3.9 percent. The surge in consumer spending has spurred demand for photographic equipment. The amateur photography market has shifted away from instant and 110 cartridge cameras toward 35 mm cameras, especially compact cameras priced under $100.[67] The 35 mm market is dominated by Japan. In the past 2 years, there has been a great deal of product innovation in this area. Also, increased competition among Japanese firms and their desire to increase U.S. market share caused prices to decline early in 1985. As the year wore on, however, the weakening of the dollar and the approaching Christmas shopping season caused prices to increase. The price for imported photographic supplies slid in 1985 as domestic and Japanese firms competed aggressively in the U.S. market for sensitized film, paper, and plates.

The import price index for collectors' pieces, including gold and silver coins, registered a 4.8-percent decrease in 1985. Prices took a 12.3-percent tumble in the first quarter as investors switched to U.S. dollar denominated investments such as bonds. Prices rebounded in the second quarter as a South African gold mine strike cut gold supplies. In late September, the U.S. Government announced that it was suspending the importation of the South African krugerrand in retaliation for the South African policy of apartheid. Though this should have affected demand for gold coins, prices fell in the fourth quarter, in part because domestic interest rates hit a 6-year low in November.[68]

Crude materials. The crude materials import index, which represents 4.2 percent of all imports, declined 7.8 percent for the year because of oversupply of basic commodities. Global stocks of rubber, lumber, and metalliferous ores all exceeded demand.

Indonesia and Thailand continued expanding rubber out-

Table 3. Changes in Export Price Indexes for selected categories of goods, December 1984–1985

SITC Category	Description	Percent change						
		Annual			Quarterly			
		Percentage of 1980 trade value	Dec. 1983 to Dec. 1984	Dec. 1984 to Dec. 1985	Dec. 1984 to March 1985	March 1985 to June 1985	June 1985 to Sept. 1985	Sept. 1985 to Dec. 1985
	All commodities[1]	100.000	−1.4	−1.3	−0.6	0.0	−1.0	0.3
0	Food	12.768	−11.3	−3.0	−0.7	−1.9	−4.0	3.8
04	Grain and grain preparations	8.341	−12.0	−6.2	−0.5	−2.3	−8.5	5.4
08	Animal feeds, except unmilled cereals	1.332	−30.0	1.2	−11.7	−5.8	10.3	10.2
1	Beverages and tobacco	1.229	−0.2	−2.7	−1.4	0.2	−0.4	−1.1
2	Crude materials	10.948	−9.6	−8.1	−3.8	−0.7	−3.6	−0.1
3	Fuels and related products	3.691	0.5	−3.1	0.4	−0.9	−1.6	−1.0
4	Fats and oils	.911	21.2	−31.4	−4.0	1.8	−20.8	−11.4
5	Chemicals and related products	9.578	−0.9	−1.1	−0.7	−0.2	0.3	−0.5
51	Organic chemicals	2.289	−5.3	0.7	−1.0	2.9	0.6	−1.8
56	Fertilizers, manufactured	1.036	−2.1	−5.1	−2.4	−5.0	2.2	0.2
6	Intermediate manufactured products	10.544	0.4	−1.2	−1.0	−0.2	0.0	0.0
7	Machinery and transport equipment, except military and commercial aircraft	35.261	3.3	1.3	0.6	0.5	0.1	0.1
71	Power generating machinery and equipment	3.943	8.5	0.1	−1.3	1.3	−0.2	0.3
72	Machinery specialized for particular industries	5.784	1.5	1.8	1.0	0.5	0.2	0.1
73	Metalworking machinery	.829	2.2	4.3	1.0	1.1	0.8	1.3
75	Office machines and automatic data processing equipment	3.990	−1.1	−2.0	−0.5	−0.9	−0.1	−0.5
77	Electrical machinery and equipment	4.738	4.4	−0.7	0.3	1.0	−0.7	−1.3
78	Road vehicles and parts	6.726	2.3	2.4	1.0	0.6	−0.1	0.9
8	Miscellaneous manufactured articles	7.397	−0.9	1.0	0.2	0.9	−0.1	0.0

[1] This category includes indexes in addition to those shown here. For all of the indexes available in each category, see *U.S. Import and Export Indexes*, USDL–86–38 (Bureau of Labor Statistics), January 30, 1986.

put despite flat demand. The increasing switch from bias ply to radial tires has left excess rubber on world markets. Longer wearing radial tires require less frequent replacement, and hence, less rubber than their bias ply counterparts. The resulting oversupply of rubber has driven prices down. The imported crude rubber index declined 12.6 percent for the year despite some price firming in the fourth quarter. In response to declining prices, Malaysian growers are switching from rubber to palm planting in order to increase future earnings.

Despite mill closings, the U.S. lumber industry continued to suffer from overcapacity in 1985. This dampened corporate profits and import prices alike.[69] The index for wood imports fell 4.4 percent for the year, reflecting a number of developments here and abroad. In 1985, an estimated 1.736 million homes were started in the United States, slightly less than the 1984 total of 1.749 million units.[70] The decrease in housing starts may reflect the decision of potential homebuyers to wait for mortgage rates to bottom out.[71] In addition, the strong building boom of 1982–84 may have satisfied pent-up housing demand.

The pulp and waste paper index plunged nearly 20 percent for the year, as Brazil, Chile, Spain, Portugal, and South Africa stepped up pulp production in order to earn foreign currency.[72] Lack of profits in the U.S. lumber industry, coupled with the prospect of tax reform which would raise the cost of farming timberland, forced many U.S. firms to abandon all or part of their lumber business in 1985.

Imported metalliferous ore prices also declined, as domestic aluminum and stainless steel production decreased last year. In 1985, primary aluminum production in the United States was 14.6 percent below 1984's volume of 4.518 million short tons.[73] Meanwhile, U.S. stainless steel production for the year was 4 percent lower than 1984 levels.[74] These declines dampened demand for bauxite and alumina used in aluminum production, and for ores of tantalum, zinc, columbium, and other metals used in steel alloying. Imported metalliferous ore prices fell 5.8 percent as a result.

Intermediate manufactures. In October 1984, the Reagan administration negotiated voluntary export restraints with 15 nations supplying steel to the United States. The goal of these restraints was to limit foreign suppliers to 18.5 percent of the U.S. steel market. Through the first three quarters of 1985, imports from these countries were 14.4 percent below the previous year's 9-month mark.[75] But imports from other nations continued to rise. In fact, 18 nations without any known steelmaking facilities were listed as suppliers to the United States last year, including such small countries as Antigua, the Netherlands Antilles, New Caledonia, and the Bahamas. Some of these shipments were in the form of processed steel products, which had been finished at facilities in the exporting nations. In other cases, however, U.S. steelmakers charged that major producing countries had violated their quota agreements by shipping steel through neighboring nations in order to avoid exceeding their own quotas.[76] Altogether, foreign steel captured an estimated 25.2 percent of the U.S market last year, down slightly from 26.4 percent in 1984.[77]

These imports encountered falling prices in the United States, as a result of overcapacity and declining demand. By one estimate, annual Free World steel production capacity currently is 625 million metric tons, whereas Free World demand is only 440 million metric tons.[78] This excess supply comes at a time when American users are reducing demand for steel,[79] because of an increase in automobile imports and a continuation of the switch from steel to plastics and other metals in the manufacture of packaging and automotive products. Reduced consumption led to price cutting by suppliers. The import price index for iron and steel declined 4.4 percent over the course of the year.

The nonferrous metals fared little better last year. In late October, the International Tin Council announced it could no longer afford to purchase excess tin stocks from producers in order to shore up the metal's price on the London Metal Exchange.[80] This decision sent tremors through the Exchange; tin trading was suspended, and prices of nickel, zinc, and other metals fell as dealers sold contracts for those commodities quickly to raise funds to cover their potential tin losses. At the time of the trading suspension, metals dealers held contracts for more than 50,000 tons of tin at the Exchange's price of $12,100 per ton.[81] The extent of traders' losses will not be known until trading resumes. Off the London Metals Exchange, tin was selling for $2,000 below the Exchange price. If prices fall rapidly once trading is resumed, the world's major metals traders could be forced into bankruptcy. In the United States, prices for imported tin fell 19.6 percent in the fourth quarter of 1985, and 16.5 percent for the year as a whole.

Platinum and silver prices were depressed early in the year, as continued low rates of inflation in the United States reduced the appeal of the two metals as inflationary investment hedges. As interest rates declined, however, platinum and silver became more attractive for investors whose return on paper assets was falling. Also, demand from the U.S. auto industry, which uses platinum in emissions control devices, increased during the second quarter as Detroit reported its highest quarterly output for the year. Fears that supplies from the Republic of South Africa, the world's number one platinum producer, might be interrupted, drove up prices late in the year.[82] Altogether, the index finished the year down 9.7 percent.

Copper import prices rose slightly in 1985, as U.S. metals firms continued to reduce capacity and to rely heavily on imports. Third World nations such as Chile and Zambia have been exporting copper extensively in order to obtain foreign exchange to service foreign debt.[83] U.S. copper imports as a percentage of consumption reached an estimated 27 percent last year, after claiming 23 percent of the

U.S. market in 1984.[84]

Nickel import prices rose in the beginning of 1985, as output failed to keep pace with demand.[85] The United States imports most of the nickel that it uses in petroleum refining, and in chemical, electrical, construction, and aircraft industries. Although activity in these industries remained vigorous late in the year, uncertainty surrounding the fate of the London Metal Exchange and its dealers caused the metal's price to fall by yearend. Overall, the import index for nickel was down 5.5 percent for the year.

Fats and oils. The fats and oils import index plummeted 56 percent for the year, reflecting abundant stocks of Malaysian palm oil, Philippine coconut oil, Argentinian sunflower seed oil, and Brazilian cottonseed oil.[86] Malaysian palm oil production, for example, was 24 percent higher in October 1985 than in October 1984.[87]

Export price trends

Machinery and transport equipment. Price advances in exports of U.S.-made machinery and transport equipment moderated in 1985. After rising 3.3 percent in 1984, the export index for these products increased a mere 1.3 percent last year. The index encompasses more than a third of the all-export index.

Prices for exported general industrial machinery, metal working machinery, specialized machinery, power generating machinery, and autos all rose. On the other hand, prices of exported semiconductors and automated data processing equipment were lower. Telecommunications equipment export prices were virtually unchanged for the year.

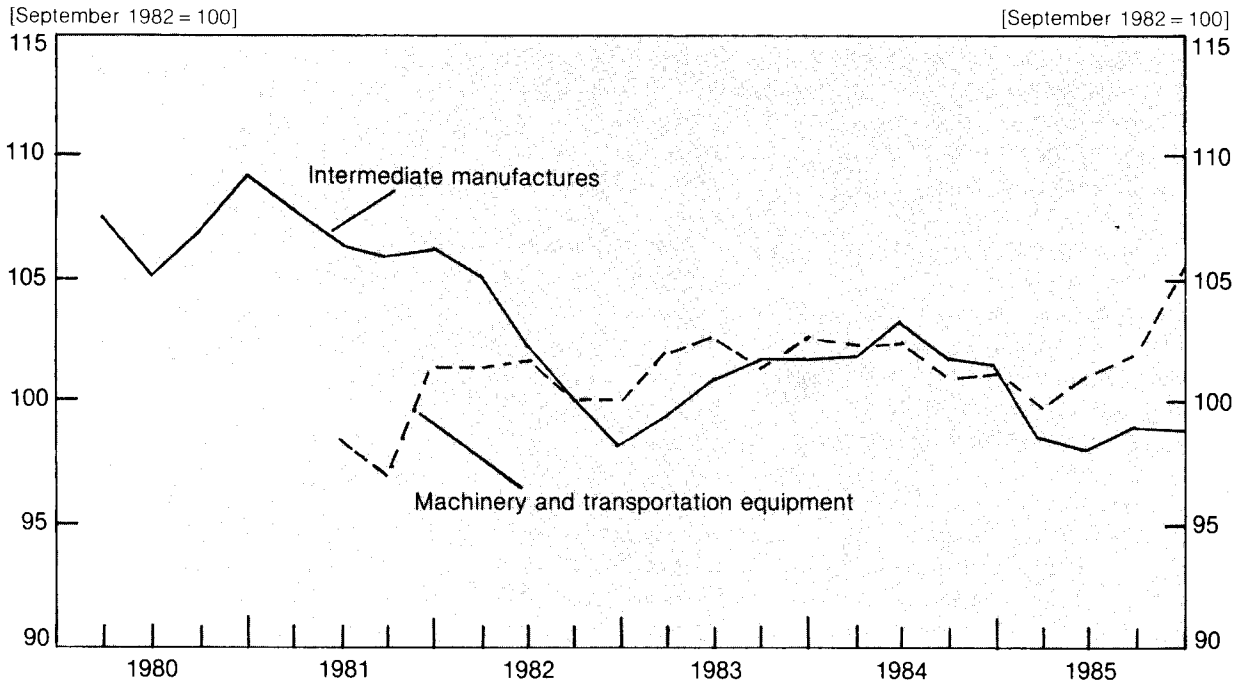
The dollar volume of machine tool exports in the first three quarters of 1985 was 12 percent higher than for the comparable period of the previous year.[88] Prices for these items advanced 4.3 percent for 1985 as a whole, continuing their strong upward trend.

The index for power generating machinery advanced a slight 0.1 percent, fueled by the 2.4-percent price rise for engine replacement parts.

The road vehicles and parts index advanced 2.4 percent for the year. This also was largely attributable to price increases for parts. In the fourth quarter, however, automobile export prices rose 2.1 percent, reflecting new model year price increases. For the year as a whole, automobile export prices advanced 4.2 percent, and parts prices increased 1.8 percent.

Automated data processing equipment, telecommunications equipment, and semiconductor export prices were constrained by several factors in 1985. First, the emergence of South Korea as a low-cost producer in these fields limited the pricing power of U.S. firms in global markets. Secondly, delivery delays and uncertainty concerning the new products developed by U.S. producers for the year caused many overseas buyers to adopt a "wait and see" attitude

Chart 6. U.S. import price indexes for selected commodity groups, quarterly data, 1980-85



toward new equipment purchases.[89] Lastly, rapid advances in technology have shortened product lifespans in these areas. Fiber optics, gallium arsenide integrated circuits, and small, personal-computer-compatible hard disk drives are steadily replacing existing product lines. This resulted in price cutting to move inventories before they become obsolete.

Food. For U.S. agricultural exporters, 1985 was a difficult year. Large crop yields caused an oversupply of grain on the market, and forced export prices down. This was reflected in the U.S. export price index for food, which declined 3.0 percent in 1985. This index comprises 12.8 percent of the all-export index. A 6.2-percent decline was recorded in the grain and grain preparations index, but the index for animal feeds was up 1.2 percent. Those two indexes account for 80 percent of the export food price index. Export prices for wheat, rice, barley, yellow corn, and yellow sorghum declined.

Record yields of corn, oats, sorghum, and rice were produced in the United States in 1985, the year of the second highest total crop production ever recorded. This occured even though 7 million fewer acres of land were in production than during the previous year.[90] Coupled with large existing inventories from 1984, this development meant supply exceeded demand.[91] In addition, two of the Nation's large customers, the Soviet Union and China, increased agricultural production last year. With the competition from agricultural exporting countries strong, the U.S. share of world agricultural exports is expected to show a decline again in 1985, following a drop to $31 billion in 1984.[92]

Wheat prices were significantly lower in 1985. The export price index for wheat declined 4.9 percent for the year, compared with a decrease of only 0.2 percent in 1984. Worldwide import demand in marketing year 1985–86 was expected to be the lowest since 1979–80 because of abundant yields in many importing countries.[93] In 1984–85, there had been a record worldwide yield of wheat. In 1985–86, the yield is expected to be lower but still above the level recorded in 1983–84. Although the 1985 U.S. wheat yield is expected to be near the 1984 level, production by the United States' four major competitors (Australia, Argentina, Canada, and the EC) is expected to be 10 million tons below year-earlier levels. The declining yields of competitors were caused by planting problems and a switch to different types of crops. However, excess accumulated inventory should negate the effects of the lower yields.[94]

Both Canada and the EC experienced problems with the quality of the wheat they grew in 1985. Because of weather problems, the amount of Canadian wheat in the top two grades was down. This prompted the Canadian Wheat Board to suspend sales to all but Canada's usual customers.[95] To combat their quality problem with wheat, the EC released bread wheats from their stockpiles.

Some of the EC's agricultural policies are undermining the United States' export trade. In 1985, the Community increased export subsidies on sales to countries targeted in the U.S. export enhancement program, especially those of North Africa.[96] The U.S. program, The Bonus Incentive Commodity Program (BICEP), which was announced May 15, 1985, is designed to allow government commodity stocks to be given as bonuses to importers of designated U.S. agricultural commodities over the next 3 years.[97]

The 1984–85 worldwide production of coarse grains was 810.24 million tons. Coarse grains include barley, sorghum, corn, rye, and oats, which are primarily used as animal feeds. For 1985–86, production is expected to reach 844 million tons.[98] The United States produces one-third of the world's coarse grains, and within that, one-half of all corn grown. The corn export index was down 7.6 percent in 1985. The U.S. supplies of coarse grains were very large because of good weather and increased planting; the Nation's total 1985 production is estimated to be 271 million tons.[99] The yield of the United States' major competitors is also expected to be large. Although production by Australia and Argentina may be down, Canada, Thailand, and South Africa expect a good output. In fact, corn yields from Canada's eastern provinces are expected to exceed all previous records.[100]

Demand for coarse grains is expected to decrease by 8 percent in 1985–86.[101] This is largely attributable to lower purchases by the Soviet Union, which both boosted coarse grain production in 1985 and had a decrease in livestock. Purchases by that nation may drop as much as 10 million tons.[102] The United States' second leading export market is Japan. Although U.S. sales to Japan decreased in 1984 because of competition from Chinese and Thai corn, this situation may change as Japanese imports are expected to increase to 21.5 million tons in 1985.[103] All U.S. agricultural exports have been hurt by the strong dollar, which makes the Nation's products more expensive in foreign currencies. Also, coarse grain sales have been affected by austerity programs implemented by some of the developing countries, declining EC imports of corn and increased exports of barley, and higher U.S. agricultural support prices.[104] The support prices, which keep U.S. farm prices higher than they would be in a free market, have encouraged many nations to develop their farm sectors and to increase agricultural output.

Chemicals. The index for exported chemicals decreased 1.1 percent in 1985, after declining 0.9 percent in 1984. Historically, the United States has enjoyed a trade surplus in the chemical industry due to its leadership in product innovation. Similarly, large investments in research and development have led to greater production efficiency. The Nation's chemical industry remained relatively unscathed by the effects of the strong U.S. dollar, with exports decreasing only 2.5 percent in 1985. However, the industry is facing stiffer competition worldwide. For example, many of the

oil-producing nations have set up petrochemical operations. With abundant supplies of low-cost inputs, these producers are further contributing to world oversupply and lower prices.[105]

The problem of worldwide oversupply greatly affected the fertilizer industry in 1985. A 12- to 15-percent oversupply of phosphate chemicals and phosphate rock on world markets resulted in price cutting early in the year.[106] Producers claimed to be selling at or below production costs, and a number of high-cost U.S. manufacturers were forced out of business. Prices for fertilizer components also fell over the year. Anhydrous ammonia, a major input in fertilizer production, experienced a drastic reduction in export prices. The index in which this compound is included—inorganic elements, oxides, and salts—declined 13.7 percent in 1985. Toward the end of 1985, the oversupply of fertilizer began to diminish as stocks were depleted, and prices subsequently rose. In the last two quarters of the year, the export index for fertilizers rose 2.4 percent.

In 1985, the United States enjoyed an increase in exports of propylene, which is used chiefly for organic synthesis. In the past, U.S. exports of propylene have been limited to Canada and Mexico because overseas shipment of the substance requires the use of refrigerated gas carriers. In 1985, a fire in an ethylene/propylene plant in Italy significantly reduced supplies in southern Europe. This, along with the tremendous price differential between European and U.S. propylene gave U.S. producers an incentive to expand into European markets. (European prices are estimated to be $410–$415 per metric ton while U.S. prices are running about $345–$350.[107]) A Far East market also appears to be opening up. The increased demand for propylene caused prices in the export index for hydrocarbons to rise 1.8 percent for the year. □

——FOOTNOTES——

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[1] Exchange rate indicated is the real trade-weighted exchange rate. See *World Financial Markets* (New York, Morgan Guaranty Trust Company, International Economics Department), December 1985, p. 4.

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