THE AUTOMOBILE INDUSTRY AND WORLD ECONOMY

JOINT HEARING

BEFORE THE

SUBCOMMITTEE ON INTERNATIONAL FINANCE

AND THE

SUBCOMMITTEE ON ECONOMIC STABILIZATION

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

NINETY-SIXTH CONGRESS

SECOND SESSION

ON

PROBLEMS OF THE AUTOMOBILE INDUSTRY AND ITS CURRENT AND FUTURE ROLE IN THE DOMESTIC AND WORLD ECONOMY

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WEDNESDAY, June 18, 1980

CHARTS AND TABLES

THE AUTOMOBILE INDUSTRY AND WORLD ECONOMY

WEDNESDAY, JUNE 18, 1980

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON INTERNATIONAL FINANCE, AND
SUBCOMMITTEE ON ECONOMIC STABILIZATION,
Washington, D.C.

The subcommittees met at 10 a.m., in room 5302, Dirksen Senate Office Building, Senator Adlai E. Stevenson presiding.

Also present: Senator Donald W. Riegle, Jr., and Senator Richard G. Lugar.

OPENING STATEMENT OF SENATOR RIEGLE

Senator RIEGLE [presiding]. The committee will come to order.

Let me start by indicating that we are somewhat delayed this morning because we scheduled as a first order of business on the Senate floor today a resolution that would set forth a general policy for dealing with the urgent problems facing the American automobile and truck industry.

We have just finished a debate on that, and we will be voting on it this afternoon at 1:30. I might say that it's been cosponsored by 75 Senators, the majority of both parties. I think it is significant that that debate has just concluded and the vote will occur today, and that this joint hearing this morning, occurs against that backdrop.

Senator Stevenson, chairman of the Subcommittee on International Finance, will be here shortly, and I appreciate his courtesy, and all of you that are here, in working around the floor schedule this morning.

This joint hearing today between the Subcommittee on International Finance and the Subcommittee on Economic Stabilization, wishes to welcome the witnesses and others in attendance at these hearings on the auto industry and the world economy.

Auto manufacturing is the keystone of this Nation's economy. It directly creates one out of every 12 manufacturing jobs and generates prime demand for such basic industries as steel, aluminum, rubber, textiles, machine tooling and, increasingly, electronics. It affects the economy of every State, and its health is vital to some 50,000 small- and medium-sized supplier firms across the 50 States, and to some 27,000 auto dealers.

The U.S. auto industry today is in serious difficulty. Sales and production have fallen by the largest amount in 20 years. Last month, 295,000 auto workers were out of work, causing layoffs of

an additional 885,000 workers in related industries, a total well above 1 million workers.

Since April 1979, 850 auto dealers have gone out of business, and failure threatens hundreds more in the next few days, weeks, and months.

The industry's collapse is costing Federal, State, and local governments over $10 billion in lost revenues and additional spending for unemployment compensation, food stamps, and social services.

And I would note that one of the feature stories on the front page of the Wall Street Journal today deals with this problem as it's impacting individual States. Not surprisingly, the State of Michigan is one of the worst hit. It leads the list in terms of economic distress and has been forced to make enormous cutbacks in State spending due to shortfalls of revenues, and increases in expenditures for the kinds of transfer payments I have just mentioned.

The Japanese efforts to further penetrate the U.S. market, are I think, escalating these problems into a catastrophe. Japanese imports now exceed 23 percent of the U.S. market, and the Japanese are expanding their manufacturing capacity enough to be able to supply 50 percent or more of this country's small car market.

That could cause a massive permanent loss of U.S. jobs and a widening of our trade deficit.

So we face here an historic challenge. I believe the United States must not become dependent upon foreign countries to meet our basic future need for vehicles to transport goods and people. American industry must be thoroughly converted to produce the advanced new vehicles that are needed for the 1980's and for future decades.

Some of the deterioration in the industry is temporary having been caused by higher interest rates and lower real disposable income. But there is the greater danger that the increase in Japanese imported autos and trucks will lead to a lasting structural deterioration and dislocation in the industrial base of the United States.

The focus of these hearings is on the impact of import competition, especially competition from Japanese auto makers. At the hearing on April 3 of this year we examined the economic effects on output, employment, prices, and energy consumption of the imposition of quotas, tariff equivalents, or orderly marketing agreement equivalents designed to reduce the Japanese market share.

Today's hearing is designed to further that inquiry by raising a set of related questions. The testimony provided by the administration officials on April 3 left open the question of whether the industry can recover the share of the market that has now been lost to imports, once the new small car capacity comes onstream. Will we recover our share, or will we discover that the share has been permanently lost, that the level of activity in our industry will be permanently reduced, and that the outlook is for more or less permanent overcapacity in the world auto industry?

Issues central to these questions are the following:

How long will it take for the U.S. industry to downsize and make other changes needed to regain its competitive position?

Can this time period be shortened? And if so, how can public policy assist this process?

When will the domestic industry be fully competitive vis-a-vis foreign rivals in both domestic and foreign markets?

What are the obstacles to attaining such competitive parity?

Is there evidence that the current plight of the industry is causing irreparable and irreversible damage to the infrastructure of supplier and dealers of a magnitude that will reduce supplier capacity and therefore permanently downgrade the relative importance of auto manufacturing in our national economy.

Overhanging the industry is the all-important question of financing. Estimates of capital requirements suggest that the industry will need about $80 billion between 1979 and 1985 in order to carry out the retooling needed to become fully competitive and to meet mandated standards.

Is it reasonable to expect the companies to raise this much money privately? Will public assistance be required? And, if so, is such public assistance desirable, and what form should it take?

There are also many trade issues. What can and cannot be done to ease competitive conditions for the domestic auto industry within the rules of acceptable international commercial behavior? What are the antitrust implications of various forms of import limitations, including voluntary restrictions? Could temporary or permanent quotas on imports be imposed without violating the rules of GATT and other trade agreements?

What is the likelihood that auto import restrictions will cause retaliation, harm our export trade, and possibly cause a trade war?

What are the prospects for expansion of U.S. auto exports and auto investments throughout the world? To what extent are foreign markets sheltered by tariffs, local content requirements, discriminatory taxation, and other barriers to market penetration?

Is it reasonable to continue a policy of free trade in autos in a world environment in which only the U.S. market is relatively free of import restrictions?

There are, finally, some long-range questions that need study. For example, what are the consequences of continuing increases in oil prices and supply disruptions? Should we begin now to assume that such increases are inevitable, and therefore should we begin to plan accordingly.

The witnesses that we have assembled for this morning's hearings are eminently qualified experts who can help us deal with these issues.

They are Dr. Robert Baldwin, of the University of Wisconsin; Dr. David Cole, of the University of Michigan; Ms. Maryann Keller who is with Paine Webber Mitchell Hutchins; and Dr. Harald Malmgren, who is a former deputy special representative for trade negotiations.

We welcome this distinguished panel.

Senator Stevenson, I have just made an opening statement, and I presume you may have one as well.

Senator STEVENSON. I will enter my statement in the record for fear of repeating what you have already said. I join you in welcoming our witnesses.

OPENING STATEMENT OF SENATOR STEVENSON

Senator STEVENSON. This is the second morning of hearings devoted to a joint consideration by the Subcommittee on International Finance and the Subcommittee on Economic Stabilization of the competitive position of the U.S. auto industry. Earlier, we heard testimony from Prof. William Abernathy of the Harvard Business School, Dr. George Eads of the Council of Economic Advisers and Robert Hormats of the Special Trade Representative's Office. The witnesses discussed the nature of the U.S. auto industry's current problems, Japanese import penetration, and the economic effects of possible import restrictions on Japanese cars. The witnesses concluded that import quotas or higher tariffs would produce limited benefits for the U.S. industry, would force consumers to pay higher prices for both domestic and imported autos, and would have a detrimental effect on our trade relations which, in their opinion, outweighed the likely benefits. The hearings did not take up the crucial question of the long-term competitiveness of the U.S. industry and the ability of U.S. producers to recapture lost market shares once their new small car capacity comes onstream. These questions we will put to today's witnesses—Maryann Keller of Paine Webber Mitchell Hutchins Inc., Dr. David Cole of the University of Michigan, Dr. Harold Malmgren of Malmgren Incorporated, and Dr. Robert Baldwin of the University of Wisconsin.

The position in which the U.S. auto industry finds itself is without precedent, but symptomatic of the more general decline of U.S. industry in competitive global markets. Imports claim 27 percent of the U.S. auto market; some 300,000 workers are on temporary or indefinite layoff; domestic automakers are sustaining the largest losses in corporate history on their domestic production; and only a government bailout, yet to be finalized, has thus far averted Chrysler's bankruptcy. Between now and 1985 Detroit will have to raise an estimated $80 billion for retooling in a bid for restored competitiveness, which has been termed the most radical "dematuring" of an industry ever.

Although current investment strategies will expand domestic small car production to 10–11 million by 1985—from 1.7 million in 1980—it is far from clear that the share of the U.S. market going to foreign imports will decline correspondingly. Restored competitiveness demands more than parity. It will not be achieved if Detroit contents itself with production plans for 1985 which only endeavor to match the quality and fuel efficiency of today's Japanese and German models.

There are questions about the long-term shape of the world auto industry and domestic employment levels that are going unanswered in all our hearings. The fastest growing markets may be outside the United States, Europe or Japan—in the Third World—and the emergence of the so-called "world car" will allow manufacturers to integrate and rationalize their global operations, producing where costs are lowest. The impact such trends may have on U.S. employment has not been addressed. Restored U.S. competitiveness will demand significantly higher productivity and labor economies built into plants over the next decade, all of which suggest that a real decline in domestic auto employment is inevitable, and could be substantial.

I'm told a Datsun plant in Japan manned by 67 workers produces 1,300 cars per day. The United States cannot meet this competition without moving substantially in the same direction, more efficient production of higher quality, more fuel-efficient automobiles. Volkswagen could put a 60-mile per gallon Rabbit into production tomorrow. Yet our estimates of domestic capital requirements seem to assume that the world will stand still while domestic producers catch up. That assumption is unrealistic. Assumptions about the price and availability of fuel for discretionary driving in the mid to late 1980's tend to be optimistic. I urge our witnesses to address the industry's assumptions.

Auto production is at the core of the U.S. economy, directly or indirectly employing one out of every five American workers. The Federal Government, as well as the industry, bears responsibility for long encouraging consumer demand for large, fuel-thirsty cars. Now it bears some responsibility for assisting the industry—but not with the trade protection which has never produced the revitalization of an industry and never failed to produce inflation, inefficiency, and retaliation.

We welcome the testimony of this morning's witnesses.

Senator STEVENSON [presiding]. We have had many hearings now in this committee and others on the condition of the automobile industry, and I would just like to underscore one point. I, and others, have repeatedly asked our witnesses in these hearings what their assumptions are with respect to the plans and projections of foreign automobile producers and when they make their own projections of the capital requirements of domestic producers.

We make various projections. $80 billion, for example, is estimated by, the Congressional Budget Office to be required for the auto industry over the next 5 years. We make certain assumptions about the requirements for automobile technology, and fuel efficiency, but these assumptions seem to include the assumption that the world is going to stand still.

We don't get answers to our questions, as Senator Riegle was indicating, about the price and availability of fuel in the mid to late 1980's, and the implications for discretionary driving.

Volkswagen has a 60-mile-per-gallon vehicle it could put into production tomorrow. It has an 80-mile-per-gallon vehicle it's moving along in development, while our plans and only our most ambitious plans—assume fuel efficiency standards by 1990 of 40 miles per gallon for U.S. fleet averages. Those are averages the Germans can almost achieve today.

Instead of assuming a static world, I hope by considering the condition of this large, vital industry, we can make more realistic assumptions about a rapidly changing world, about the development of markets which may or may not materialize in the less developed countries, about the implications of production of world cars, offshore production facilities closer to inexpensive labor markets, declining employment here, and also about the technology and the capital investments of foreign producers, not just with respect to the automobiles, but with respect to facilities for the production of automobiles as well.

Japan's Nissan Co. produces some 1,300 Datsuns a day, with 67 production line workers.

It's not just a high quality or fuel-efficient automobile, but also the efficient production of that vehicle that is required if the U.S. auto industry, if it is to survive. And survival, I think, means not just catching up, but leapfrogging, and no one has yet told us what we have to leapfrog or catch up with in this very competitive world market.

Thank you, Senator Riegle.

Senator RIEGLE. Dr. Cole, let us start with you. I know you have another appointment earlier than the other witnesses. Let me ask all of you, if you can, to summarize your statements. We will put your entire statements in the record, but to the extent that you can summarize, that will give us more time for discussion. So we invite you to begin, if you would.

STATEMENT OF DAVID COLE, DIRECTOR, OFFICE FOR THE STUDY OF AUTOMOTIVE TRANSPORTATION, UNIVERSITY OF MICHIGAN

Dr. COLE. Chairman Riegle, Chairman Stevenson, and members of the subcommittees, I appreciate the opportunity to discuss the problems of the automotive industry and its present and future role in the domestic and world economy.

The industry is still strong and competitive, but it is beset by severe temporary problems that could have lasting effects. Therefore, this inquiry is very timely.

In my testimony today, I will begin with a brief discussion of the recent history and probable trends in automotive technology in the market. I will then consider industry capital requirements and the status of the vehicle manufacturers and their suppliers and dealers. I will conclude with some remarks on the competitive situation and research needs. A more complete discussion, as Senator Riegle has mentioned, is included in my written statement.

As a faculty member at the University of Michigan, I draw on a long, distinguished, and growing record of cooperation and helpful interaction between the university, government, labor, and industry. The University of Michigan has contributed to the education of a significant share of the industry's technical and business leaders. Practically every aspect of the automotive transportation system is studied in depth, including both technological and nontechnological factors.

We are deeply involved in problem-solving and identification and have moved from the ivory towers. I and my colleague, Mr. Lawrence Harbeck, who is with me here today, have developed and directed an annual automotive industry seminar that is a leading forum for interactive, two-way discussions between vehicle manufacturers, their suppliers, and representatives of labor and government.

The university's primary responsibilities remain those of teaching and research, but there is no conflict between these missions and the shirtsleeves participation in the real world.

The automotive industry has made mistakes, of course. But in judging it, it is only fair to keep the following sequence of events before us:

For most of the post-World War II period, the real cost of energy was dropping.

Partially as a consequence of the declining real cost of gasoline and resultant consumer perceptions and demand, North American passenger cars became large and heavy.

In Europe and Japan, where cars were not so much of a necessity, gasoline prices were kept high by adding taxes. Also, punitive taxes were placed on weight and horsepower.

Because of higher costs, narrower roads, and shorter distances traveled, cars in Europe and Japan were small and economical.

IMPORTS ONLY RECENT FACTOR

Imported cars were not a major factor in the United States until the 1970's. But even between 1970 and 1972, while import sales were edging up from 1.2 to 1.5 million units, sales of domestic cars increased from 7.2 to almost 10 million units. The increase alone in domestic car sales was almost twice the level of import sales.

In late 1975 and early 1976, when many of the decisions concerning 1980 model cars were being made, import sales had just suffered a tremendous drop in penetration—from 21.7 percent in March of 1975 to 11.6 percent in November, a decline of almost 50 percent in only 6 months.

During this same period, Government-mandated gasoline prices remained essentially unchanged at about half of today's level.

A little over 1 year ago, large domestic passenger cars were selling well, and import sales remained depressed. Dealer inventories of imports were near record highs.

Now that the American consumer has seen the light, and also essentially decontrolled gasoline prices for the first time, small-sized U.S. and import cars are suddenly popular again. Import manufacturers can meet added demand for small cars by working overtime in large capacity, small-car facilities.

American vehicle manufacturers, led by many years of big car demand, based in part on artificially low fuel prices, must catch up, and it will take time and money to build the facilities to do this.

Recently I participated in the design and management of a major survey of technical, marketing, and administrative decisionmakers in the automotive and supplier industry.

We developed a consensus view of the automotive future in the study.

CONSENSUS VIEW OF THE AUTOMOTIVE FUTURE

Automotive engines of the future will be predominantly in line four-cylinder and V–6 designs. In 1990, four-cylinder engines may account for at high as 75 percent of total production. Diesel engines should reach 25-percent penetration, and electric powered vehicles could account for 5 percent of sales by 1990.

More exotic engine concepts, such as the gas turbine or the Stirling engine are not expected in the 1980's.

The front engine, front drive concept with the engine located transversely in the vehicle will become the predominant passenger car drive train in this country.

The conversion to new engines and new drive trains will be enormously expensive.

Electronics are expected to play an increasingly prominent role, and in general, lightweight materials will come into far greater use

in the never-ending drive of the automotive designer to maintain the largest possible passenger and load volume, while reducing weight to minimize fuel consumption.

The average weight of the U.S. produced car should drop from 3,300 pounds in 1980 to 2,900 pounds in 1985; and finally to 2,500 pounds in 1990. Steel and cast iron use will be reduced significantly. At the same time, plastic, in all its various forms, and aluminum use will expand dramatically.

The many advances predicted will require additional work on the part of the U.S. automotive industry, but these improvements could not occur in the relatively short timeframe considered if the industry had not made a major effort in recent years to get these programs started, even before the belated recognition by the U.S. consumer that energy problems are real.

The marketing panelists in our survey forecasted a 2 percent annual sales growth in automotive sales through 1990. The total U.S. market is expected to be in the range of 11 to 12 million cars by 1985, and 12.5 to 13 million units in 1990.

A major change in the distribution of car sizes is anticipated and, in fact, size may cease to be an important distinguishing factor in the marketplace. The general overall marketing trend can be summarized as a modest sales increase of more durable, efficient, and smaller vehicles through the coming decade.

We have seen a wide range of estimates of capital that will be required by 1985. Our estimate is $25 billion per year from 1979 through 1985. Over the 5-year period, this figure could include $75 billion for U.S. motor vehicle manufacturers, and very importantly, $50 billion for the U.S. suppliers.

Any present-day estimate can be quickly reduced, of course, if poor vehicle sales or other circumstances make such enormous investments impossible. Any forced decline in capital spending delays the restoration of full competitiveness for the U.S. automotive manufacturers.

Perhaps the only uncertainty about the industry's capital needs is that they are large beyond comprehension and will create immense financial strains.

Any reasonable action that can be taken to relieve the pressure will help accelerate progress. Perhaps the best way to help would be immediate changes in depreciation regulations to allow an equally immediate improvement in internally generated cash flow.

Related steps could include provisions to permit a more rapid write off and/or increased investment tax credit for special tools needed for Government-mandated items, and the fast refunding of taxes to companies not in a profit position. New production facilities obsoleted by recent market trends could be considered for more rapid write off, as well.

Inseparable from the automotive industry's capital problems is the overall capital investment situation in the United States. Recent estimates indicate that capital investment as a percent of GNP is 20 percent in Japan; 15 percent in Germany; but only 10 percent here.

These data would indicate that investing in Japan and Germany is more attractive. We would benefit from Government policies that offer more encouragement to savings and investment.

It is important to keep in mind the long leadtime between management decisions and production for the market. Years are required to make a modification, that is to produce a new model, or to produce much larger quantities of an existing model.

Long leadtimes are caused by several limiting factors, including financing, availability of trained engineers and other personnel, and limited ability of the machine tool industry to supply advanced production equipment.

Capital and financing problems are particularly severe today because of the premature obsolescence of huge amounts of existing capital equipment that were designed to produce in large quantities vehicles that are now selling at low volume.

Major losses of capital investment hurt the U.S. automotive industry more than they would automotive industries in other countries, because the U.S. industry is particularly dependent on using capital investment to offset high labor costs.

The only way the United States can be productively competitive is by investing more per worker and per unit of finished product than do its competitors. If foreign competition continues to have lower labor costs and, in addition, is able to employ more capital per worker, U.S. industry will be uncompetitive.

Perhaps it is time to evaluate the broad collection of regulations applied to the automotive industry in the context of today and a likely tomorrow, rather than the past in which these regulations were created.

REVIEW OF LAWS AND REGULATIONS

We strongly support current efforts to conduct a complete review of all laws and regulations pertaining to the automotive industry. Perhaps a nongovernmental, independent organization should be established to study conflicting regulatory demands.

Whatever steps the Government takes to assist the U.S. automotive industry, we suggest that they be positive and undertaken in a spirit of good will. The objective should be to bring all segments of the industry up to the strength of the best, not to tear down the strong.

Think of the automotive industry as a willing workman, whose left arm has been injured in an accident and is bleeding profusely. How do we help him? Do we provide aid, perhaps a transfusion? Or do we even him up by injuring his good right arm?

Conditions are changing so rapidly that uncertainty is greater than ever. We know that complete car and truck lines will be redesigned once, and perhaps two or three times, during the 1980's. Usage of some of the supplier-provided components, such as rear axles and carburetors, will be greatly reduced. Many components and subsystems will be radically altered by new materials, or replaced completely by new technologies.

The uncertainties of the more than 40,000 suppliers and equally numerous dealers are greater than the manufacturers since they face the uncertainties of the manufacturers plus the uncertainty of their relationship with the manufacturers.

When sales of domestically produced motor vehicles are poor, many suppliers and dealers are hurt even more than the vehicle manufacturers. But when sales pick up again, the suppliers and

dealers either recover or are replaced. So the overall infrastructure is not permanently depressed, despite many individual tragedies.

However, it is indeed possible that the relative importance of automotive manufacturing in the U.S. economy will be downgraded for many years, if not permanently, because of the long range damage to the vehicle manufacturers. The impact on the supplier and dealer network could be irreparable.

If the U.S. automotive industry achieves its announced product plans, it should be highly competitive in both domestic and export markets by 1985.

Whether it will be allowed to compete in foreign markets is, of course, a separate matter. However, if an industry can earn the right to compete, surely the U.S. industry is doing so now.

To the extent that the U.S. Government has any control over international trade, it would seem eminently sound business to take steps now, while import sales are strong, to insure that when U.S. cars become competitive in foreign markets, they be allowed to compete.

Perhaps an agreement should be reached to the effect that for any car imported in the United States, the U.S. auto industry should be allowed to export a car to the country of origin of the import, at no greater financial or redtape disincentive than the United States now imposes on imports.

The U.S. automotive industry should be allowed to bank these rights for use in future years. We might call this the "Golden Rule" of international trade.

It is not certain now that the industry can technically meet all of its goals. Many product objectives, particularly for the years beyond 1985, are dependent upon technical breakthroughs that have not yet been accomplished. Research is the connecting link between objectives and achievements.

The automotive industry is successfully engaged in a short-term program to optimize existing technologies. Emission and efficiency characteristics, weight, ride, handling, et cetera, are being improved simultaneously, but the limits to this developmental phase have been almost reached. Progress is slowing. Technology to date has run far ahead of a comprehensive understanding of key basic processes.

A broader and deeper research base than now exists is required to carry development successfully into the longer term, to examine alternative engine concepts, and to prepare for substantial vehicle changes.

COOPERATIVE AUTOMOTIVE RESEARCH PROGRAM

Because of the urgent need for basic automotive research, the University of Michigan—and here I can speak for the University—is enthusiastically in favor of the cooperative automotive research program, known inelegantly as CARP.

We believe CARP not only promises great results, but also is a rare opportunity to create a large scale interdisciplinary program that could substantially advance continuing cooperation between industry, labor, Government, and the academic community.

Finally, and probably most important, the United States must concentrate resources on research to offset the windfall advantages of our foreign competitors. Consider the contrast:

At a time when the U.S. automotive industry is forced to lay off engineers and every other kind of employee, and cannot hire new research experts, and is pouring every dollar it is allowed to retain or can borrow into new capital requirements, foreign competitors are taking billions of dollars out of America to spend on fresh research in both product and manufacturing technology in an attempt to maintain and extend their current advantage.

The United States must act now to provide the research support needed to meet tomorrow's problems, or the windfall luck of the imports may become permanent.

Earlier we have made specific proposals to aid the automotive industry in its hours of need, but the real key lies in cooperation. The Government's regulatory responsibilities may require adversarial relations between Government and industry, but the Government wears more than one hat, is more than just a regulator. It has also assumed the responsibility for helping to maintain productive jobs.

To accomplish this objective, Government must strengthen industry. In this role, there is no place for antagonism.

Relative to the size, economic importance, and complexity of the U.S. automotive industry, we have very little time left to set our affairs in order and confront tomorrow.

If the industry and Government cooperate, we can create our own future and restore prosperous, sunlit days. If we fail to join forces, we may all witness the irreversible contraction into faltering mediocrity of the giant U.S. automotive industry. It is time to stop squabbling over who should steer a damaged ship, and take some lessons from our foreign competitors on how to cooperate, how to succeed. It is time to work together.

Thank you.

Senator RIEGLE. Thank you.

[Complete statement follows:]

TESTIMONY OF DAVID E. COLE, DIRECTOR, OFFICE FOR THE STUDY OF AUTOMOTIVE TRANSPORTATION, OF THE UNIVERSITY OF MICHIGAN

Chairman Riegle, Chairman Stevenson, and Members of the Subcommittees, I appreciate the opportunity to be here today to discuss the problems of the automotive industry and its present and future role in the domestic and world economy. The U.S. automotive industry is still strong and competitive but it is beset by severe temporary problems that could have lasting effects. Therefore, this inquiry is very timely.

My research and teaching careers have been devoted almost totally to technical and policy aspects of automotive vehicles in particular and the automotive industry in general. About a year and a half ago, in recognition of the pervasive importance of automotive related research to the University, a new research coordinating organization, The Office for the Study of Automotive Transportation (OSAT), was created and I am its first director. I also continue to teach and conduct research as a professor in the Mechanical Engineering and Applied Mechanics department of the College of Engineering.

In my testimony today I will begin with some background information on The University of Michigan's relationship to the automotive industry. This will be followed with a discussion of probable trends in automotive technology, industry capital requirements, the status of the vehicle manufacturers and their suppliers and dealers, the impact of recent developments on labor, and the place of mass transit. I will conclude with some remarks on the marketing and competitive situation and suggest research programs and government actions that might be undertaken to strengthen the industry.

INTRODUCTION

The automotive industry is changing faster than ever before and this pace of rapid innovation is likely to continue or even accelerate in the years just ahead. The vehicle manufacturers and their suppliers are being swept along in turbulent transition. Sudden changes create major problems but the U.S. automotive industry has a record of solving what seem to be insurmountable difficulties. The purposes of this paper are to (1) outline the status of the industry, (2) estimate its future, and (3) suggest actions that will allow the industry to do again what it has done many times before—weave problems into opportunities.

THE UNIVERSITY OF MICHIGAN AND THE AUTOMOTIVE INDUSTRY

I alone cannot speak for the rich diversity of powerful human and technical resources of The University of Michigan, but as a faculty member there I draw on a long, distinguished, and growing record of cooperation and helpful interaction between the University and the industry. The University of Michigan's almost 47,000 students and 15,000 faculty and staff are located on three campuses in the heart of the largest concentration of automotive design, engineering, manufacturing, and marketing facilities in the world. For ten years the University has been televising continuing education programs directly into automotive industry laboratories. Through these programs plus regular on-campus study, The University of Michigan has contributed to the education of a large share of the industry's practicing engineers.

Transportation engineering courses have been taught at the University for 128 years and courses on automotive subjects were introduced in 1907. Objective analyses of U of M engineering faculty members have reached the modest conclusion that the University's automotive research capability and associated facilities are probably the most advanced and comprehensive of any university in the world. Essentially every aspect of the automotive system comes under close scrutiny including engines, transmissions, fuel management systems, combustion, emissions, turbo and super chargers, fuels, lubricants, suspensions, aerodynamics, acoustics, tires, traffic flow, highway safety, and the highway itself.

As environmental, safety, and energy concerns have grown, the breadth of our automotive research has expanded. It now includes public policy analysis, social and other behavioral research, urban and regional planning, economics, natural resource planning and protection, the computer sciences, biomedicine and others, as well as the traditional core of engineering research which includes not only the expected hard sciences but other major activities such as rehabilitation engineering where faculty from engineering, the medical school, and public health concentrate their skills on research to aid the disabled driver.

Among the University's 24 schools and colleges, 31 centers, 19 institutes, 9 hospital units, and 3 bureaus, few, if any, are not at least indirectly concerned with automotive research. Very directly involved are the University's Highway Safety Research Institute (HSRI), the Institute of Public Policy Studies (IPPS), the Institute for Social Research (ISR), the Literary College's Economics and Social Science Departments, the School of Business Administration, the Institute of Labor and Industrial Relations (ILIR), the Industrial Development Division (IDD) of the Institute of Science and Technology (ST), the two Offices of Energy and Transportation Research, the Center for Japanese Studies, the School of Public Health, the Law School, the College of Architecture and Urban Planning, and, of course, the Engineering College.

In view of the breadth and depth of the involvement of so many University units in automotive research, another organization, the Office for the Study of Automotive Transportation (OSAT), of which I am Director, was established to function as a point of contact for automotive research and teaching activities within the University, and to interact with outside interest groups throughout the country and the world. This objective is so important, and so germane to this hearing, that it bears restating: Two of OSAT's primary tasks are (1) to provide a focus for consideration of the automotive industry's major problems and opportunities, both technical and social, both domestic and international, and (2) to encourage and enhance interaction between motor vehicle manufacturers, their suppliers, labor, government, consumers, and the academic community.

In partial accomplishment of this broad objective, I and Mr. Lawrence T. Harbeck, my colleague in OSAT, have developed and directed, with the assistance of other University components, an annual automotive industry seminar that is a leading forum for interactive, two-way, discussions between the vehicle manufacturers, their suppliers, and representatives of labor, government, and others. Attendance at our automotive seminar has grown 7-fold in five years. Our discussion

leaders are largely top executives from the vehicle manufacturers; two thirds of the audience represent supplier management and half of these are chairman, presidents, vice-presidents, or directors of their companies.

The experience of directing these conferences for six years, together with research and other activities over even longer periods, has resulted in literally thousands of contacts between OSAT staff and representatives of the automotive industry and directly associated or interested leaders in labor and government. I emphasize these many industry, labor, and government contacts to establish that I do not have much time to spend in ivory towers.

My position in this regard is not unique. Dr. Harold Shapiro, a dinstinguished economist, the former manager of a family business, where he learned to meet a payroll, and newly appointed president of The University of Michigan, has made it emphatically clear that he expects faculty members to interact frequently and pragmatically with representatives of industry, labor, and government. The University's primary responsibilities remain those of teaching and research but there is no conflict between these missions and shirtsleeves participation in the working world.

TECHNOLOGICAL TRENDS

My office, OSAT, recently participated in the design and management of a major Delphi Survey[1] of technical, marketing, and administrative decision makers in the automotive and supplier industry. The Delphi technique is an iterative process in which carefully selected experts work independently and anonymously to arrive at a consensus view of the future; in this case, the automotive future. If the proper individuals are selected their prediction tends to be accurate because they have made or are going to make the decisions that lead to the results they are predicting. Many factors were examined in this study, including technology and marketing. The following discussion is a brief summary of part of the full report, copies of which are available from Arthur Andersen & Co., financial sponsors of the survey.

Powerplants

The automotive engines of the future will be predominantly in-line 4-cylinder and V-6 designs. The engines of the 1960's and 1970's, the in-line 6-cylinder and V-8 configurations, will only plan a minor role. Our forecast suggested tha in 1985 50 percent of the engines produced will be 4's and 25 percent V-6's; in 1990 the 4-cylinder production may be as high as 75 percent while the V-6 fraction will remain approximately the same as 1985. Diesel engine use is forecast to increase from 15 percent in 1985 to 25 percent in 1990 and turbo or supercharging will be used extensively on both gasoline and diesel engines. By 1990, electric vehicles may account for as much as 5 percent of U.S. sales. There is a reasonable chance that stratified charge spark-ignited engines will be introduced in the 1980's. Several technical and economic problems must be resolved, however, before production can begin.

More exotic engine concepts such as the gas turbine or the Stirling engine are not expected in the 1980's. Fuel injection will be more common on gasoline engines; single point injection could be used on 30 percent of 1985 engines and 50 percent of 1990 engines. Multi-point fuel injection for the gasoline engine is not expected to increase beyond 10 percent penetration in both 1985 and 1990. At least 80 percent of all gasoline engines will be matched with 3-way or dual-bed catalytic emission controls in the last half of this decade.

Drive trains

The front engine front drive concept with the engine located transversely in the vehicle will become the predominantly drive train configuration in the decade ahead. This system will be used primarily in passenger cars but will also be applied to some light trucks and vans. Our technology experts predicted that front wheel drive technology will add $125 to the manufacturing cost but will result in weight savings ranging from 150 pounds in a subcompact car to 250 pounds in a full-size car. This drive-train technology is thought to be applicable to vehicles up to 3,000 to 3,500 pounds, or essentially all of the proposed future passenger cars.

Electronics

Electronics are expected to play an increasingly prominent role in the automobile and light truck of the future. Today, about 5 percent of the cost of the vehicle is represented by electric systems. This percentage is expected to increase to 10 percent in 1985 and 15 percent in 1990. We foresee on-board computer diagnostic

[1] U.S. Automotive Industry Trends for The 1980's, a Delphi Forecast, sponsored by Arthur Andersen & Co., December 1979.

systems that will provide the operator with a much better understanding of the state of tune and maintenance requirements of the vehicle. Microprocessors will be used in practically all future vehicles.

Materials and components

Dramatic shifts are expected in automotive materials in tomorrow's cars and light trucks as they are down-sized and unweighted. In general, lightweight materials will come into far greater use in the never ending drive of the automotive designer to maintain the largest possible passenger and load volume while reducing vehicle weight to minimize fuel consumption. The average weight of the U.S. produced car is forecast to drop from 3,300 pounds in 1980 to 2,900 pounds in 1985 and finally to 2,500 pounds in 1990. The most significant material reductions will occur with steel and cast iron. Steel use will be reduced from slightly more than 2,000 pounds in 1978 to only 250 pounds in 1990. At the same time, plastic in all its various forms is projected to increase from 175 pounds to 300 pounds and aluminum from 115 to 200 pounds. Most of the aluminum increase will be in castings.

Plastic materials of many types will be used, including a substantial increase in fiber based composite materials. Only about 35 pounds of composites are used in current vehicles but this will increase to 100 pounds in 1985 and 200 pounds in 1990. The expert panelists forecast that 10 percent of exterior panels in U.S. produced cars will be constructed of fiber-reinforced plastics or other composite forms in 1985 and that this figure will double by 1990. One of the primary factors in the decision whether or not to utilize lightweight materials is the dollar value of weight savings. Our panelists projected that the value of a pound of weight saved is currently in the range of 50 cents to 90 cents a pounds, but will be $1 per pound by 1985 and approximately $1.25 per pound by 1990. We found significant concern that certain materials may come into short supply. For example, rhodium, cobalt, platinum, and chrome are all viewed as being vulnerable.

Vehicle operation and maintenance

From the 1960's to today, we have witnessed a dramatic reduction in the number of scheduled maintenance visits by the car owner. Presently, scheduled maintenance is required every 6,000 to 7,500 miles Our panelists predict that this interval will increase to 10,000 miles in 1985 and to 15,000 miles by 1990. This certainly will place a premier requirement on all automotive materials if they are to fit with this more demanding maintenance schedule. Another indiction of this trend is that only half of the vehicles in 1990 are expected to be equipped with spare tires.

The many advances predicted in the Delphi survey will require additional work on the part of the U.S. automotive industry but these improvements could not occur in the relatively short time frame considered if the industry had not made a major effort in recent years to get these programs started—even before the belated recognition by U.S. consumers that energy problems are real.

CAPITAL REQUIREMENTS

We have seen a wide range of estimates of the capital that will be required to bring the U.S. automotive industry into compliance with the CAFE standard of 27.5 mpg by 1985. One of the better substantiated figures we have heard is $25 billion per year from 1979 through 1985; an annual level (although in depreciated dollars) approximately equal to the cost of the Apollo moon landing program. This figure would include $75 billion capital requirements for U.S. motor vehicle manufacturers and $50 billion for their U.S. suppliers over the five year period. Any present day estimate can be quickly reduced, of course, if poor vehicle sales or other circumstances make such enormous investments impossible. Ford Motor Company announced in early May the cancellation of $2.5 billion of its capital expansion plans. Any forced decline in capital spending delays the restoration of full competitiveness for U.S. automotive manufacturers.

Perhaps the only certainty about the industry's capital needs is that they are large beyond comprehension and will create immense financial strains. Any reasonable action that can be taken to relieve the pressure will help accelerate progress. Perhaps the best way to help would be immediate changes in depreciation regulations to allow an equally immediate improvement in internally generated cash flow. Related steps could include provisions to permit a more rapid write-off and/or increased investment tax credit for special tools needed for government mandated items and the fast refunding of taxes to companies not in a profit position. New production facilities obsoleted by recent market trends could be considered for more rapid write-off as well. Longer term, the elimination of double taxation on dividends might make it easier to raise fresh capital.

There are other actions that can be considered but in our judgement these offer the most immediate and continuing promise. Inseparable from the automotive industry's capital problems is the overall capital investment situation in the U.S. Recent estimates indicate that capital investment as a percent of GNP is 20 percent in Japan, 15 percent in Germany, but only 10 percent here. These data would indicate that investing in Japan and Germany is more attractive. We would benefit from government policies that offer more encouragement to savings and investment. Surely a reduction in inflation would be a result.

In understanding the ebb and flow of small vs. large car sales in the U.S. market, it is important to keep in mind the long leadtime between management decisions and production for the market. Years are required to make a major modification, to produce a new model, or—and this is very important—to produce much larger quantities of an existing model. This last point is little recognized and worth repeating. It takes years to build or modify major production facilities to produce large additional volumes of cars or trucks—even if the vehicle to be produced is already in existence.

Long leadtimes are caused by several limiting factors including (1) financing, (2) availability of trained engineers and other personnel to design and test vehicles and set up new manufacturing facilities, and (3) the limited ability of the machine tool industry to supply production equipment. Capital and financing problems are particularly severe today because of the premature obsolescence of huge amounts of existing capital equipment that was designed to produce, in large quantities, vehicles that are now selling in low volume.

Major losses of capital investment hurt the U.S. automotive industry more than they would automotive industries in other countries because the U.S. industry is particularly dependent on using capital investment to offset high labor costs. The only way the U.S. can be productively competitive is by investing more per worker and per unit of finished product than do its competitors. If foreign competition continues to have lower labor costs and, in addition, is able to employ more capital per worker, U.S. industry will be uncompetitive.

MOTOR VEHICLE MANUFACTURERS

We can be fairly certain that the United States will still have one manufacturer producing a full line of motor vehicles in 1985. We cannot be at all sure that we will have two, and three seems highly unlikely. I see no advantages to the nation, no technical product advantages, and no advantages to G.M. employees and shareholders, if Ford and Chrysler are unable to compete across the board. Despite its troubles, however, the U.S. automotive industry today is still the most competitive and technically competent in the world. It has unmatched engineering and manufacturing strength. But it is weakening and needs help—not a handout, but rational assistance.

The industry has made mistakes, of course. But in judging the U.S. automotive industry, it is only fair to keep the following sequence of events before us:

1. For most of the post WWII period the real cost of energy, adjusted for inflation, was dropping.
2. In the U.S. and Canada, the two countries most dependent on automotive transportation, the retail price of gasoline reflected this decline.
3. As a consequence of the declining real cost of gasoline, and resultant consumer perceptions and demand, North American passenger cars became large and heavy. Customers wanted comfort and safety and, with low priced and available fuel and new materials, the most economical way to meet their demands was by making the cars heavier.
4. In Europe and Japan, where cars were not so much of a necessity, and driving habits, patterns, and needs were different, gasoline prices were kept very high by adding taxes. Also, punitive taxes were placed on weight and horsepower.
5. Because of the high gasoline costs, narrower roads, and shorter distances travelled, cars in Europe and Japan were made small and economical to meet a different customer demand.
6. Imported cars were not a major factor in the U.S. until the 1970's. In 1959 the import share of market touched 10 percent but fell back to 5 pecent in 1963 and never got over 12 percent—into the teens—until 1970.
7. Between 1970 and 1972, while import sales were edging up from 1.2 million units to 1.5 million, sales of domestic cars increased from 7.2 million to almost 10.0 million. The increase alone in domestic car sales was almost twice the level of total import sales.
8. Sales of both imports and domestic cars fell sharply in 1974 but domestic car sales were up to 9.0 million again in 1978—only two years ago.

9. In late 1975 and early 1976, when many of the decisions concerning 1980 model cars were being made, import sales had just suffered a tremendous drop in penetration—from 21.70 percent of market in March, 1975, to 11.66 percent in November of the same year—a decline of almost 50 percent in only eight months. During this same period, government mandated gasoline prices remained essentially unchanged at about half of today's level.

10. Little over one year ago, just before the terrorist government of Iran made hostages of American citizens, large domestic passenger cars were selling very well and import sales remained depressed at penetration levels over one-third below year earlier levels. Dealer inventories of imports were near record highs in terms of days' supply.

Now that the American consumer has seen the light (and also seen essentially decontrolled gasoline prices for the first time) small sized U.S. cars and imports are suddenly popular again. Import manufacturers can meet added demand for small cars by working overtime in large capacity small-car facilities necessitated by decades of action by their governments to keep fuel and other automotive taxes high. American vehicle manufacturers, led by many years of big-car demand based on artifically low fuel prices, must play catch-up ball—and it will take time and money to build the facilities to do this.

Earlier we suggested ways to speed up the flow of capital to the manufacturers. Increased capital flow will be a long term need if automotive change continues on a fast tract—and we see no signs of a slow-down.

For the short term, it would be desirable to relieve some of the pressure of the windfall luck of the importers who have been forced to specialize in small cars and, through no foresight of their own, were ready at hand to take advantage of the almost overnight switch to real-world gasoline prices in the U.S. market. On page 18 of this hearing, under "Markets and Competition", we propose a specific plan.

Emissions and safety standards are expensive and are not widely viewed by the consumer as having significant value. In particular, a trade-off relationship exists between emissions and fuel economy. Tight emission standards penalize fuel economy and add considerably to cost. Perhaps it is time to evaluate the broad collection of regulations applied to the auto industry in the context of today and a likely tomorrow rather than the past in which these regulations were created. For example, would 90 percent control of exhaust hydrocarbons or carbon monoxide, rather than the 95 percent control, yield cost and economy advantages greater than the small decrease in emission performance?

It might be an opportune time to conduct a complete review of all laws and regulations pertaining to the automotive industry. Perhaps an independent organization should be established to study conflicting regulatory demands, e.g., fuel economy versus exhaust emissions.

Whatever steps the government takes to assist the U.S. automotive industry, we suggest that they be positive and undertaken in a spirit of goodwill. The objective should be to bring all segments of the industry up to the strength of the best; not to tear down the strong. Think of the automotive industry as a willing workman whose left arm has been injured in an accident and is bleeding profusely. How do we help him? Do we provide aid, perhaps a transfusion? Or do we even him up by injuring his good right arm?

SUPPLIERS AND DEALERS

The May 7 letter from Senators Stevenson and Riegle asks "is there evidence that the current plight of the domestic auto industry is causing irreparable and irreversible damage to the infrastructure of suppliers and dealers of a magnitude that will permanently downgrade the relative importance of automobile manufacturing in our national economy?"

The infrastructure of suppliers and dealers is a follower, not a leader. When sales of domestically produced motor vehicles are poor, many suppliers and dealers are hurt even more than the vehicle manufacturers; but when sales pick up again the suppliers and dealers either recover or are replaced—so the overall infrastructure is not permanently depressed, despite many individual tragedies.

However, it is indeed possible that the relative importance of automobile manufacturing in the U.S. economy will be downgraded for many years, if not permanently, because of long-term damage to the vehicle manufacturers. In fact, the evidence to date would seem to indicate that almost irreparable harm may be only months away.

In the face of their own difficulties, the vehicle manufacturers are, and have been for some time, making extraordinary efforts to assist their suppliers in these difficult times. The vehicle manufacturers openly discuss many of their future plans for new vehicles, new engines and drivetrains, lightweight materials, etc. This openness, compared to past secrecy, is not entirely altruistic, of course. The vehicle

manufacturers are dependent on their suppliers' ability to raise capital to match new component requirements and want to be sure that the suppliers have enough information to plan ahead and be ready to meet changes when they occur. Unfortunately, conditions and affected programs have changed so rapidly for the industry that uncertainty is greater than ever, despite careful efforts to plan ahead and share information.

One of the major activities of my office is to assist the vehicle manufacturers and their suppliers to maintain and increase this important two-way flow of information. Earlier we discussed seminars and other techniques we use to accomplish this objective. Our efforts have also been in the direction of assisting suppliers in their efforts to live with this uncertainty. We know that complete car and truck lines will be redesigned once, and perhaps two or three times, during the 1980's. Usage of some supplier provided components, such as rear axles and carburetors, will be greatly reduced. Many components and subsystems will be radically altered by new materials, or replaced completely by new technologies.

Radical upheavel in long-standing product lines of traditional vehicle manufacturers and their parts and materials suppliers will require increased emphasis on strategic and product planning. Coordinated efforts are essential between vehicle manufacturers and suppliers to meet tight redesign schedules and avoid duplication and waste. Vehicle manufacturers' plans and objectives should continue to be communicated to suppliers and a two-way flow of strategic planning information established.

My office, OSAT, is coordinating U of M efforts to expand this exchange of vital information. We are, for example, helping in the formation of a Motor Vehicle Suppliers Association (MVSA). The scope of the task can be understood when it is realized that the industry is estimated to have more than 40,000 suppliers. Government can assist materially in impoving the ability of suppliers to plan successfully and will increase their probability of business success and survival if legislators and regulators refrain from making rapid policy changes.

LABOR

The "automotive industry" is a convenient abstraction that can stand for capital and facilities and vehicles and parts and service and a host of other components but more importantly, it represents people; millions of workers. Suprisingly, the exact number is unknown. The interrelationships of motor vehicles to other segments of the economy are so complex that it is not easy to track them all down.

The Motor Vehicle Manufacturers Association (MVMA) has a statistical department that estimates that better than one of every five jobs in this country is dependent on the production of motor vehicles or a related field. When total U.S. employment hits 100 million, which it should do soon, the 1 in 5 estimate indicates 20 million jobs associated with the automotive industry. Of these, less than one million are directly occupied in producing vehicles and parts, although this figure is low in the sense that it leaves out many workers who produce parts for the supplier companies.

A few numbers we do know are that on Monday, June 9, there were 235,000 hourly workers on indefinite layoffs from the four U.S. vehicle manufacturers; another 52,000 laid off temporarily; perhaps 45,000 salaried workers out of a job or soon to be, and—no one knows exactly—perhaps half again these numbers affected in the supplier industries.

These are the really gut numbers with which to measure the impact of the OPEC oil cartel, artifically priced U.S. gasoline, and the resulting import sales.

PUBLIC MASS TRANSIT

Question has been raised as to whether government should plan for assistance to public mass transit or should exphasis be on assistance to the producers of private passenger automobiles (private mass transit).

Considerable effort has been expended in studying the possibilities of substituting mass transit for personal cars. A good analysis to start with is "Energy, The Economy, and Mass Transit", by the Office of Technology Assessment, U.S. Congress, December 1975. The study is comprehensive and not easily summarized in a report as short as this. Furthermore, one of the study's conclusions that is most important to this hearing is not covered in its own summary. We are referring to the finding that, essentially, the U.S. has no choice but to continue use of passenger cars.

The OTA study estimated that public transit for only 5 percent to 8 percent of total trips in all U.S. urban areas and only 12 percent of the home-to-work trips in urbanized areas of 250,000 or more. The study estimated that heroic support for

mass transit combined with heavily punitive measures against private cars might double mass transit use in 5 years. The longer term solution was seen to require government actions that "would shape and guide (land) development into more positive relationships with transit and energy." What this means, in essence, is that until you control where people live, and also force a change in present living patterns, public transit cannot account for a major part of personal travel.

We interpret the OTA study and other related analyses as follows: American life has become increasingly dependent on and molded by convenient, affordable motor vehicles. Personally owned transportation has made the United States the most mobile society in the world and U.S. citizens are extremely sensitive to attacks on this freedom and the many other freedoms associated with it. Tractors and mechanized equipment have revolutionized farming. Motor vehicles have dramatically affected the design of homes, cities, and rural areas. And they have become a pervasive factor of daily life for nearly every person, group, business, and government in the nation.

Motor vehicles have also become a fundamental factor in the American economy. Industries that manufacture, sell, maintain, and depend on them account for a large share of the U.S. gross national product. If, for example, Americans stopped buying U.S. made automobiles, the national economic structure would collapse.

Any deliberate attempt to change the status of private cars and trucks in the economy and in the culture should be undertaken with considerable caution; any major unplanned negative impact on the entire automotive industry, such as the current sales and capital crisis, should spark positive, helpful government assistance.

In short, we think the better choice is to concentrate on helping the producers of private passenger cars. We do not believe that the regimentation necessary to make public mass transit "work" is in accord with national principle.

MARKETS AND COMPETITION

It is difficult to comprehend the size of the car and truck market that is support by U.S. consumers. No other market in the world approaches it for volume of sales, homogeneity, ease of entry, and attractiveness to competition. Figures like 12 million units per year are discussed but hard to grasp. We have broken sales down to an hourly rate to give us a number we can get our arms around.

On the average, U.S. consumers buy a combined total of more than 1,000 new passenger cars and trucks every hour of the day and night, seven days a week, all year long—even in an off year like 1980. This sales pace has held since 1963. In record year 1978 the rate was over 1,700 per hour. Our Delphi Survey forecasts that by 1990 the average could be 2,000 new car and truck sales per hour; enough vehicles to fill a 10 acre parking lot. (Fortunately, older models will be scrapped to make room.)

The maketing panelists in this survey forecasted a 2 percent annual sales growth for the U.S. automotive industry through 1990. The total U.S. market is expected to be in the range of 11–12 million cars by 1985 and 12.5–13 million units in 1990. The light truck market is expected to exerience a one-third increase during the 1980's growing to between 3.5 and 3.8 million units in 1985 and to 4 million units by 1990. Marketing panelists from U.S. supplier companies forecast an annual rate of increase of 3 percent for OEM products and 5 percent for replacement parts. They foresee a substantial increase in world-wide demand for parts.

No dramatic shift is forecast in the proportion of components manufacured in-house by the U.S. manufacturers. G.M. is expected to continue making 50 percent of its own parts, Ford 40 percent, Chrysler about 30 percent, AMC 20 percent.

A major change in the distribution of car sizes is anticipated. Both the intermediate and full-size vehicle penetration should be reduced significantly. For example, in 1978 the full-size market share was approximately 25 percent. This could be reduced to the area of 16 percent in 1985 and to 10–12 percent in 1990. In contrast, the compact and subcompact shares are expected to increase significantly. The subcompact is expected to increase its penetration from 27 percent in 1978 to 30 percent in 1985 and up to 35 percent by 1990. The general, over-all, marketing trend can be summarized as a modest sales increase of more durable, efficient, and smaller vehicles through the coming decade.

If the U.S. automotive industry achieves its announced product plans, it should be highly competitive in both domestic and exports markets in 1985. Whether it will be allowed to compete in foreign markets is, of course, a separate matter and beyond the ability of our surveys to forecast. However, if an industry can earn the "right" to compete, surely the U.S. automotive industry is doing so now as imports swarm in to feast on its ill luck.

To the extent that the U.S. government has any control over international trade, it would seem eminently sound business to take steps now, while import sales are strong, to ensure that when U.S. cars become competitive in foreign markets, they be allowed to compete. Perhaps an agreement should be reached to the effect that for any car imported into the U.S. (past, present, and future) the U.S. auto industry should be allowed to export a car to the country of origin of the import, at no greater financial or red-tape disincentive than the U.S. now imposes on imports. The U.S. automotive industry should be allowed to "bank" these rights for use in future years. We might call it the "Golden Rule" of international trade.

RESEARCH NEEDS

We started a paragraph in the previous section with the phrase: "If the U.S. automotive industry achieves its announced product plans,—" all will be well. But it is not certain that the industry can, technically, meet all of its goals. Many product objectives, particularly for the years beyond 1985, are dependent on technical breakthroughs that have not yet been accomplished. Research is the connecting link between objectives and achievements. To provide a better understanding of the broad scope of automotive research needs, I cannot do better than paraphrase part of the introduction to a report [2] submitted to DOT by a panel of which I was chairman.

Existing automotive technology is more advanced than the understanding of how automotive systems work. This may seem unlikely to the non-technical person but is the rule rather than the exception. Many engineering advances result in part from trial and error. An idea for a new way of doing things is tried and if it works it is used. But this is not necessarily the same as understanding completely why it works.

It is important to be aware of this "cut and try" aspect of engineering but it should not be overemphasized. Engineers and other scientists have created an enormous quantity of well established theoretical knowledge about engines and other technologies. This body of theory forms the basis for training the engineer and scientist and gives them a practical guide for developing ideas that are tried out empirically. They do not "shoot in the dark".

But the more we succeed the more we realize how much we do not know. Scientists and engineers are like explorers of a new world. Every mountain they climb discloses a new horizon and a dim and distant view of entire ranges of unconquered peaks that were not even visible from the previous advance.

Engineers are no more precise in their use of the English language than other scientists but there is rough general agreement that "research" and "development" are separate activities. Through research we find out, in detail, just exactly what is going on and form testable theories as to why these things are happening. If further tests validate a theory it may be applicable in practice. Without waiting for proof, however, it is common to try out a new idea before it is completely established in theory. If it works, it can be used before the "what" and "why" are understood completely. This process is called development.

In the early stages of improving a technology, development can take shortcuts that usually save time because there is an abundance of ideas that are reasonable even if unproved. As technology improves, the theoretical limits of perfection as defined by the laws of nature are approached but never exceeded. Development increases in cost and decreases in success as trial and error produce a growing proportion of errors. Eventually, when research has been used up, when everything reasonable has been tried, the development batting average drops alarmingly. Basic research is needed then to increase understanding and provide novel viewpoints and fresh insights.

If we had another 100 years to develop automotive systems to meet today's (and tomorrow's) efficiency and emission objectives we could probably do it as long as these objectives do not require violation of a fundamental law. But the clock is running and we must compress a century of development into a decade of research. This will only be possible if support is comprehensive and continuing.

The automotive industry is successfully engaged in a short term program to optimize existing technologies. Emission and efficiency characteristics, weight, ride, handling, etc. are being improved simultaneously. But the limits to this developmental phase have almost been reached. Progress is slowing asymptotically toward zero. Technology to date has run far ahead of a comprehensive understanding of key basic processes. A broader and deeper research base than now exists is required to carry development successfully into the longer term, to examine alternative engine

[2] Report to Transportation System Center, U.S. Department of Transportation, October 1979.

concepts, and to prepare for substantial vehicle changes. The opportunity and challenge for research is to close the knowledge gaps which now exist and thereby guide the optimization process closer to the fundamental limits.

Because of the urgent need for basic automotive research, the University of Michigan—and here I can speak for the University—is enthusiastically in favor of the Cooperative Automotive Research Program, known inelegantly as CARP. We believe CARP not only promises great results but offers a rare opportunity to create a large-scale interdisciplinary program that could substantially advance continuing cooperation between industry, labor, government, and the academic community.

At the University of Michigan we have been actively preparing to take part in the CARP program since it was first announced over a year ago. The U of M has initiated a University-wide effort that has identified over 100 faculty members who are interested in CARP. This summer, my office will coordinate the activities of twelve research team leaders who will be developing firm research proposals. I should add that we are embarking on this ambitious program even before the government and industry have completely finalized their specific CARP research requests. We at the U of M, including particularly President Shapiro who has been a CARP enthusiast from the beginning, take the program very seriously.

Obviously, there are many advantages to a university in gaining added research. Not the least of these is that research enables a university to do its job better.

One of the most important aspects of research is its educational impact. The educational value of research cannot be over emphasized. The disciplines included in automotive research form a large part of the technical background which any engineer or social scientist must have. Thus a major indirect benefit of the CARP program would be a substantial increase in the output of young engineers and scientists from the nation's universities with a background and training directly relevant to automotive technology. Without such a stream of professional, both interested in and knowledgeable about this technology, the engineering developments required to maintain the viability of our automotive transportation system in the long term future will be in jeopardy.

A related objective of this effort should be the creation of incentives which will focus the current nonautomotive research community on automotive problems. At the present time the cadre of automotive experts is small relative to the challenge and additional researchers are needed to address the magnitude of the tasks ahead.

The time is ripe to expand the country's automotive research skills. Engineering colleges are enjoying high levels of enrollment. The quality of U of M engineering students is the highest in many, many years. Students are dedicated, purpose oriented, problem-solving go-getters. It will be tragic if the downturn in domestic automotive sales should truncate realization of the potential of these splendid young people. CARP is needed, and expanded programs like it, to ensure that the nation does not waste this human opportunity.

Finally, and probably most importantly, the U.S. must concentrate resources on research to offset the windfall advantages of our foreign competitors. Consider the contrast: at a time when the U.S. automotive industry is forced to lay-off engineers and every other kind of employee and cannot hire new research experts, and is pouring every dollar it is allowed to retain or can borrow into new capital requirements, foreign competitors are taking billions of dollars out of America to spend on fresh research in an attempt to maintain and extend their current advantage.

This scenario would be a joke if it were not true. But it is a fact and not very funny at all. The U.S. must act now to provide the research support needed to meet tomorrow's problems or the windfall luck of the imports may become permanent.

COOPERATION

The above title to the final section of this report sums it all up. Earlier we have made specific proposals to aid the automotive industry in its hour of need but the real key lies in cooperation. The government's regulatory responsibilities may require adversarial relations between government and industry, but the government wears than one hat, is more than just a regulator. It has also assumed a responsibility for helping to maintain productive jobs. To accomplish this objective, government must strengthen industry. In this role there is no place for antagonism.

Relative to the size, economic importance, and complexity of the U.S. automotive industry, we have very little time left to set our affairs in order and confront tomorrow. If industry and government cooperate we can create our own future and restore prosperous, sunlit days. If we fail to join forces we may all witness the irreversible contraction into faltering mediocrity of the giant U.S. automotive industry, the greatest engine for economic well being and personal freedom that has ever existed. It is time to stop squabbling over who should steer a damaged ship and take

some lessons form our foreign competitors on how to cooperate—how to succeed. It is time to work together.

Senator RIEGLE. We both have some questions we want to raise with you, but let us next call on Ms. Keller.

STATEMENT OF MARYANN N. KELLER, FIRST VICE PRESIDENT, PAINE, WEBBER, MITCHELL & HUTCHINS, INC., NEW YORK

Ms. KELLER. Thank you.

Since Dr. Cole has covered many of the same subjects that I have in my prepared testimony, I——

Senator RIEGLE. Would you pull that mike right down in front of you? It doesn't work very well, but I want to make sure everybody in the room can hear you.

Ms. KELLER. Thank you.

I'll try to be a little more specific in my comments.

In the letter which Senator Stevenson and Senator Riegle sent to me, I was asked to address the question of the survival of the domestic industry, the competitive prospects of our industry vis-a-vis the Japanese, capital formation and sufficiency, and what specifically might be done to help get the industry out of its slump.

Before I address these, let me say that I share Senator Stevenson's concern about the reliability of any forecast on the matter of future Japanese penetration.

I think one of the reasons for that is the inconsistency of this Nation's energy policy. I think this is one of the things that has gotten the industry into trouble. We are very quick to blame management and say, "Well, you should have known, you should have had small cars."

The fact of the matter is the consumer bought every big car that automakers could build through December 1978. There can be no more graphic evidence of the consumer lack of awareness of energy conservation than the sale of nearly 4 million lightweight trucks in 1978, with at least 70 percent of them meant for personal use.

So if you're going to have fuel economy standards, complement them with an energy policy that's going to indicate to the consumer that energy prices are going up. It will shape the model mix a lot more effectively than fuel economy standards.

Senator RIEGLE. Excuse me. Can I get you to pull that mike about another inch toward you?

There are people in the back of the room who want to hear you.

Ms. KELLER. As to the question of the survival of the auto industry, I don't really think that that really is the question. The most Draconian scenario, which would be the total elimination of the industry, is impossible.

Auto manufacture represents an enormous component in our GNP. If we were forced to import all of our vehicles, the balance of payments deficit would be so huge that our dollar would be worthless and the price of imports would be so great that we couldn't afford them. Survival is not really the question.

SHIFT IN BALANCE OF COMPETITION

What we really should deal with is the balance between domestic cars and imports, and the competitive balance within the domestic industry itself.

For the last year or so, the Japanese have been able to capitalize on a very abrupt shift into small cars. U.S. companies did not have the capacity or the technically sophisticated car to match those of European and Japanese suppliers. We also lacked product variety.

It is important to recognize that even among Japanese products, there are products that aren't selling either. Although Japanese cars have a reputation for good fuel economy, the consumer is making a distinction between their high- and low-mileage cars. Popular cars offer 25 miles per gallon. The consumer is not buying anything with lesser fuel economy, whether it happens to be branded Toyota or Ford. As more domestic small cars are available the Japanese share should contract.

Within the U.S. auto industry, the balance of competition is going to shift. American Motors is going to become strictly an assembler of automobiles designed by Renault and its share is difficult to predict though it will probably remain at 2 percent or so of the domestic car market.

Chrysler's viability over the long term, in my opinion, is still not assured, even with the Government guaranteed loans. This company may become our version of British Leyland. As Chrysler retreats from some segments of the car and truck market its penetration levels will probably shrink modestly.

Neither Ford nor General Motors can look to Government or foreign benefactors at this point, and are forced to play by the rules of private enterprise.

General Motors can outspend Ford by a considerable amount and is in a position of relative strength. General Motors will increase its share in the United States and stands to dominate not only domestically but potentially in Europe and Latin America by the mid-1980's. Ford stands to lose share because it cannot afford to remain a full-line competitor.

Between 1980 and 1984, General Motors will spend worldwide something like $40 billion, and only about $1 billion of that each year will be spent abroad. Ford's total expenditures will amount to $20 billion.

I have provided more detailed forecasts of their capital expenditure budgets and financing requirements in my prepared testimony.

Capital formation is a key problem for automakers. The outside capital requirements are staggering for this industry. Ford and GM have typically been self-financing, and by anyone's measure of creditworthiness both of them are very sound.

General Motors began this year with about a 4½ percent debt to total capital ratio. For comparative purposes, a single A rated company in this country would have a 30-percent debt to total capital ratio. Ford was of about 11 percent at year end.

So, by conventional measures, these are financially sound companies with good borrowing capacity. However, the industry suddenly requires extraordinary amounts of capital. GM, Ford, and their credit subsidiaries could have annual borrowing needs equal

that of the telephone system. From Wall Street's perspective, that is an extraordinary amount of money that will have to be provided to companies that, heretofore, were self-financing. Borrowing is particularly difficult given the current situation in the industry.

Senator RIEGLE. Could I just ask you one question at that point, so we don't lose it? And I don't want to interrupt the flow of your presentation, but when one thinks about the capital requirement for the basic companies, and then the second capital requirement for the supplier network, which is also quite enormous, and then you lay that beside other major segment capital requirements say like the telephone industry, which you mentioned, is it your view or the view on Wall Street that there will be sufficient capital in the aggregate to meet these needs?

Ms. KELLER. I don't believe it is. The capital formation process in this country is not particularly good, and I certainly do agree with Dr. Cole's statement that taxation policies discourage savings and investment.

Capital adequacy, both from external and internal sources, is one of the critical problems that has to be addressed for this industry. There are a lot of ways of boosting capital formation. For example, changes in depreciation rates would increase cash flow, and improve the ability of a company to generate funds internally.

This gets us into the area of what might be done by Government to aid the industry. I think there is a temptation now to solve the industry's problems, which are obviously huge, with short-term solutions.

In my opinion, there is only one thing that can be done to aid the industry over the short term. The industry's problems stem not only from a model mix that doesn't conform to the consumer's wants but also to the fact that the country is in a recession.

It's not going to do too much good to implement a tax credit for the purchase of fuel-efficient cars, when every fuel-efficient car that General Motors and Ford can build is sold.

TAX CREDIT OR TAX REBATE

Sales would increase, however, if consumers received a tax credit or tax rebate for the purchase of any domestic car or truck. Such action should help to reduce dealer inventories and permit higher production levels by the fourth quarter.

It's important to realize that, despite the fact we refer to some models as large by today's standards, they are considerably more fuel efficient than their predecessors of 5 years ago.

That would help to take care of an immediate problem. The program could be terminated at the beginning of the 1981 model year when availability of small cars would improve.

Beyond that, I think a considerable amount of planning has to be done to make this industry much more competitive on a worldwide basis. That calls for a more reasoned role by the U.S. Government in the development of long-term solutions.

I think it is important to analyze how the U.S. Government interacts with the industry compared with the roles played by the Japanese Government or the European governments with their respective industries. The Japanese Government role is promotion-

al whereas the European governments are entrepreneurial. The U.S. Government's role is adversarial and legislative.

A shift in the attitude might increase the investment community's willingness to lend to this industry. One of the things that discourages investors, unfortunately, is the stigma of being a regulated industry, which clearly this is.

It is fairly obvious the Japanese have helped their industry and promoted growth, provided capital and guidance.

European governments roles perhaps are more varied. The Europeans participate through total ownership of companies, in the case of Renault or British Leyland, or partial ownership in the case of Volkswagen.

European try to compensate for poor economies of scale of their auto industries by permitting the formation of consortiums, sharing of technology, and joint ownership of component facilities.

They also fund research and development, much more aggressively than we do. For example; between 1978 and 1979, Volkswagen received from the German Government 140 million deutsch marks for the specific purpose of research and development for new technologies. Between 1979 and 1982, they will receive 135 million deutsch marks for fuel efficiency. Between 1979 and 1982, they will receive 110 million deutsch marks for safety and emissions control.

I think that additional government effort in the area of research and development would clearly be warranted.

European governments are also very fond of using monetary grants and special tax concessions to spur capital investment in the auto industry.

General Motors and Ford subsidiaries in Europe have been beneficiaries of these grants in Britain, Spain,and Austria.

It's been estimated, for example, that this year grants by European governments will total $1 billion, and future grants through 1985 will amount to $1 billion annually.

There are measures which might be considered which would certainly help balance within the competitive environment among domestic automakers, General Motors has the greatest resources and it is obvious that Ford is the company that's under the greatest amount of pressure.

Ford's losses this year will be enormous and perhaps consideration of a tax loss carryback provision stretching back 10 years might be warranted to assist companies reporting such staggering losses.

In addition, investment tax credits do very little good for a company that is unprofitable. There might be some consideration given to an actual refund rather than a credit for these measures. A full review of writeoff policies for equipment depreciation and tool amortization is also warranted.

Thank you.

Senator RIEGLE. Thank you very much.

[Prepared statement follows:]

STATEMENT OF MARYANN N. KELLER, FIRST VICE PRESIDENT, PAINE WEBBER MITCHELL HUTCHINS

The U.S. automotive industry is in a state of crisis stemming from the near doubling of the price of gasoline over the last 18 months. This created a shift to

small, fuel efficient cars which Detroit could not supply. The blame for this predicament should be shared by government and industry, alike. It's easy to criticize management today yet we forget that as recently as October 1978, domestic manufacturers were sold out of full-sized cars equipped with the largest available V-8 engines. Small foreign cars were stocked up at ports in record numbers despite discounting and heavy advertising. The import share was only 14.5 percent at that time. Japanese automakers, at that time, contemplated new strategies for the U.S. market which suggested moving out of high volume, low priced cars into larger and specialty products. As a result of consumer preference, domestic manufacturers, were reluctant to increase more capital on subcompact models and instead directed the bulk of their funds toward reducing the fuel consumption of larger models.

The government's avowed goal was energy conservation, its action with respect was energy decontrol suggest that it was politically unacceptable to allow gasoline prices to rise. Washington placed that burden of conservation squarely on the auto companies. Providing incentives to the consumer through a gas guzzler tax or rising fuel prices which would have altered to mix gradually into small cars and caused management's to focus investment in these segment. Since gasoline prices fell in real terms between 1975 and 1978, consumers favored larger cars. Fuel economy standards necessitated that investment be made to improve the miles per gallon rating of these vehicles. There is no more graphic piece of evidence of consumer lack of regard for energy conservation and pollution control standards than his escape from the catalytic convector equipped auto into the lead gasoline light weight truck over 6000 lbs. GVW starting in 1975. Demand for these vehicles baffled automakers who were unable to supply vehicles in spite of repeated price hikes. This situation ended abruptly at the end of 1978. In 1979, light weight truck demand fell 17.2 percent compared with a 12 percent decrease in domestic car sales.

There is a normal tendency to want to correct the problems of high unemployment and lack of acceptable models quickly. However, lead times in the auto industry are long, capital requirements high and technological risks great. Short-term solutions may cause more problems as I will indicate later. We need not question the viability of a domestic auto industry in the future. A more relevant question would be an assessment of the competitive balance within the industry in 5 years among the domestic manufacturers and between the domestic companies and foreign automakers. Domestic automakers recovered from previous recessions more or less simultaneously. Market share gains and losses were small from one year to the next. Recovery from this recession, however, could be vastly different with some companies enduring a permanent lose of share for certain companies.

American Motors will become an assembler of automobiles, designed by Renault, the French government owned company, which is seeking to broaden its base in the U.S. Its future is linked to the acceptance of Renault products, Renault's desire to make additional capital commitments, and to that company's ability to sell Jeeps in export markets.

Chrysler's viability is not assured by government guaranteed loans. In my opinion, the company's unfavorable cost structure, new products from Ford and more so GM, the probable abandonment of the light weight truck and the big car markets will weaken Chrysler's share further and prevent a turnaround. Chrysler may become our version of British Leyland which survives only by repeated infusions of cash. Now that government and labor are full partners in the operation of the company, it will probably be more difficult to close plants and streamline operations which would cut jobs—since aid was granted to present jobs. Chrysler might be saved through a formal link with a foreign company, though I am hard pressed to identify any with both the resources and desire to take on Chrysler.

General Motors and Ford have no government or foreign benefactors and must play by the normal rules of free enterprise. GM can and will outspend Ford and starts from a position of relative strength and since money begets power the company stands to dominate the worldwide auto industry by the mid-80's. Between 1980 and 1984, GM will spend $40 billion compared to Ford's $20 billion. General Motors, by 1985, will be the only auto company in the world capable of building a full range of cars and trucks. In addition huge investments of $1 billion or more a year will be made overseas to expand capacity and integrate those production facilities with North America. By 1985 General Motors could have the most modern facilities and improve its unit labor costs. Not only will GM have a complete line of vehicles but will have superior engine technology as well. GM will dominate the market segments which we refer to as large and intermediate size cars though these products will be substantially smaller than they are today. GM will thereby be able to shield itself from direct competition with the Japanese. In the exercise of its strength, GM will expand its market share to 70 percent of the domestic car market from the present 64 percent and potentially improve its profitability.

Ford cannot afford to match GM's expenditures and will, over time, be forced to cutback on the number of models offered and withdraw from the highly profitable, but low volume larger car segments. This will leave Ford vulnerable to head-to-head competition with the Japanese at the low end of the market. Thus, while the auto industry survives in 1985 its character could change from that of an oligopoly to more of a monopoly—particularly in certain market segments.

There are two questions which should be considered with respect to the Japanese. First, can market share be recaptured from them and second, can it be done profitably? The Japanese have been depicted as villains preying on domestic automakers. In fact U.S. small cars are not now competitive but will become increasingly so with the introduction of K-cars, Escort and J-cars. We would expect their market share to pull back to 20 percent or so once these cars are in production by the second half of 1981. Currently the foreign share is about 27 percent with the Japanese accounting for 70 percent of that.

The equally important question to U.S. companies is the limitation they impose on the profitability of domestic small cars because of their more than a $500 cost advantage per unit. Higher tariffs or quotas will raise the general price level of small cars and allow U.S. companies to increase profits on them. They will not, in my opinion, boost unit sales of domestic cars since the small car market has always been where the greatest price sensitively is observed. The Japanese have developed good dealers and service and have gained a reputation for quality. This may permit them to hold onto a large share than was possible several years ago but probably not as high as it is presently.

I regard capital sufficiency as a more serious fundamental problem facing the industry than Japanese competition. Not only must we develop more appealing models, but also permanently improve our cost structure and quality through plant modernization and automation.

Capital formation to provide for these projects is a critical problem for the automakers which has been aggravated by losses this year and rising capital spending requirements. Chrysler and American Motors will rely on their respective partners for needed financial support. General Motors and Ford are confronted with the problem of raising record amounts of capital from outside lenders, antagonizing shareholders with dividend cuts and altering the perception of the companies which heretofore had been essentially self-financing.

Both GM and Ford began the year with modest debt to total capital levels of 4.4 percent and 10.9 percent respectively. A single A credit in this country might be 30 percent debt to total capital. Their impressive balance sheet strength at the beginning of the year pales next to the straggering amounts of capital that will have to be obtained by the industry each year. For example, I estimate that General Motors will generate a total of $39 billion from income depreciation and amortization through 1984. Its total cash requirements through this period will amount to $47 to $50 billion for modest dividends, capital spending and working capital needs attributable to rising sales. GM will have to borrow up to $2 billion a year through 1982 to fund these requirements.

Ford's case is similar. Cash generated could amount to $15 billion with capital needs estimated at $22 billion. Ford has already placed $650 million in debt this year and we estimated that the company will need almost $1 billion each year in external financing through 1982.

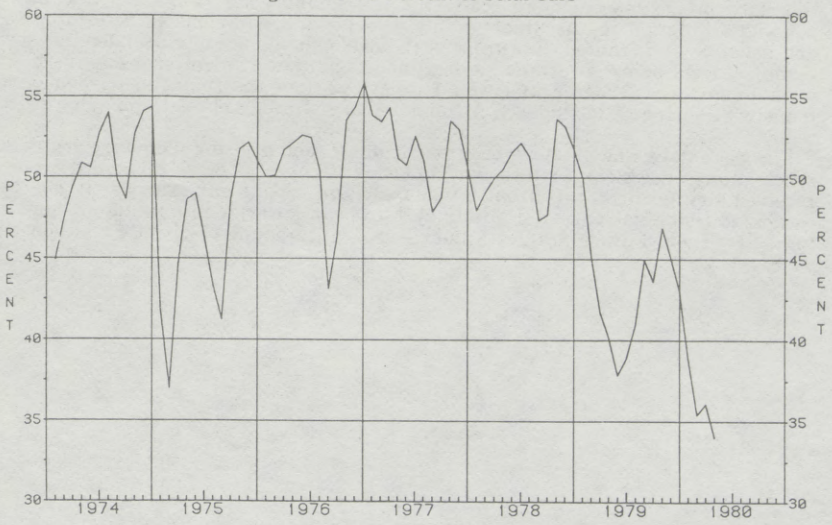
These sums are staggering by themselves but combined with the annual debt requirements of General Motors Acceptance Corporation and Ford Motor Credit, the auto industry's annual borrowing needs could exceed those of the telephone system. We wonder whether lenders will be willing to provide that amount of new capital annually to this industry. The general preception among investors is a growing awareness of GM's strength relative to Ford which might make it more difficult for Ford to attract the needed funds and, assuming it does, the company will have to pay higher rates.

The role of the U.S. government toward the auto industry has been as a legislator compared to that of the role of the Japanese government which is promotional and those of European governments which are entreprenurial. A shift in that attitude toward one of the other approaches would be important in the investment community's willingness to lend. There is an obvious reluctance to lend to regulated industries. Recently there have been many suggestions discussed to help the industry's cash flow through tax credits and the like aid in certain projects. While measures which would provide investment tax credit for model tooling expenditures, research and development or accelerated depreciation are intuitively appealing it should be obvious that the greatest benefits accrue to the company most capable of spending the greatest amounts of money—which is obviously GM. Proposals such as this have great merit and are used throughout the world to assist automakers, however, care

must be exercised that they don't distort the competitive balance any further. It is a fact that the cost of meeting regulatory standards is equal for each company and therefore proportionally more costly for the smaller ones. As such, a review of pending regulation in the areas of safety, noise and emissions to determine costs and benefits is warranted. In Europe such developments are often funded by several manufacturers or by governments—and additional government sponsorship of such work might be considered and would relieve part of the financial burden on the industry. Sharing of technology, a commonplace strategy abroad, might be permitted.

European governments have been particularly fond of using monetary grants and special tax concessions to lure new industry. General Motors and Ford have all received significant grants from Canada, Britain, Spain and Austria. It has been estimated that this year total grants by European governments to automakers will total $1 billion. Future grants through 1985 will amount to about $1 billion each year.

Large Cars As a Percent of Total Cars



Gasoline Prices

Gasoline Prices (line), Consumer Price Index (dash)

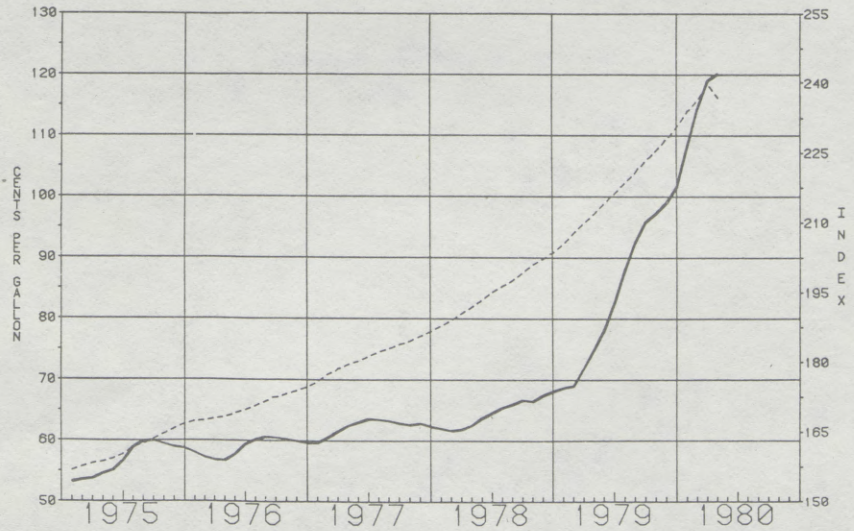


Table 1

General Motors Corporation
Cash Flow Analysis
(Dollars in millions, except per share data)

	1974	1975	1976	1977	1978	1979	1980E	1981E	1982E	1983E	1984E
Sources:											
Net income	$ 950	$ 1,253	$ 2,903	$ 3,338	$ 3,508	$ 2,893	$ (584)	$ 1,785	$ 3,040	$ 4,158	$ 5,304
Per share	3.27	4.32	10.08	11.62	12.24	10.04	(2.00)	6.00	10.00	13.00	17.00
Depreciation	846	906	939	974	1,181	1,237	1,450	1,750	2,100	2,450	2,750
Amortization	858	1,180	1,297	1,406	1,856	1,950	2,250	2,580	2,900	3,300	3,600
Other	106	66	56	(158)	(65)	(321)	100	150	200	200	250
Total from operations	$ 2,761	$ 3,405	$ 5,195	$ 5,560	$ 6,480	$ 5,759	$ 3,216	$ 6,265	$ 8,240	$10,108	$11,904
Issuance of stock	—	—	3	2	20	250	250	280	250	250	250
Issuance of debt	242	753	129	131	112	41	2,000	2,000	1,000	500	200
Total sources	$ 3,003	$ 4,158	$ 5,327	$ 5,693	$ 6,612	$ 6,050	$ 5,466	$ 8,545	$ 9,490	$10,858	$12,354
Applications:											
Dividends	$ 986	$ 701	$ 1,603	$ 1,958	$ 1,725	$ 1,533	$ 861	$ 713	$ 730	$ 1,232	$ 1,716
Per share	(3.40)	(2.40)	(5.55)	(6.80)	(6.00)	(5.30)	(2.95)	(2.40)	(2.40)	(4.00)	(5.50)
Net capital expenditures	1,391	1,103	906	1,760	2,612	3,205	4,000	4,600	4,500	4,200	4,200
Expenditures for tools (net)	1,096	1,036	1,308	1,776	1,827	2,015	3,100	3,600	3,800	3,800	3,800
Decrease in debt	122	406	282	106	201	140	50	100	100	150	200
Other	63	60	65	19	(72)	418	100	100	100	150	150
Total applications	$ 3,658	$ 3,306	$ 4,164	$ 5,619	$ 6,293	$ 7,311	$ 8,111	$ 9,113	$ 9,230	$ 9,532	$10,006
Beginning working capital	$ 6,197	$ 5,542	$ 6,394	$ 7,557	$ 7,630	$ 7,949	$ 6,688	$ 4,043	$ 3,475	$ 3,735	$ 5,061
Change in working capital	(655)	852	1,163	74	319	(1,261)	(2,645)	(568)	260	1,326	2,288
Ending working capital	$ 5,542	$ 6,394	$ 7,557	$ 7,630	$ 7,949	$ 6,688	$ 4,043	$ 3,475	$ 3,735	$ 5,061	$ 7,349
Cash flow adequacy:											
Sales	$31,549	$35,725	$47,181	$54,961	$63,221	$66,311	$57,500	$63,500	$73,000	$83,000	$94,000
Incremental sales	(4,249)	(4,176)	11,456	7,780	8,260	3,090	8,811	6,000	9,500	10,000	11,000
Year-end w.c. as % of sales	17.6%	17.9%	16.0%	13.9%	12.6%	10.1%	7.0%	5.5%	5.1%	6.1%	7.8%
Projected change in w.c. (LIFO)							(2,645)	(568)	260	1,326	2,288
Required increase in w.c. (LIFO)							(881)	600	950	1,000	1,100
Net excess (shortfall)—(LIFO)							(1,764)	(1,168)	(690)	326	1,188
Cumulative excess (shortfall)							(1,764)	(2,932)	(3,622)	(3,296)	(2,108)

end of file 16b

TABLE 2.—GENERAL MOTORS FINANCIAL STATUS

[Dollars in millions]

	Long-term debt	Shareholders' equity	Total capital	Debt/total capital, percent	Debt/equity, percent
1984E	$5,980	$28,072	$34,640	17.3	20.9
1983E	5,980	25,072	31,052	19.3	23.9
1982E	5,630	21,896	27,526	20.5	25.7
1981E	4,730	19,336	24,066	19.7	24.5
1980E	2,830	17,984	20,814	13.6	15.7
1979	880	19,179	20,059	4.4	4.6
1978	979	17,570	18,549	5.3	5.6
1977	1,068	15,767	16,835	6.3	6.8
1976	1,070	14,385	15,455	6.9	7.4
1975	1,223	13,082	14,305	8.5	9.3
1974	876	12,531	13,407	6.5	7.0

Table 3
Ford Motor Company
Cash Flow Analysis
(Dollars in millions, except per share data)

	1974	1975	1976	1977	1978	1979	1980E	1981E	1982E	1983E	1984E
Sources:											
Net income	$ 361	$ 228	$ 983	$ 1,673	$ 1,589	$ 1,169	$(1,089)	$ 246	$ 1,000	$ 1,524	$ 1,935
Per share	3.09	1.95	8.36	14.16	13.35	9.75	(9.00)	2.00	8.00	12.00	15.00
Depreciation	531	584	590	629	736	896	1,150	1,400	1,600	1,750	1,950
Amortization	393	435	431	488	578	708	900	1,125	1,225	1,375	1,525
Other	(44)	(27)	(6)	198	191	233	200	200	225	225	250
Total from operations	$ 1,361	$ 1,288	$ 2,029	$ 3,021	$ 3,314	$ 3,290	$ 1,211	$ 3,046	$ 4,150	$ 5,074	$ 5,960
Issuance of stock	3	29	11	40	57	33	50	50	50	50	50
Issuance of debt	579	218	186	69	35	368	1,500	1,200	750	500	400
Total sources	$ 1,943	$ 1,535	$ 2,226	$ 3,130	$ 3,406	$ 3,691	$ 2,761	$ 4,296	$ 4,950	$ 5,624	$ 6,410
Applications:											
Dividends	$ 298	$ 243	$ 263	$ 359	$ 417	$ 468	$ 303	$ 123	$ 125	$ 318	$ 516
Per share	(2.56)	(2.08)	(2.24)	(3.04)	(3.50)	(3.90)	2.50	1.00	1.00	2.50	4.00
Net capital and tool spending	1,415	911	1,025	1,744	2,525	3,413	3,100	3,800	4,000	3,900	3,850
Decrease in debt	79	160	309	121	250	238	225	100	200	325	350
Other	311	56	49	163	111	356	200	200	250	250	250
Total applications	$ 2,103	$ 1,370	$ 1,646	$ 2,387	$ 3,302	$ 4,475	$ 3,828	$ 4,223	$ 4,575	$ 4,793	$ 4,966
Beginning working capital	$ 1,660	$ 1,500	$ 1,666	$ 2,246	$ 2,789	$ 3,093	$ 2,309	$ 1,242	$ 1,315	$ 1,690	$ 2,521
Change in working capital	(160)	165	580	743	103	(784)	(1,067)	73	375	831	1,444
Ending working capital	$ 1,500	$ 1,666	$ 2,246	$ 2,989	$ 3,093	$ 2,309	$ 1,242	$ 1,315	$ 1,690	$ 2,521	$ 3,965
Cash flow adequacy:											
Sales	$23,621	$24,009	$28,840	$37,842	$42,784	$43,514	$34,000	$37,500	$42,000	$47,500	$54,500
Incremental sales	606	388	4,831	9,002	4,492	730	(9,514)	3,500	4,500	5,500	7,000
Year-end w.c. as % of sales	6.4%	6.9%	7.8%	7.9%	7.2%	5.3%	3.7%	3.5%	4.0%	5.3%	7.3%
Projected change in w.c. (LIFO)							(1,067)	73	375	831	1,414
Required increase in w.c. (LIFO)							(450)	175	225	275	350
Net excess (shortfall)							(617)	(102)	150	556	1,094
Cumulative excess (shortfall)							(617)	(719)	(569)	(13)	1,081

end of file 16d

TABLE 4.—FORD MOTOR FINANCIAL STATUS

[Dollars in millions]

	Long-term debt	Shareholders' equity	Total capital	Debt/total capital, percent	Debt/equity, percent
1984E	$4,425	$12,902	$17,327	25.5	34.3
1983E	4,375	11,433	15,808	27.7	38.3
1982E	4,200	10,177	14,377	29.2	41.3
1981E	3,650	9,252	12,902	28.3	39.5
1980E	2,550	9,079	11,629	21.9	28.1
1979	1,275	10,421	11,696	10.9	12.2
1978	1,145	9,686	10,830	10.5	11.8
1977	1,360	8,457	9,817	13.8	16.1
1976	1,411	7,107	8,518	16.5	19.9
1975	1,534	6,350	7,884	19.4	24.2
1974	1,477	6,241	7,718	19.1	23.7

U.S. TREND IN IMPORT NEW-CAR STOCKS, IMPORT INVENTORY BY COUNTRY OF ORIGIN

	Japan	West Germany	Other	Total
1978:				
January 31	348,307	106,583	72,062	525,952
February	382,077	115,768	78,411	576,256
March	393,704	119,571	78,965	591,240
April	420,793	115,542	75,892	612,227
May	441,826	104,252	79,938	626,016
June	474,050	112,552	89,032	675,634
July	453,150	113,616	84,872	652,638
August	428,931	98,929	67,380	595,240
September	417,874	80,134	64,328	562,336
October	436,874	81,399	55,927	574,200
November	474,860	84,285	69,510	628,655
December	493,760	83,808	83,601	661,169
1979:				
January	525,057	76,156	91,192	693,405
February	529,703	75,422	83,077	688,202
March	474,423	66,604	97,993	639,020
April	426,217	64,200	83,820	574,237
May	337,075	62,124	85,886	485,085
June	315,982	61,622	83,227	460,831
July	304,225	51,645	79,164	435,034
August	269,806	47,842	68,070	385,718
September	260,096	48,424	63,715	372,235
October	278,938	51,819	72,607	403,364
November	298,508	62,723	72,597	433,828
December	308,524	62,247	85,851	465,352
1980:				
January	283,219	70,432	61,783	415,434
February	251,554	70,732	82,932	405,218
March	245,371	79,860	96,705	421,936
April	252,226	94,942	99,561	446,729

Senator RIEGLE. And now, Dr. Baldwin?

STATEMENT OF ROBERT BALDWIN, PROFESSOR OF ECONOMICS, UNIVERSITY OF WISCONSIN

Dr. BALDWIN. Thank you, Senator.

Senator RIEGLE. We'd also appreciate it, too, if you can summarize as briefly as possible.

Dr. BALDWIN. I should like to begin by answering the questions concerning the possibility of imposing import constraints on autos within established international rules that you asked me about in your letter.

One approach, that the United Auto Workers has just utilized is to seek import relief through sections 201 through 203 of the Trade Act of 1974. This is an approach that all trade specialists can approve of.

It involves an orderly, rational evaluation of an import problem in which the facts can be fully and carefully developed by the industry, by the importers, and most important, by the International Trade Commission.

A determination can then be made by this semijudicial body as to whether these facts fit the conditions for import relief laid down by Congress.

Moreover, any import relief granted under this approach is fully consistent with the international rules to which the United States has agreed.

DIFFERENCE BETWEEN PROTECTIVE MEASURES

There is a very significant difference between protective measures adopted within the framework of agreed-upon international rules, and unilateral actions taken outside of these rules.

The first promotes international order and harmonious relations; whereas the second fosters international bitterness and hostility.

Unfortunately, some who favor protection on a permanent basis continue to pose the policy choice we face as being between free trade and selective protection.

Actually, the relevant choice is between international economic order, in which selective protection is permitted, under fair, reasonable conditions, and international disorder, in which everyone goes his own way.

The type of protection being sought by the UAW fits the former case, and should be strongly supported.

Now what about the possibilities of an affirmative decision in this case? I should stress first of all that three conditions must be met, and they must all be met at the same time:

First, imports of an article must have increased absolutely or relative to domestic production.

Second, the domestic industry must be seriously injured or threatened with serious injury.

And third, increased imports must be a substantial cause of serious injury or threat thereof.

I don't see any great problems with the first two. Clearly the industry has been seriously injured, and imports have obviously increased, both absolutely and relative to domestic production. It's the last criteria that may be a source of difficulty, because the 1974 act specifically defines substantial cause to mean "a cause which is important and not less than any other cause."

Now there seems to be general agreement, as has been pointed out, on just why the industry is in trouble. The oil crisis touched off a shift in consumer taste toward more fuel-efficient cars.

In response to that preference change by consumers, imports increased very rapidly. At the same time domestic sales of small cars increased. It was large car sales that decreased here.

So it seems to be that increased imports were a response to a shift in consumer buying patterns rather than an initiating factor.

In addition we now have another causal factor at work, namely, the recession itself. We see that imports are now beginning to decrease as well as domestic production.

In the over 40 import relief cases that the ITC has handled, there have been 5 in which the Commission has rejected the petition on the grounds that imports were not a substantial cause of injury.

In three of these cases, the ITC decided that injury was due to some general economic condition, like a recession. One of the other two cases involved the auto industry itself. When the auto industry switched to purchasing lighter parts made of plastics and aluminum, this had an adverse effect on the zinc industry, and production went down. The commissioners agreed that the zinc industry was seriously injured, but they determined that increased imports were not the substantial cause. The injury was a result of the increased mileage standards imposed by the Environmental Protection Agency.

The wrapper tobacco case is another example where the ITC rejected import relief. Everyone agreed that the industry was injured, but it seemed to be due to declining sales of large cigars, which in turn was related to the public health warning against smoking.

So the Commission is going to have to decide whether this case is similar to the ones I have just cited, or whether the increased imports themselves are a substantial cause of injury.

Of course, one can do no more than speculate until the facts are fully and carefully developed before the ITC, as I am sure they will be. But I personally would not be overly optimistic about the possibilities of obtaining import relief by the section 201 route.

Another way to gain import relief is to use section 301 of the 1974 Trade Act as amended by the Trade Agreements Act of 1979. The President himself can directly impose import restrictions if he believes that the policies of another country are, for example, unjustifiable, unreasonable, or discriminatory to U.S. commerce.

IMPORT CONTROL

There have been calls for this type of import control because of the nontariff barriers we face in exporting U.S. cars to Japan.

I think there is no doubt that we do face some serious nontariff barriers against auto exports to Japan and to other countries, but I would suggest the proper way to deal with this problem is to utilize the new codes that we have just agreed upon in the Tokyo round, particularly the codes on standards and the code on customs valuation practices.

Now a final means to gain import relief would be for the Congress to directly impose quotas or other restrictions. Congress, on the basis of the Constitution, has the full right and responsibility for regulating foreign trade.

One proposal that the UAW has made, and the Ford Company has supported, is that Congress should approve import quotas coupled with a 75 percent U.S. content requirement for the sales of any foreign autos beyond the quota limits.

A domestic content requirement such as this is not consistent with the national treatment provision of the General Agreement on Tariffs and Trade (GATT). Paragraph 5 of that agreement specifically states:

> No contracting party shall establish or maintain any internal quantitative regulations relating to mixture, processing, or use of products in specified amounts or proportions which requires, directly or indirectly, that any specified amount or proportion of any product which is subject to the regulation must be supplied from domestic sources.

I think there is no doubt that if a domestic content requirement was introduced, it would have adverse effects on U.S. exports. There may not be direct and immediate retaliating action. That isn't what we should worry about. What one has to be concerned about is that foreign countries will drag their feet in removing the very many other barriers that impede U.S. trade.

I feel that the United States has a great potential for additional exports if all countries liberalize and harmonize regulations in the areas of government purchasing policy and product standards. An action like this, I think, would give other countries a perfect excuse

for not accelerating their liberalizations in these areas, and would have adverse effect on U.S. exports.

In several respects, the auto industry actually fits the classic description of an infant industry. It needs time until it can acquire the know-how and training to produce small fuel-efficient cars at a competitive price.

But we also know that the best way to deal with the infant industry case is not through import controls, but rather through direct financial assistance to the workers and, if necessary, to the industry itself.

Quite aside from the international repercussions of any import actions, there is a question of whether import controls really would help the industry from an employment viewpoint. I won't go into this very much. George Eads testified not long ago about the possibilities.

Senator RIEGLE. I might say there is some strong difference of opinion on that.

Dr. BALDWIN. Right. But he did, in his testimony, come up with a rather modest employment increase. Even taking some rather extreme cases, it seemed that the employment impact was rather modest.

A study that has recently been completed at Wisconsin, one of our Ph. D. theses, tends to support Dr. Eads' conclusion. The student found the substitution possibilities between foreign cars and domestic cars was not very high, by no means a one for one relationship. To block out foreign cars doesn't mean you are going to buy many large domestic cars.

What she did find was that the sales of domestic cars were quite responsive to changes in the prices of domestic cars. This suggests the possibility perhaps of rebates, or other means of lowering the price of domestic cars in order to increase their sales. Her analysis suggests that a 5-percent decrease in price could lead to between 6- and 11-percent increase in the quantity sold. That could be quite substantial.

In this connection, I'd like to point out that to keep the price of U.S. cars competitive, you must also be concerned about protectionism in other sectors.

For example, the trigger price mechanism in the steel industry tended to keep the price of steel higher than it otherwise would have been.

Of course, since the auto industry is an important user of steel, this tends to put the industry at a competitive disadvantage.

Now I might just briefly comment on some of the barriers to exports of U.S. cars. I think this has been gone over fairly well. We know the Japanese have several of them, particularly their whole inspection process, where they can look at every single item, rather than use a sampling technique. They also still have very high commodity tax, even though they reduced it from something like 40 to 20 percent.

Other countries also have nontariff barriers impeding U.S. auto exports. The French have a road-use tax which tends to discriminate against the larger cars. During the Kennedy round, we actually reached an agreement with the European Community whereby they would reduce this tax. But it was not approved by the Con-

gress. It was tied up with removal of the American Selling Price system of customs valuation.

I would suggest that the best way to handle this whole problem of nontariff barriers and our export potential is to utilize the new codes and press our case for eliminating some of these unreasonable barriers within the GATT framework.

I think we must also recognize that even if we eliminated all of these barriers, the possibilities for increasing U.S. auto exports are limited. I don't think this is going to, by any means, solve the problem. I tend to think that, even with a successful transition, the auto industry is not going to reemploy all the workers that they had in 1978. I think we have to look forward to a reduction in employment in the auto industry, and I would urge that more action be taken concerning what is going to become of those excess workers?

Workers in my State of Wisconsin, in Janesville, may not in the long run end up producing small cars. They may be permanently unemployed. You must begin to think of what other industries can be brought into that area. How can these workers be retrained? What aids can be given to facilitate their adjustment?

It doesn't do any good to have foreign auto companies come in and build plants in California or Ohio, while the workers, in Detroit and in my State remain unemployed.

We must begin to focus attention on these workers.

Senator RIEGLE. Well, let me thank you for your statement. I just want to make two brief comments, and then Dr. Cole, I know, has to leave, and so I thought we might ask a few questions before we go to our last witness.

But I think the scale of the number of displaced workers that you speak about is something that we really have to ponder and look at, because if we are talking about the need to absorb maybe as many—it's not just the directly employed auto workers, but the tremendous infrastructure, the secondary jobs that are attached to this industry, we could easily be talking about a half million jobs, and in a situation where job creation isn't moving along all that swiftly, anyway, the talk about having to find a way to absorb that volume of worker displacement I think is an altogether different magnitude task than we have even started to debate.

The other point I would just make in passing, and that is with respect to Eads' analysis—and we have gone through this at endless length with him and the others at the Council of Economic Advisers—I think it is important to point out that they argue that in the very short run, in a 4- to 6-month period, that they don't see much gained by import restrictions.

We have some difference of opinion on that. But if one stretches it out over the period of the transition, say 2½ years to 3 years, then the analysis changes quite dramatically.

Eads is prepared, I think you will find, to acknowledge that there would be substantially higher reemployment, say, after 1 year, and that capital formation in the domestic industry would be enhanced.

Now that doesn't minimize some of the subsidiary problems that you, I think, correctly raised here that have to be thought about as a tradeoff.

But the fact of the matter is it depends how long you talk about having some kind of device that would perhaps restrict imports, whether a marketing agreement or what-have-you, in terms of what the genuine economic effect turns out to be, and I think that's a very important distinction to make here, because I think we can have a very major effect if we want to talk about it, say, over a 2-year period rather than over a 4-month period.

[The statement follows:]

STATEMENT OF ROBERT E. BALDWIN, PROFESSOR OF ECONOMICS, UNIVERSITY OF WISCONSIN-MADISON

TRADE POLICY AND THE U.S. AUTO INDUSTRY

I should like to begin by commenting upon the questions directed to me in the letter from Senators Stevenson and Riegle inviting me to testify that concern the possibilities and consequences of imposing restraints on imports of automobiles.

One approach is to seek temporary import quotas or increased tariffs through the import relief sections of the Trade Act of 1974, namely, Sections 201-203. Under these provisions the International Trade Commission initiates an investigation to determine whether an article is being imported in such increased quantities as to be a substantial cause of serious injury, or threat thereof, to the domestic industry producing a like or directly competitive article. The Commission reports its findings to the President who must accept a negative determination but can reject an affirmative finding. However, if he does reject an ITC recommendation for import relief, the ITC recommendation can be implemented by a majority vote of both Houses of Congress. The United Auto Workers union has recently filed a petition with the ITC for import relief under these provisions.

What are the chances of an affirmative decision from the ITC in this case? In considering the question it should be stressed that each of three conditions must be met before the ITC can recommend import relief to the President. First, imports of an article must have increased absolutely or relative to domestic production. Clearly, this condition is satisfied since, as Assistant Secretary of Commerce Katz reported in his March 18 testimony before the Trade Subcommittee of Ways and Means, imports of cars increased 16 percent in 1979 while sales of domestically produced cars fell 10.5 percent. Moreover, the import penetration ratio has increased steadily for many years and very significantly since 1976.

Secondly, the domestic industry must be seriously injured or threatened with serious injury. Although the industry as a whole has only been in serious economic difficulties since last fall and thus does not meet the 4- or 5-year period criterion sometimes used by the Commission, I would be surprised if the ITC did not find the injury criteria to be satisfied. The short-run decline has been so significant, e.g., 200,000 idle workers, large excess capacity, and poor profit performances, and the future outlook is so bleak that a finding of serious injury or threat thereof seems justified under the injury criteria established by Congress.

Finally, increased imports must be a substantial cause of serious injury or threat thereof. The 1974 Trade Act defines "substantial cause" to mean "a cause which is important and not less than any other cause." It is with respect to satisfying this third condition where I think an auto import relief case under Section 201 could run into difficulties.

There seems to be general agreement on just why the industry is faced economic hardships. The second oil crisis in 1979 triggered a rapid shift in consumer demand to small, fuel-efficient cars. Consumers were responding in part to the higher cost of fuel and, more importantly I think, to the prospect of continued long gas lines or outright gas rationing. The fact that sales of both imported small cars and domestically produced small cars increased in 1979 (16 percent and 8 percent, respectively) supports this interpretation and suggests that the increased imports were a response to a shift in buyer preferences rather than an initiating factor in the current difficulties for the auto industry. It should also be noted that, while purchases of domestically produced large cars fell by 1.2 million units, sales of imported and domestically produced small cars only rose 600,000 units. In recent months still another important causal factor has entered the picture, namely, the general recession. This is indicated by the fact that sales of some small cars, both imported and domestically produced, declined in May.

In the over 40 decisions the ITC has made under Section 201 of the 1974 Trade Act there have been 5 cases where it has made a negative finding on the grounds that imports were not a significant cause of injury. In three of these cases the

Commission decided that general recessionary conditions were more important than imports as a cause of the industry's economic problems. In the other two cases if focused on factors peculiar to the industry. In the unalloyed, unwrought zinc case, for example, the Commission pointed to the shift by the auto industry to such lighter weight materials as plastics and aluminum and away from zinc as the substantial cause of serious injury. This change in purchasing patterns by the auto industry was in turn caused by the requirement to increase mileage ratings imposed by the Environmental Protection Agency. Similarly, in the wrapper tobacco case the ITC found that the domestic industry's problems were caused mainly by the decline in the consumption of large cigars due to the public health warnings against smoking. Although imports of wrapper tobacco increased in contrast to domestic production, the Commission attributed this to the distinctive characteristic of these imports.

The Commission must decide whether the auto case is similar to the above cases or whether the increased imports themselves are a substantial cause of serious injury. Since the full set of facts will only be developed in the course of the Commission's investigation, one can only speculate about the outcome at this time. However, personally I would not be especially optimistic about the possibility of obtaining import restrictions via the Section 201 route.

A second method by which import restrictions on automobiles could be introduced is through the initiative of the President under Section 301 of the Trade Agreements Act of 1979. Under this provision of the law the President can directly impose restrictions if he believes that the policies of another country are, for example, unjustifiable, unreasonable, or discriminatory and burden U.S. commerce. There have been calls for restrictions against imports of Japanese cars under this section because of alleged import restrictions in Japan against U.S. cars. Such action could, however, immediately lead to some type of retaliation by Japan against other U.S. exports to that country or possibly to a request by the Japanese to the GATT for decision as to whether the U.S. action is justified.

A final means of introducing import controls is, of course, directly through Congressional action. One proposal by the UAW and the Ford Motor Company requiring Congressional action would be the imposition of import quotas coupled with a 75 percent U.S. content requirement for any sales by foreign auto makers beyond the quota limit.

A domestic content requirement such as this is not consistent with the national treatment provision of the GATT Paragraph 5 of Article III states: "No contracting party shall establish or maintain any internal quantitative regulation relating to the mixture, processing or use of products in specified amounts or proportions which requires, directly or indirectly, that any specified amount or proportion of any product which is subject to the regulation must be supplied from domestic sources."

There is little doubt in my mind but that the introduction of such a provision would lead to adverse effects on other U.S. export goods. It is not just a question of immediate retaliation but of a stiffening of foreign resistance to U.S. efforts to reduce the many foreign nontariff barriers that hamper our exports. We have a great potential for increasing our exports if we can reduce and harmonize foreign subsidies to industries, restrictive foreign requirements in the area of government procurement, and burdensome standard regulations by other governments. A domestic content rule on the part of the United States provides other governments with the perfect excuse for not increasing the degree to which their own economies are opened.

Quite aside from the international consequences of attempting to stimulate the domestic production of automobiles is the issue of whether such a policy will in fact provide significant help to the over 200,000 workers idle in the industry. In April George Eads of the President's Council of Economic Advisors reported to the Trade Subcommittee of Ways and Means his estimate that a 250,000 unit cutback in imported cars would provide only about 20,000 domestic jobs and a 500,000 unit cutback only 40,000 jobs. A recent study of one of our students at Wisconsin dealing with the responsiveness of domestic sales to changes in the cost of imported cars tends to support Eads' conclusion.[1] While the quantity of cars imported is quite responsive to the price of imported cars, raising the cost of imported cars by means of quotas or tariffs is not likely to stimulate a great rush for the purchase of domestic cars. There is not, in other words, a one for one substitution relationship between small imported cars and large, domestically produced automobiles.

One possibility that the study suggests might prove effective in stimulating employment is to lower the price of domestic cars through such schemes as rebates.

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[1] Jan—Yu Ho Li, "Short-Run Demand for Imports and Domestic Substitutes in the United States," Ph. D. Thesis, 1980 (unpublished).

Sales of domestic cars seems to be quite responsive to the price of these cars. The study indicates, for example, that a 5 percent reduction in the price of domestically produced cars would increase sales by between 6 and 11 percent. On the basis of current production levels this would mean between about 320,000 and 580,000 units annually.

The best long run solution to the problem is, of course, to increase the domestic production of competitively priced small cars. However, it is not going to help the over 200,000 unemployed auto workers if this takes several years or is accomplished by the expansion of foreign owned production in the United States in areas where the unemployed workers do not reside. To expedite the switch over to small car production and to undertake the production in the areas where the unemployed workers reside, more attention should be given in my view to mergers and other cooperative arrangements with foreign auto firms. These are the firms that already possess the technology needed to produce fuel efficient cars and this technology coupled with the superior production and marketing facilities of U.S. firms would seem to offer the best prospects of overcoming in the shortest time the current competitive advantage of imported cars over domestically produced ones. The American Motors case illustrates the benefits of this approach. Discussions such as these being held by Chrysler and Mitsubishi should be encouraged.

A final topic on which I wish to comment is the extent to which foreign trade barriers impede the sales of U.S. cars. One such barrier is road-use taxes that place a disproportionately high burden on the large cars that U.S. firms produce. The Japanese have such a tax but have significantly several years ago, Some of the countries in the European Community, e.g., France, also have discriminatory road-use taxes. During the Kennedy Round of trade negotiations an agreement was worked out with the Community by which these taxes would be reduced in return for the abolition of the American Selling Price method of valuing imports for customs purposes. However, the Congress did not accept this proposed NTB agreement. Now that ASP has been abolished as part of the latest trade negotiations we should renew our efforts to eliminate the discriminatory nature of foreign road-use taxes.

It is frequently alleged that the implementation of standards requirements in countries such as Japan unduly burden U.S. exporters. Fortunately the new standards code negotiated during the recently concluded Multilateral Trade Negotiations provides a means for raising this issue in an international forum and for seeking the correction of any discriminatory practices along these lines. The other codes covering domestic subsidies, customs valuation practices, and government procurement policy should also be used to ensure that our automobile exports are not being placed in a disdadvantageous position because of trade barriers in these areas.

Efforts to liberalize the barriers against automobile imports in the less developed countries also would be helpful in stimulating exports. At a minimum most developing countries impose very high duties on imports of finished cars and low duties on imports of automobile parts for local assembly. Many even have high duties on most parts so that even the components of automobiles and trucks are produced at high costs within the developing countries. Of course, if we are to penetrate these markets, we must also make concessions on the barriers we impose on imports of labor-intensive manufactures.

While the reduction of foreign barriers to U.S. automobile exports will provide marginal assistance to the industry, I think this sector will only regain its strength when it has switched much more extensively to the production of small, fuel-efficient cars that can compete with foreign-made automobiles. However, it seems likely that even if this transition is made successfully within a few years total employment in the industry is likely to decline appreciably. We must begin to make efforts to attract new industries to the affected areas and retrain the workers for the new jobs they must take.

Senator RIEGLE. But in any event, Dr. Cole, let us raise a couple of questions with you, and I'd like to just start with this one.

The Japanese now appear to have a lead over the United States in small cars. Some people think that we can catch up with a one-time all-out retooling effort. Others think that there may be a longer gap; that we may be in a situation where by the time we catch up, they have moved forward to a new generation of cars that pose a whole new challenge to us, and I am wondering what your view is on that.

Dr. COLE. I would tend to agree with that, Senator Riegle. The Japanese are progressing very rapidly on several fronts that we don't normally think of as constituting automotive technology.

For example, in your opening statement you mentioned the great productivity of new Japanese facilities. They are making tremendous progress from the manufacturing side, in addition to progress on the design side.

Fortunately for the United State most of the Japanese manufacturers are faced with the very expensive reconfiguration of their vehicles to front engine-front drive. This reconfiguration is necessary to make them suitable for the market of the middle and late 1980's.

The Japanese are investing vast quantities in research, and basic engineering in an intense effort to develop markets all over the world.

CONTINUED COMPETITIVE PROBLEMS WITH JAPAN

I think we are not going to see a ceasing of the competition problem as the industry in this country just makes the transition to more fuel-efficient front-drive vehicles. We are going to continue to have a problem with the Japanese and I think it is one of the reasons that I am so concerned about the post-1985 period and the fact that we should be doing more work in technology to prepare ourselves for the continuing confrontation with our friends overseas.

Senator RIEGLE. Let me ask you this:

Some people say that it will be 1983 before the domestic industry is really competitive across the board with the Japanese. Do you agree with that, first of all, as a rough timeframe?

Dr. COLE. I think that may be soon. I think across the board——

Senator RIEGLE. In other words, in——

Dr. COLE. It will be probably 1985. We have some serious limitations, and in some cases the industry itself may not be very good at assessing these limitations. The problem, for example, of the machine tool industry being able to furnish the highly productive manufacturing capacity needed to make the new drive trains and new engines is a serious problem.

We just can't turn that industry on quickly.

Senator RIEGLE. Somebody told me the other day that every tooling company in the world is booked to capacity right now trying to digest this transition in the auto industry.

Dr. COLE. That's absolutely correct, with one caveat on that, and that is they are tooling companies that are capable of producing high productivity manufacturing equipment. Old fashioned tooling companies are not so busy. New equipment must be related to high productivity. That's the message of the next 5 years.

Senator RIEGLE. Well, the second part of my question, though, is if in your view it may be 1985 and not 1983 before the domestic companies are really positioned to go ahead with the Japanese, my question is, as you project the trend lines for the Japanese versus the trend lines for the domestic industry, will we in fact be on a par in 1985, or will they have made a new technological advance that puts them some distance ahead of where we otherwise will be in 1985?

Dr. COLE. I think we will be very fortunate if they don't move ahead by a substantial increment in 1985. I think new technology of engines and so on is going to be implemented by the Japanese. We are so caught up with the short-term problems, we are not recognizing the target is moving really rather fast.

Senator RIEGLE. Well, if we were going to mount a massive national effort, and it's sort of the teamwork approach with business, Government, and labor, sort of the CARP formula or something like that, where in your view would that best be done in order to get this job done? There is a division of opinion. Some say do it under the aegis of the Department of Transportation; others say, no, pull it out of there and put it in NASA, and I wonder if you have a view on that and what it would be.

Dr. COLE. I am a member of the NASA Space Science and Technology Advisory Committee and Energy Subcommittee. Our subcommittee reviews NASA activities in the energy field. I am unsure whether NASA or DOT is the proper organization to deal with this matter. I think we have to find a relationship between Government and industry that is mutually attractive in regard to this task.

I know that presently the automotive industry is less than enthusiastic about certain elements of the Government being involved in research that might have any relationship to a regulatory agency.

I think it is important to try to develop an administrative structure within Government and industry that we can all be happy about, if we are going to be productive in developing a major research effort.

It's taken much longer than I thought to develop this relationship with regard to the CARP program. I'm hopeful that an accommodation can be reached rather soon, because unless we begin tapping some of the advanced technological resources, we are just enhancing the probability that our problems are going to be even greater in the years ahead.

Senator RIEGLE. It sounds to me like you're saying we ought to treat this with sort of wartime seriousness in terms of the nature of the mobilization effort, and that we've got to blend these sectors into a common effort over and beyond anything we have seen in recent times.

Dr. COLE. Absolutely.

Senator RIEGLE. Senator Lugar is here, and Dr. Cole has a time problem that will force him to leave shortly, and I don't know if there are any particular questions that you would like to raise. I know Senator Stevenson has some, too, but I want Senator Lugar to have an opportunity to be able to make any opening statement that he wishes. But I wonder if we could finish with Dr. Cole. You may have questions, and then Senator Stevenson may, and then maybe we can excuse Dr. Cole and then have any opening statement that Senator Lugar may wish to make.

Senator LUGAR. Thank you, Mr. Chairman.

I was intrigued by the analysis that you had, Dr. Cole, under the section of motor vehicle manufacturers. You report there is a 10-point chronology of what occurred during the transition period in the auto industry. Specifically, you point out that for a long time our gasoline prices were more strictly controlled, and thus very

low, and that American consumers made a logical choice in terms of comfort and safety when they bought large cars.

This runs, I suppose, counter to all the popular wisdom presently, because we all know, in quotes, almost as revealed truth, that nothing other than a small car will do in this country.

But the facts are that after the panic is over, a lot of Americans probably still would like a safe car, and probably would like a comfortable car, too.

Do you have any comment at all while we are all, in pursuit, about how the demand for small cars is to be met? The demand is obviously real, and it is obviously being met by Japanese cars, or other foreign cars but is there any opportunity that you can see as an analyst of this industry, and you have followed it over the years, that in the meanwhile American companies will be able to sell a fair number of cars on the basis of comfort and safety, in addition to fuel economy?

Or is there such a panic in the land that literally this idea is passe, and we are fated simply to see a good part of the production of the industry in disarray, people unemployed, and what-have-you, in this interim period?

PANIC PERIOD

Dr. COLE. I think we are certainly in a panic period that is somewhat analogous to the Arab embargo of the early 1970's, and I expect we will have some reemergence of a larger vehicle market, although I would guess not to the extent that it was prior to the Iranian crisis.

In general, we are going to see a far more attractive comfortable small car that should, with the advancements that have been made in technology, be equally comfortable in terms of quietness, ride, and other characteristics to the larger vehicle. Many improvements have been made in the small car safety area as well.

Perhaps you have seen some data on the GM "X" cars, which are probably an average size car of 1985 to 1990. They have been able to pass some of the key safety tests that NHTSA has performed on them. Whereas many larger vehicles have not.

Certainly there is going to be a difference in safety if for no other factor than just the mass difference between the small car and the big car and how they might interact in an accident.

One thing is clear. There will be an intense marketing effort to move people away from the concept of size as a discriminatory factor in cars. I think we are going to find very, very expensive small American cars as well as less expensive small cars.

We also have to recognize that we have a market in this country that demands in part large passenger and luggage volume. That is, we have a great number of large families. In the future we are going to be looking at a spectrum of package sizes more realistic, perhaps, than we are seeing right now. The current model mix is heavily influenced by the problems of a general recession and the aftereffects of the Iranian fuel crisis and rapid fuel price rise and uncertain availability.

All in all, I would say that the industry has the message. Cars are going to be more realistic in terms of what the consumer will need and demand. They are not going to be less comfortable. They are going to be a more attractive buy, and I think substantially

more so than many of the products that have been made up until this very year.

Senator LUGAR. Dr. Cole, admittedly a so-called conventional family, as we used to call them, is no longer the conventional family. But take my own situation. I have a wife and four boys, and so there is six of us. A fairly large station wagon has been a staple of our transportation for a long time. I trust that's probably true for a lot of people in this country. And it's not comforting at all to hear that the station wagon might be smaller and more expensive.

As a matter of fact, I think I would prefer about the same size and pay more for the gasoline.

Is it not the case that the crisis that we are facing now—and there is some unanimity of feeling, I think, with Doug Fraser and the automobile managements on this—came about when the American public feared it couldn't get any gasoline?

In other words, through the crisis actually contrived by the Federal Government and its overly controlled policies in our economy, there came panic through lines. Once consumers thought that you really couldn't get gasoline, whatever the price, didn't people begin to shift their demands markedly.

Conversely, if they were assured that there would be ample supplies of gasoline at the market price, whatever supply and demand dictates, would this not change the configuration of this problem very substantially?

In other words, if we made true economic decisions as Americans would we not simply decontrol gasoline to begin with, and have done so a long time ago? Would we not be assured that we have a supply at whatever level the market calls for, and then make rational decisions on safety and comfort and whether our families need station wagons, and things of this sort? I would suggest that the alternative is upon us—a panic which has thrown 300,000 people out of work, and now costs us billions of dollars in compensatory payments to people who would prefer to work, and an opening up of our whole market to jeopardy from the Japanese and others?

Wouldn't a sensible policy be a return to market economics, freedom of choice of Americans, as to what they want to pay for gasoline as opposed to safety and the rest?

Dr. COLE. I agree completely. I think the fuel supply uncertainty was the triggering mechanism rather than cost in leading us to the escalation of small car demand last spring (1979). Certainly there is some elasticity related to cost. I am not an economist and I don't understand this consideration in detail, I believe a free market choice will lead to the production of a spectrum of fuel-efficient vehicles which will meet the broad demands of the consumer, assuming of course fuel is available.

In my personal life, I, as you, Senator Lugar, have looked at the situation of vehicle needs. I only have two boys, but I do have a very large Labrador retriever. [Laughter.]

I am a station wagon person, at least for trips. I have no alternative, until the boys and the dog leave. [Laughter.]

We have a station wagon that we keep in a barn and we bring it out when we want to go fishing or spend weekends together in the country.

I think we have to recognize that there is a market for a distribution of vehicles, large and small, skewed more toward the small than in the past.

Senator LUGAR. Thank you very much.

Senator RIEGLE. Senator Stevenson.

Senator STEVENSON. Thank you, Senator Riegle.

Dr. Cole, you referred somewhat respectfully, I thought, to the manufacturing procedures of the Japanese. What will be the effect of increased Japanese investment in Japanese assembly plants for the production of small automobiles in the United States? What will the effect on American producers and American workers be?

Dr. COLE. The major effect from the Japanese standpoint is that their cost will be reduced in terms of labor hours per unit produced. This will give them relatively strong leverage on price.

Senator STEVENSON. Excuse me. I didn't make the question clear. I meant——

Dr. COLE. No, I was going to get to that.

Senator STEVENSON. [continuing]. With respect to those investments in the United States.

Dr. COLE. Oh, if they were to make those investments in manufacturing capacity in the United States to produce——

Senator STEVENSON. I assume they won't make any other kind of investments in the United States.

Dr. COLE. I would hope that we would learn some lessons from what they are doing in manufacturing technology. If they were to build a plant here as Honda is doing presently in Columbus, Ohio, I would assume that the manufacturing technology associated with that plant will be much less labor-intensive than the typical American plant.

Of course, you have to recognize that we have situations as with Pontiac, where recently they decided that an entire plant is out of date. They are essentially abandoning it in favor of a brandnew ground-up factory which is going to incorporate the best knowledge that we have today in manufacturing technology.

JAPANESE MORE AGGRESSIVE

I think the Japanese are perhaps more aggressive in the pursuit of advanced manufacturing technology than we are, and of course you have to recognize another concern of the Japanese. They are very concerned about several potential competitors, the Taiwanese, the South Koreans, and others, that have relatively low labor costs in comparison to their own.

Senator STEVENSON. What is the answer to the question? There is as you know a big effort to encourage the Japanese to invest in assembly facilities here, and I am leaving aside components; let's confine it for the moment to assembly facilities.

You indicate that Japanese facilities are less labor-intensive; they are labor-unintensive. There are, of course, many other factors involved, including all the inputs, energy, steel, and so on.

But what will be the effect of that form of Japanese competition on the domestic producers? Will it put them to a greater or a lesser

disadvantage? What will be the net effect on the employment of auto workers in the United States? Will there be more facilities here, perhaps? I don't know. Less in Japan. Will the net effect be a plus, or a minus?

Dr. COLE. I think that's very difficult to answer in specific terms. Certainly by having manufacturing facilities here, I would suspect that they would have far less pressure to hold back sales of their products. That is it essentially would open the door to increased sales as they would be able to produce here and offshore.

I think that the Japanese——

Senator STEVENSON. And offshore.

Dr. COLE. Pardon?

Senator STEVENSON. And offshore.

Dr. COLE. They will become part of the auto industry here very much as Volkswagen has become a part of the domestic industry. They—VW—are still importing substantial numbers of vehicles from Germany. They have become a part of our structure, so to speak and so will the Japanese if they produce cars in this country.

One key fact is that the Japanese are going to continue to place a price ceiling on the American product, and this becomes a serious problem for the American manufacturer as he attempts to recover some of his enormous capital investment. Of course the consumer benefits but the domestic industry will recover more slowly.

I am still not sure I am answering your question, and I don't know if there is an answer because of the uncertainties involved.

Senator STEVENSON. Well, that's a good enough answer. The Government acts as if the answer was certain, and so does the UAW. I am suggesting and you are agreeing, that the answer is very uncertain.

Dr. COLE. Yes.

Senator STEVENSON. If these efforts succeed, the effects may be adverse for American producers already suffering from severe foreign competition, and the autoworker may suffer more, too.

You said at one point you thought the American producers would be competitive by about 1985, and then shortly after that you indicated that foreign automotive and manufacturing technology is being pushed ahead rapidly, that it is not a static world. How competitive will the domestic producers be in 1985? It's said that Detroit may produce between 10 and 11 million small cars by then, but how competitive can we expect them to be in terms of quality, fuel economy, innovation, and design? What will the competition be producing by then?

Dr. COLE. The competition is going to increase their production of small front-drive cars, and as I mentioned earlier, the Japanese are in transition now from the front-engine rear-drive to front-engine front-drive technology. Toyota and Nissan have a substantial conversion task ahead.

Honda, of course, is already there. As it occurs to me, the major expense of downsizing is in basic engines and drive trains. In 1985, our industry will be essentially there. The costs of added improvements are going to be much, less in my opinion. That is when we start talking about the hardcore dollar cost of building these new cars, the largest costs are in the engine and drive train area. It

should be less costly to bring other fuel saving technologies to the market place.

You have asked or commented on quality which is obviously a very serious issue. In my discussions with people in the automotive industry, it is clear substantial strides are being made right now in quality. For example corrosion protection has been improved dramatically.

Unfortunately, quality is a very difficult issue to define. Consumers generally think in terms of "fits and finishes," how smooth that finish is, how good the paint job is, how big the crack is between the fender and the hood. That's part of quality, and the Japanese in particular, and certainly many of the Europeans, have done an extraordinarily good job of paying attention to those kinds of details for many years.

But when we go beyond that form of quality, below the surface quality, we find that the U.S. product is at least comparable on a per dollar basis to what is offered from overseas; for example in terms of maintenance requirements, the durability of major subsystems such as the engine, transmission, and major suspension components.

All in all, we have to be very concerned about the moving target the foreign manufacturers are presenting to us. Perhaps I should have mentioned earlier that one of the things that will characterize the decade of the 1980's is technology. We are going to see technology become a much more important factor in vehicles.

I am not worried about General Motors and its ability to develop advanced technology. They are making rapid progress and their capabilities are enormous, as Ms. Keller has discussed earlier, in terms of the financial side. But some of the other manufacturers may have more serious problems in being able to be a part of the advanced technology revolution.

In fact, by 1983, General Motors, I think, should be broadly competitive internationally. It will be 1985 before some of the other manufacturers will be broadly competitive.

ENGINES AND DRIVE TRAINS

Senator STEVENSON. You mentioned downsizing and underscoring the engine and the drive train. Where will these small car components come from in 1985? Will General Motors and Ford and Chrysler be making all of their own engines and transmissions then?

Dr. COLE. Some of them are likely to come from offshore, with the emergence of the world car and parts that can almost be interchangeable from one country to the other, I think we are going to——

Senator STEVENSON. Some? Most?

Dr. COLE. Some. Most will be manufactured in this country. It will depend on the manufacturers' ability to finance and purchase the machine tools necessary to put these plants in place to do the job.

If that can be accomplished cost effectively within this country, I think it will happen. But from an expediency standpoint, and from a cost standpoint, perhaps more components will be sourced overseas than under normal conditions.

You are aware, for example, that Chrysler went to VW for 300,000 engines and drive trains per year. They now have an arrangement with Mitsubishi for engines. It's not because they want to. I'm sure that they would rather have those facilities in this country and have the profit associated with that major component. But there was no choice.

Senator STEVENSON. Finally, I chair a subcommittee with jurisdiction over technology and we have been holding hearings on automotive technology. After holding those hearings, I can't share all of your optimism about the state of U.S. technology and the CARP program. That's a minuscule program. It doesn't begin to approach the cooperative efforts of other countries.

Do you remember how much money is in CARP for fiscal year 1981?

Dr. COLE. It's just comparatively a few million dollars, but at least it's a start.

Senator STEVENSON. Well, it may be a start. Maybe we ought to start, as Senator Riegle indicated, on something altogether larger than has been suggested by anybody so far. But one of the problems we have faced is the industry.

It doesn't want to be helped by the Government. It's totally unlike the aerospace industry which soaks up all the technology it can get.

You mentioned NASA. I started, as you did, opposed to the idea of NASA as the agency for conducting this cooperative research program. I have changed, after having explored the subject, partly because NASA has been able to establish a very good relationship with industry over the years, partly because it conducts most of the automotive technology research and development being performed now, partly because the Department of Transportation has virtually no experience in research.

But no matter where the program is, the auto industry doesn't want to be helped. I don't understand that. I preside over the subcommittee which handles NASA and I note there is no reluctance on the part of the aerospace industry to accept Government involvement in research and development. It's no coincidence that those industries which benefit the most from Government support are the most competitive. The automobile industry is not, but the aerospace industry, yes.

Senator RIEGLE. Would you yield? Oh, I'm sorry, you weren't quite finished.

Senator STEVENSON. Well, I'm puzzled and troubled by this. We are trying to put together a comprehensive program for the automobile industry, and one part will be a cooperative technology effort. The EEC. I don't think you mentioned it. They recently approved a new cooperative inter-European automotive technology effort.

Foreign governments, by a multitude of means support their industries. We want to support the auto industry, but the industry doesn't seem to want the Government's support.

What are we to do in such circumstances? We can't force the industry to accept help or to cooperate in a cooperative program, if it doesn't want to. It goes along very reluctantly with CARP, mainly because CARP doesn't amount to anything.

Senator RIEGLE. Would you yield?

Senator STEVENSON. Why don't we hear from Dr. Cole?

Dr. COLE. It's a very broad and complex problem in terms of how the industry should relate itself to government in this area.

One of the objections, and I'll take the industry side just for a moment, is the tendency to not solve problems that are needed, but to deal with things such as demonstration vehicle programs which soak up an immense amount of money, without focusing on the key problems.

To use an example, the gas turbine engine. The gas turbine engine has one basic problem. It happens to be materials technology in the gasifier turbine. It is important to raise the gas temperatures in order to make it a high fuel economy engine. Research should be concentrated on the material problem rather than the building of a demonstration engine. Industry wants assistance with specialized problem solving but they resent others doing or trying to do the job the industry can do better than any other group, i.e., constructing the total system.

So there is a problem that we can think of as vectors moving through space. Government has one impression of what research and technology should be. Industry is thinking of it in a different way, and somehow we have to get these vectors so that they begin to intersect and learn how to work together. I think it's important.

Senator STEVENSON. It's not industry, it's the automotive industry.

Dr. COLE. Yes, I'm speaking of the automotive industry.

Senator STEVENSON. No one has suggested that the United States develop products. All that has been suggested is basic research. All I am suggesting, as are many others, is that this basic research go through the demonstration stage.

That is a form of Government support and involvement in research that is welcomed by other industries, including the aeronautics industry, which is delighted to have the Government carry its basic research through the demonstration, for example, of an engine.

Senator RIEGLE. Excuse me just one minute, if I may. I'd like to make just one observation to broaden this discussion a little bit, because this is a vital point, and I share some of the same concerns that Senator Stevenson has.

But I think there is a profound difference between the history as it relates to the auto industry and as it relates to the aerospace industry, and one of the main obvious differences is the fact that the defense connection with the aerospace industry has caused this in large measure. It is a semicaptive industry as it relates to national security needs in a very close and enduring government relationship, both in terms of product definition and financing.

You have a transfer of personnel back and forth, military officers into aerospace companies, and you name it, so that you've got an altogether different historic and current relationship that is the bedrock of how that has evolved, versus the situation in the auto industry.

I think in the auto industry, two things have happened:

ADVERSARY RELATIONSHIP

First of all, you had typically, I think, an undue and excessive adversary relationship between Government and the auto industry, and we could probably debate the rest of the day in terms of how you assign the shares of responsibility as to why that relationship has been more an adversarial relationship than it might have had to be, and why a lot of difficulties and problems have arisen.

But I will tell you this, and I consider myself one of the better voting-recordwise, consumer advocates in the Congress, if one can find a way to measure who is and who isn't.

But I look at, for example, Joan Claybrook's performance in the Department of Transportation, and I see a number of times where no effort is made to try to work things out in a cooperative way with industry.

I see Ralph Nader, who has very strong feelings about the auto industry, in his own way reaching through that agency of Government time and time again in ways that are counterproductive to the overall blend of interests of the country as a whole. This happens to be my own view.

But unless somebody's going to analyze that history a little more carefully, before we start making general comparisons to the aerospace industry, we've got to recognize the things that are very different in the two industries.

I would like to be able to start fresh with respect to the auto industry and I would expect the auto industry to come forward at least half way and the Government to come the other half of the way and also bring labor in order to work out an authentic harmonious cooperative partnership.

I don't think the country can afford even another day's waste of time and effort and energy to not have that. But I must say that any intransigents that I see on the industry side—and there is some of that—and part of it's buried in this history of unhappy relationships. But I also see it in the Government today. I see us get sandbagged time and time again, I saw it on the Chrysler thing right here in this committee, by agents within the Government who basically don't want to foster that kind of a climate.

So, you know, if we're going to make peace, and I think it's long overdue, and I want to see that kind of peace made, there are going to have to be adjustments on both sides, and quite frankly, we haven't found the genius to do that yet.

Dr. COLE. It's a terribly difficult job, and I think you have stated it well, Senator Riegle, and I sympathize with the problem as Senator Stevenson has stated it. It's very, very difficult, and a more harmonious relationship is absolutely necessary.

Senator STEVENSON. I am not quarreling with the history. Senator Riegle is absolutely right about the history. That's the explanation. What I'm trying to get is an answer, and I suggest that the answer is not to put Joan Claybrook's department in charge of this research.

Dr. COLE. That's fundamental to any industry involvement, that a regulatory group not be involved in basic research. But knowing the personality of many leaders of the industry, many of these people have grown up in a school of "hard knocks", and they grew up making decisions without the Government as a part of the

decisionmaking process, and they are learning, and it's a hard learning process for them, there's no question about that at all. And they still have a ways to go yet.

Senator RIEGLE. Let me just say we need to move to Ms. Keller because she has a time problem. I know you do as well. We have questions for the record, all of us, that we'd like to have you respond to, Dr. Cole, and we also have Mr. Malmgren here who is able to stay if we were to ask questions of Ms. Keller. Is that correct, or is that not correct? I don't want to trespass on your patience much longer, although I do want to have a chance to question Ms. Keller before she has to leave.

Senator Stevenson, do you have any particular questions you'd like to direct at Ms. Keller?

Senator STEVENSON. Well, I'd still like to know what Volkswagen's fleet fuel efficiency standards are going to be in 1985.

Ms. KELLER. I'm not sure that's the relevant question. The relevant question is what is the price of gasoline in 1985? Because the 70-mile-per-gallon, 80-mile-per-gallon car, by definition is going to be something that's very tiny, and as Senator Lugar and Dr. Cole indicated, and I myself will concur, we don't necessarily want that to be our primary vehicle.

Senator STEVENSON. I think you are right that we have to make some assumptions about the price of gasoline. The price of gasoline is not set by a free market. But Senator Jackson and others in the Department of Energy are good at making, these assumptions. We were making some pretty accurate assumptions up here back in 1972, but nobody would listen to them. What are your assumptions about the price of gasoline?

Ms. KELLER. We are assuming that the price of gasoline will rise at a real rate of 3 to 4 percent a year plus inflation.

Senator STEVENSON. Three percent?

Ms. KELLER. Three to four percent plus inflation.

Senator STEVENSON. That's a very optimistic assumption.

Ms. KELLER. Plus inflation.

Senator STEVENSON. Plus inflation. What's your assumption with respect to inflation?

Ms. KELLER. Something like 8 or 9 percent a year.

Senator STEVENSON. So in real terms it's about 11-12 percent a year through 1985? Assuming there will be gasoline for discretionary uses by then. You make some assumptions that there won't be interruptions of supply——

Ms. KELLER. That's right.

Senator STEVENSON [continuing]. That produce a rationing. I think that's an optimistic assumption.

In 1980 dollars, what does that mean for the price of gasoline in 1985?

THREE DOLLARS A GALLON

Ms. KELLER. Oh, it probably will be somewhere around $1.55 to $1.60 or so a gallon in real terms and about $3.00 a gallon in nominal terms.

Senator RIEGLE. Excuse me. I want to make sure everybody——

Senator STEVENSON. Approximately $3.

Ms. KELLER. Between $2.50 and $3 in nominal terms.

Senator STEVENSON. Well, we won't argue. I guess I would still consider that an optimistic assumption. But I accept it because I think it suffices to warrant another assumption, which is that the consumer is going to continue to be looking for a cost-competitive, fuel efficient vehicle by 1985. He's going to be shopping between the products of domestic and foreign producers, and as you and others have indicated, the miles per gallon is going to be a major factor. He's going to be willing to pay a premium for mileage.

That being so, why isn't the offering of the foreign producers relevant? You have nodded up to this point, but when I asked you about what they are going to be achieving, you seemed to indicate that it is not relevant.

Ms. KELLER. I didn't say that at all. I said that the price of gasoline would dictate whether the market would be as oriented toward the most efficient cars as it is today, or whether it would be broadened out to allow a larger share of our market in what will then be a smaller, though still defined as a larger, car.

Senator STEVENSON. OK. One of the facts is the disposable income of the individual.

Ms. KELLER. Yes.

Senator STEVENSON. Some of us get rather pessimistic about the condition of the consumer by 1985, too. But I apologize for interrupting you, if I did.

We are agreed at this point that the price of gasoline is going to be a major factor, because it will be high, if gasoline is available at all.

That being the case, the competing products of other countries and their fuel efficiency is not irrelevant. Isn't it relevant then to ask what those products are going to be? Do we know?

Ms. KELLER. I think it would be safe to assume that every major European manufacturer will have a car capable of offering fuel economy in the area of 55 to 60 miles per gallon by the middle of the 1980's, and I think that is a similar conclusion that can be drawn for the Japanese.

Senator STEVENSON. I'm sorry?

Ms. KELLER. By the middle of the 1980's.

Senator STEVENSON. Did you say a car?

Ms. KELLER. A car. I don't believe that it will be the fuel economy average for the fleet, for any manufacturer. I think we are talking about a single model.

I visited Volkswagen in Germany a month ago, and they were talking about their 70-mile-per-gallon car, not cars.

Senator STEVENSON. What kind of fleet averages will they have?

Ms. KELLER. That would depend upon how many of each and every model they sold.

Senator STEVENSON. And what will we be producing by 1985?

Ms. KELLER. Well, the fuel economy standard is 27½ miles per gallon, but every manufacturer has indicated that it will exceed that standard by a fairly healthy margin, and again it's going to be based upon what the mix of cars will be and the price of gasoline.

I think that General Motors is suggesting that their fuel economy—and they, by the way, will be the only manufacturer capable of offering what I would call a full line of cars, by that year—will be well above 30 miles a gallon, with some cars having fuel econ-

omy of perhaps as much as 50 miles per gallon, and others having fuel economy of as little as 24 to 25 miles per gallon.

I think we have a tendency to extrapolate the present into the future, and right now we are witnessing panic buying of small cars, not because the price of gasoline is $1 dollar a gallon, but because it got there in 12 months. Had we taken a 3- or 4-year period to get from 58 cents a gallon to $1.20 a gallon, that fact would not have been as noticeable to the consumer as in a 12-month period and the mix would have gradually shifted toward smaller cars.

I think the model mix will be shaped over the next 5-year period based upon the pattern and level of gasoline pricing as well as availability.

If we have gradual increases and an energy policy that says gasoline prices are going up 3 percent to 4 percent plus inflation each year, no matter what OPEC does, there will be a shift into efficient cars but not necessarily into the highest mileage subcompacts alone.

That would be more coincident with the manufacturer's capacity to build than it has been in the past.

Senator STEVENSON. But the production decisions for 1985 have to be made pretty soon, don't they?

Ms. KELLER. The models have to be decided upon now.

Senator STEVENSON. Those investments have to make assumptions about what the investment will produce. I keep asking these questions of the industry, and I can't get any indication at all from them. General Motors says it's going to give the consumer a choice. It wasn't until very recently that Chrysler indicated it would not go back to the production of Imperials.

We are asked to provide them with trade protection, refundable investment credits, and accelerated depreciation, without any insurance that these enormous concessions by the Government and the taxpayer will produce competitive products. All I'm trying to get is some assurance that if we go all out to help, we will help. I'm concerned by a track record that does not give me and cannot—for heaven's sake—give anybody any confidence in this industry.

BRAINWASHING THE CONSUMER

I agree it is partly the Government's fault for not educating the consumer, but it is certainly also partly the fault of the industry spending billions and billions of dollars brainwashing the consumer into buying gas-guzzling automobiles year after year after year.

Ms. KELLER. I doubt that they brainwashed the consumer between 1975 and 1978. Auto makers were themselves astonished by the demand for lightweight trucks, and were completely unable to meet the demand.

Senator RIEGLE. And vans.

Ms. KELLER. Between 1975 and 1978, we had gone through one major energy shock, but it didn't impact purchasing habits at all.

Senator STEVENSON. I don't think they were trying very hard to understand the energy crisis. They wanted to make a profit on the sale of large automobiles. They could have understood the energy situation; other countries understood it.

There were people here who understood it.

Ms. KELLER. Strangely enough, in Europe, after the energy crisis, there was no major shift in the model mix. It is only today that

there is a shift taking place to the smaller model cars, but it's only today it's happening.

Senator STEVENSON. But isn't that the point? Their cars were already smaller.

Ms. KELLER. They are smaller because they have few roads comparable to ours, distances are shorter, and gasoline has always been much more expensive. Had we had the same circumstances, I'm sure our industry would have developed the same way.

Senator RIEGLE. Would you yield at that point?

Senator STEVENSON. Every time I yield to you, I don't get the floor back. [Laughter.]

Senator RIEGLE. I assure you, you will. But this question you raised, I think, lies at the center of trying to understand what's happening and where we are and where we might be going. And I think some of the illustrations you make with respect to Europe, that you are making in terms of the configuration of their circumstances. It is even more dramatic in Japan, where you've got even smaller distances over which people can travel in cars. I was wondering, too, you know, obviously there is this huge difference in what energy costs have been. But I think there is also a question of what disposable incomes have been and how people value comfort, and I think one knows, too, even without getting the precise statistics, that if one looks at just imperative buying size in terms of both height and weight between Americans—they have a very different diet, and have for years, versus Japanese. It's not just true of those countries, it's true of a lot of countries. I was reading the other day how Scandinavians got smaller over a period of time because of the introduction of herring into their diet.

But all of these things bear on the question of why people had developed certain buying patterns. It's not hard for me to see why in the United States when gas was well less than $1 a gallon, you could jump in a car and whether you were Jack Kerouac or somebody else, and sail across to California and go through the national parks on the way. There was a tremendous inducement to do that.

I mean it was a terrific value, and people took advantage of it. And we have even heard one very thoughtful member of this committee today say that he's still not ready to surrender his choice for at least one of maybe two cars, the station wagon, because of particular needs he sees versus economic tradeoff.

So I don't know that we can oversimplify it. I think there is a danger if we do, because I think it leads us to the notion that maybe there is a kind of answer that I think is not there. I mean that our answer has to come back around to very complex strategy that matches a very complex problem, and I thank my colleague for yielding.

Senator STEVENSON. Well, I don't want to waste time arguing. The point is simply that we tend to look backward and take snapshots of the market as of a given moment. We rarely look into the future, and when we do, it is with very little vision.

I think other countries have been much more perceptive. I suggest that we try to look into the future now. It is not unreasonable for us to hear something of the industry's plans before we make large concessions and provide support. And so far we are not

getting that. We are getting more information from Volkswagen than from domestic producers.

FUTURE ENERGY POLICY

Ms. KELLER. I think it is going to be important for you, the Congress, to give some sign to the industry as to what future energy policy is in this country. As an analyst, I remember that from 1974 to 1978 I discussed their assumptions about gasoline pricing and availability.

By 1975, I stopped publishing a chart on gasoline pricing in my analysis of factors impairing auto sales because it was a flat line, and therefore not a factor in altering buying decisions. When one questioned the auto companies about their assumptions on gasoline pricing, the response was that it is politically unacceptable in this country for the price of gasoline to rise to world market levels. Energy policy supported that conclusion and determined product development and sales.

Product development was also determined by fuel economy standards and that was insufficient in view of current gasoline prices, If gasoline prices will be pushed up to world levels, the rules of the game have been changed, and Detroit should be informed.

Senator STEVENSON. Well, I can't be any more optimistic about the Government, either.

One question:

How would you feel about linking extra accelerated depreciation and refundable investment credits beyond what industry gets generally? What about trying to use tax incentives as a means of not only helping, but also encouraging the industry to tool up for the production of fuel efficient automobiles?

I can't be much more precise about that. I don't know how you would——

Ms. KELLER. Those are very interesting concepts. I think that specific impact on each company as a result of any or all of these programs would have to be considered carefully. They certainly are interesting concepts and I think, worthwhile pursuing.

Senator STEVENSON. Thank you.

Senator RIEGLE. If I may, I'd like to just pick right up on that point, because I think probably, Senator Stevenson, you and I would be pretty much in agreement on this. I think at this point, in terms of the kind of extraordinary initiatives that are needed to help the industry, that there has to be a quid pro quo, and I wouldn't suggest that money just be shoveled out the door without a corresponding agreement, at least on general goals.

In other words, goals should be established. What I am concerned about is I think there should be a kind of compact between industry and Government on an emergency basis to see that certain assistance is provided in exchange for a commitment to certain specific goals.

The line I would hope we would not cross is the Government going beyond the working out of the agreed-to goals into saying now this is the way we want you to meet the goal, because then I think you run into the problem where the Government engineer or the Government administrator or the Government person in the bureaucracy wants to second-guess how it ought to be done. And

the inevitability of conflict there is so great that it takes only a gram of wisdom to decide to avoid that problem, and to thrash it out at the goal level.

And once that's set, and I think everybody should be at the table, I think the Government needs to be at the table, the heads of industry, and the UAW, because, you know, how workers feel and how they perform and their part in this is integral to the success. And that's what is needed now.

Now, you know, no one can convene that meeting other than the President of the United States. I mean it's the nature of our system that that's where that kind of an effort really has to be initiated and carried forward.

We have made some progress. There was a meeting here recently of 20 Senators with the heads of the companies and the UAW, followed up then by a meeting that the President himself held with the same group, and a task force has been put to work.

Now, what that will produce remains to be seen. It's underway, it's headed by the Department of Transportation.

But I would fully agree that we ought to have a situation here where if we're going to have a crash program, that's designed to meet certain national objectives, and it involves a partnership between the private sector and the public sector, we have to develop the mechanisms by which this can be done without this being a situation where we are in either direct conflict with one another, or we organize it in a way where it can't succeed. And so that's the point that we're at today.

Now I happen to think, having lived with this problem for a long time and talked about it with people from all over the place, I think the public is ready for this. I think the public understands that we've got a problem here that requires an extraordinary combination and a partnership to work our way out of this dilemma, and that that really is the thrust of the auto resolution that we'll be voting on at 1:30 today. It sets up a policy framework that aims everybody right toward that conclusion.

Now, implementing it is going to take some leadership skill, genius, and commitment that so far has not been forthcoming, at least on the administrative side of Government, but one hopes and trusts that we will see that forthcoming, because it's vital.

Senator Stevenson just indicated that he had to leave for the vote that just started, and I know, Ms. Keller, that you must leave, but let me just ask you one question before you do, and then we go to our last witness here.

And that is you emphasize the need for domestic firms to improve their cost structures, and I would agree with that, and I'm just wondering what your thoughts are as to the best ways to assist the firms to do this.

IMPROVING COST STRUCTURES

Ms. KELLER. I've mentioned a number of them. They have been mentioned by other witnesses as well. Obviously if you can generate more money internally, you don't have to borrow as much and thereby can control what could be a monumental increase in interest expense. Facilities modernization will help to control variable costs—particularly labor costs.

Any mechanism by which the internal generation of capital improves cash flow would benefit the industry including accelerated depreciation, tax credits for model tooling, et cetera, any of those things.

The industry's own ability to obtain needed capital varies by company. I am fairly well convinced that General Motors will. It is quite obvious from what this company has done in the last 2 months that it will be the low-cost producer in the United States. It has, in a recession, actually increased its capital spending budget, whereas Ford has had to cut theirs. General Motors, by 1985, will have state-of-the-art production capability, using robotics to the same extent as the Japanese.

I am not sure that that statement would be as true for the others.

Senator RIEGLE [presiding]. When you look at the case of Ford, where their debt equity ratio in 1978 was 11.8 percent, and is projected in 1983 to be 38.3 percent, how does that strike you as an analyst, and what do you infer from that?

Ms. KELLER. I think that the market has already assessed Ford's dilemma. My personal opinion now, as far as the stock is concerned, is that it is not an attractive investment. The company has little dividend-paying capability because of the need to borrow that much capital, and therefore is an unattractive investment.

As far as the bond markets are concerned, Ford, early this year, was considered a triple A company. Its rating was then reduced to double A. It is now selling in the market, as a weak single A. So the markets have reflected the deterioration at Ford.

I think the capital funding requirements of Ford are its greatest problem, and are being viewed as such by the investment community. And even with greater debt Ford will fall further behind GM over the next 5 years. Since investors have to be compensated for risk, it will be more expensive for Ford to borrow than GM. Ford will have to pay a higher interest rate to get that money. And will be in competition with General Motors for the same pool of money. It will be less attractive under all of these circumstances.

There are mechanisms used by other countries where interest expenses are rebated or some part of the burden of R. & D. is assumed. All of those things will help the industry. My concern with any assistance program would be that it does not proportionately favor one company versus another.

Senator RIEGLE. Well, I strongly agree with that, and as a matter of fact, the approach we have been following here in the Senate has been to try to be evenhanded in the response. We had the Chrysler loan guarantee package which is tailored to the specific needs of that case, but also if you look at the auto legislation that we have moved through the Commerce Committee, on which I serve, you will see that we have tried to take steps that deal with Ford's problems in a way that we can deal with those, and Volkswagen of America's and the way we can deal with those, and American Motors and so forth.

So I think that is essential, to keep that diversity in that blend and to try to keep all the parts of the industry alive and healthy.

Ms. KELLER. The irony is that Ford becomes the auto company that borrows at the highest cost now, because Chrysler is essential-

ly going to be funded with Government-guaranteed loans, and thereby paying a lower interest rate than even Ford.

Senator RIEGLE. Well, I grant that. On the other hand, you know, you have working for Ford the fact that they have got a foothold in the foreign market, which is a cash generator for them, that is not available at this point to Chrysler.

But I guess the conclusion that one still ought to draw from this is that we're at a point now where it's important that the leadership, the public leadership in our country, namely the President has to initiate a consortium effort where we get the principals that we've been talking about around the table and to work through a strategy that does have this kind of equity in it, and is sensible and workable, that looks out, say, through 1985, where we agree on a course of action that we can carry out, that helps the country get through this difficulty.

You talk about Ford's rating dropping. There was a story in The New York Times a couple of days ago about how the same thing now has happened to the State of Michigan. The seventh largest State has gone from a double A rating to a single A rating because of the tremendous financial difficulties we are experiencing, essentially because the sickness in this industry that we are talking about has gone unattended for the most part in terms of any kind of sensible public policy.

And here we see the Japanese Government very much on top of this problem in terms of that kind of equivalent consortium effort, and the German Government investing literally millions of dollars in Volkswagen to help them maintain a state-of-the-art position, and we are way behind. And this is one of the reasons why I've been trying to push the whole effort forward and to elevate the consciousness level so that we finally bring about enough understanding at one time so that we get action.

We are still not quite there. I wish I could say that we were, but at least today, in an hour's time where you are going to see the Senate go on record in behalf of a very strong statement, and putting the Senate on record as calling for a policy framework that will give us this answer that we are all saying here that we need to have.

Let me make this suggestion. Those were the second bells on the vote. I know you must leave, or at least that was the message that I had. We have one witness yet to hear from, and both of you to question. I am prepared to stay as long as you can stay.

What I'd like to suggest—Senator Stevenson should be back momentarily—is that we put the committee in recess for 5 or 10 minutes, while I go and vote. I'll come right back and then we'll go to our last witness whose patience is going down in the history of this committee as being among the greatest, and we are very anxious to hear from him in terms of what ought to be done on the import issue.

So we'll be back very shortly.

[Recess.]

Senator STEVENSON [presiding]. The meeting will come to order.

I apologize, Mr. Malmgren, for this long delay, and I thank you for your patience. The next time you will know to tell us you have a plane to catch. Please proceed. If you would like to summarize

the statement, we will be happy to enter the full statement in the record.

STATEMENT OF HARALD MALMGREN, FORMER DEPUTY SPECIAL REPRESENTATIVE FOR TRADE NEGOTIATIONS

Dr. MALMGREN. Thank you, Mr. Chairman. I am honored that you and Senator Riegle asked for my opinions on the present predicament of the American automotive industry.

I am going to cover, as you suggest, in general terms what I have to say, first about the legal situation what is possible under the law that Congress has written about imports; second, the international context; third, the question of foreign investment; and then finally I want to come back to some things you've been saying, as well as Senator Riegle, about the nature of the problem.

As you know, Mr. Douglas Fraser, one of our outstanding labor leaders, has been calling for a number of actions, no one specific action.

Among these, he has asked that the flow of exports from Japan be moderated, and that there be Japanese investment in production facilities in the United States and the administration has tried to meet some of those demands with a series of actions.

They have encouraged investment in the United States, and they have sought to have the Japanese acquire more parts in the United States, and also to liberalize the market in Japan for exports to Japan.

Now on the latter two points there is some progress. The Japanese have in fact agreed to a recent package of liberalization which puts them pretty close to comparable situation in terms of access to their market.

Senator STEVENSON. Excuse me. A comparable situation?

Dr. MALMGREN. To many other markets, including the United States. I'll come back to what I mean by comparable, because it's a little complicated.

The Japanese will send a team here to look at the parts purchasing business very soon.

But what the administration has not done is talk about export restrictions. Now there is a reason for this, and it's not just obtuseness or stubborness, there really is a reason and it lies in Congress, not in the executive. I think this is something that has not been discussed up here very fully.

ANTITRUST POLICY

It primarily relates to antitrust policy. The Japanese Government, as it appears to me, and perhaps even the major Japanese automative producers, seem at this time to be willing to consider export limitations. But the U.S. Government is unwilling to discuss them.

I am told that when this idea has come up between the two governments, American officials have said that they cannot discuss any form of trade restraint. They can neither encourage nor discourage, is the quotation I've been given, regarding any line of thinking of this sort.

Now behind this wall of silence, I gather further, is that a number of warnings from the Department of Justice have been

made in writing and by phone to various other officials in the U. S. Government, that any discussion by any U.S. official or private party which might lead to limitation of exports to the United States could constitute a violation of the antitrust competition laws.

To be present, even, at such a discussion could be a violation. Obviously that is a strong deterrent to any official who is interested in this issue.

Moreover, unilateral action by Japanese manufacturers themselves to curtail their U.S. sales could also run afoul of our competition laws.

Now this is not an entirely new problem. As you know, I was involved in some trade policy matters over several administrations, and I recall, although I was not involved in it in the 1960's, that officials of the State Department tried to arrange a voluntary export arrangement with Japan on steel, and they were soon afterward accused of conspiring to restrain trade in the courts, and after a series of court actions, the Congress in the 1974 Trade Act, which I was involved in drafting, had to write a special provision into the law retroactively letting off the officials from that conspiracy charge.

Now if you take this situation and you add to it in the mid-1970's, in the 1975, 1976, 1977 period, Japanese steel companies, European steel companies, Japanese and European governments, all said that they would like to negotiate an orderly marketing agreement with the United States to restrain steel exports to the United States, and the U.S. Government said we cannot discuss any such arrangement. We will not be party to one, we will not listen to one.

Now, it's small wonder, then, that the administration is unable to deal with the question of restraining Japanese exports voluntarily or otherwise. It is not an easy matter for Japanese producers to consider, either.

As for the Japanese Government, it is my opinion—I am not a lawyer, but I am often preaching to lawyers—it is conceivable that the Japanese Government has some powers, but even then it would be hard for that Government to decide how to act without knowing what the U.S. Government thought was reasonable, and the U.S. Government cannot discuss it.

Now there's a long history behind this, between Congress and the executive branch. As you well know—and I dislike lecturing the Congress about this, it's just that this drafting problem seems to keep coming up—the U.S. Constitution reserves to Congress the power to regulate foreign commerce. The President does not have any powers in this field.

Therefore, the President can act only if the Congress grants him specific authority to act. On many occasions in recent decades, I remember back to the late 1950's as well as the 1960's and 1970's, there have been bills before Congress which would have granted to the President discretionary power to negotiate or otherwise implement import restrictions, when imports were threatening to disrupt or imperil domestic producers. But the Congress itself chose not to grant such discretionary powers to the President, explicitly declined to offer those powers, and instead the trade laws have

been rewritten and rewritten and become so complex that only lawyers can handle them, and the laws very narrowly allow discretion under certain conditions.

So when outsiders are asking the Government to do something about the export levels, the answer is nothing can be done without a change in antitrust policy or a change in the trade law or else someone has to follow these specific procedures under the law.

Now even the President can't break this law. The President put on an import surcharge in August 1971, and the court struck it down, saying he didn't have that power. It's nowhere in the law that he could do this. So it's a very difficult field, and one has to remember that the antitrust people look at the trade law as exceptions to the antitrust law, and therefore only those exceptions specifically defined are allowed. Everything else is a violation of antitrust laws.

Indeed, anything else is a conspiracy to restrain trade. Anything. Even in this use of the trade laws, there have been speeches by antitrust officials recently saying that if you bring a capricious case, that it could be construed as conspiracy to restrain trade. It is a very strict situation at this time.

Now, what does the trade law allow? Well, Professor Baldwin already touched on that. I don't want to review everything. It allows a number of channels through which one can go to get import relief. I have listed some of them. I omitted one. He referred to section 301 of the Trade Act of 1974 and 1979, and that has to do with situations when somebody else who is unfair to you, you can retaliate by restricting imports into the United States.

But the trouble there is that it's hard to find something that you can call really unfair to you in other markets any more, particularly inasmuch as the Japanese have now liberalized quite a few of the remaining impediments on the nontariff front.

So it is difficult to make a case that's compelling.

Now there are three avenues that are relevant to the auto industry:

One is possible antidumping action, but that was looked at 3 or 4 years ago and it was found that dumping charges could not be substantiated except in one or two cases, and in those cases there were price adjustments from foreign manufacturers, but not Japanese. They were from European sources, as I remember them.

COUNTERVAILING DUTY ACTION

Another possibility is to attack foreign government subsidies through countervailing duty action. The problem there is that there are subsidies to foreign producers in some countries, but not Germany and Japan. There are subsidies that one way or another come through indirectly, for example, the British motor car manufacturers who are being salvaged daily from a disastrous situation.

Indeed, some of our own producers benefit from those subsidies abroad, particularly Ford Motors, and it would be difficult to attack them without attacking ourselves, so to speak.

That leaves really only one avenue left, and the United Auto Workers have chosen to take that avenue under section 201, or the escape clause of the Trade Act, and frankly I believe that was the proper course for them to turn to.

Now that particular avenue has, if I can comment on it in general terms without being a lawyer about it, first of all, the case was filed June 12, so that means that nothing can be expected or nothing is likely to come out of the International Trade Commission, as they have to look at the question of injury, until around December 10 or 12, after the election.

And then the President has, if they find injury, about 60 days or less, if he likes, to decide to do something following their recommendations, or something else, if he likes. But you're talking about February.

So now the question is, Is there anything that can be done in the interim?

Well, legally, no.

Senator Riegle, I was just touching on this point earlier, because I know you have been concerned about perhaps there was some way to restrain imports on a voluntary basis, and I explained that the Antitrust Division of the Justice Department has given the word out to all parties concerned that any such discussion, to be present in one, even, is conspiracy to restrain trade.

Senator RIEGLE. Now discussion by anybody?

Dr. MALMGREN. Anybody. Government official, private person, anybody. Congressman. Anybody. Union official. So the problem is in the law, and it's a law that Congress wrote, so it's a very difficult problem.

Senator STEVENSON. You've put the fear of God into Senator Riegle. I think he expects to be indicted. [Laughter.]

Dr. MALMGREN. I'm not a lawyer.

Senator RIEGLE. It may well be—nor am I. It may well be that the Justice Department has put that word out. I don't know that that necessarily means they are correct in their assessment, whether in fact that may not be a mistaken policy that they are pursuing.

Dr. MALMGREN. There are questions I have about it, but we can come to those afterward, but because our experience has not always been quite so sharply defined in the law, and in the administrations I have served, we didn't have quite this hostility between Justice and others.

But it is there, and I am not so much worried about Congressmen or Senators in that regard, although if you try to negotiate yourself, you've got another problem with the Constitution as regards Presidential powers for negotiation.

But, needless to say, anyway, we have this escape clause case now and the only thing that could be done to speed that up is that the Congress could ask the ITC to expedite the case. Probably the ITC would respond, but then they might not be so serious about the investigation, either, so it's a little bit a question of gambling, whether you really want them to go faster. But they could. Under the law they can step up the pace.

Now the question is then whether they will determine that imports are a substantial cause of serious injury. That we'll see.

Now this escape clause approach is different from antidumping and countervailing duty in the following manner internationally:

If you can show antidumping action is appropriate, or that there are subsidies, then you don't have to pay anybody any compensa-

tion, you just take action, because these are unfair trade practices under the GATT.

But the escape clause is different. It was designed for situations when government thought they had a basic industrial problem and an unemployment problem, and some period of time would get them past the difficulty. Then you could ask or you could take action, let's say, to raise tariffs and impose quotas for a period of time, because of that fundamental finding that there was serious injury, and the only hitch to this is you have to pay for it. Why? Because whatever your tariffs are, they are the result of years of negotiation, and somebody else paid for those tariff concessions with concessions in other industries.

We might have lowered auto restrictions in exchange for chemicals or for steel or for tractors or something else. Somebody paid for them, and those concessions are what we call bound. So if you want to lift them, you may under the GATT, provided you can show injury, but you have to pay compensation, or you have to allow somebody else to retaliate against you by an amount of trade coverage roughly equivalent. We are talking about $15 to $20 billion in trade.

So, in a way, if somebody wanted to play hard ball here, they could put the United States in that situation, that other U.S. workers and industries would conceivably either suffer greater import pressure than they would have expected otherwise, or lose export opportunities. And it's a big scale. We've never had a case this big, and the ITC's never faced anything like this.

The trade law never was tested in this way.

Senator RIEGLE. Could I just ask a question on that, just a technical question, and that is when the trade problem in cars and trucks here is essentially a Japanese problem insofar as the Americans are concerned, would it be only the Japanese that would be entitled to find the offset items, or might others?

In other words——

Dr. MALMGREN. The problem is this, that under the GATT you can take such an action as I was describing, but you cannot take it against Japan. You can't pick a country and say I'll take it against you. You have to take it against everybody. So Germany——

Senator RIEGLE. But wouldn't it be a way to define the initiative in such a way that it hits a country that penetrates beyond a certain percentage?

Dr. MALMGREN. You can hit the sector in which the major damage is done to a party by some ingenious drafting of the remedy. You know, you can classify and subclassify. There are ways to do these things. Sometimes we say we can't, but usually we find a way if it's necessary.

Dr. BALDWIN. We did that in the so-called chicken war.

Dr. MALMGREN. We separated out Spanish brandy from French brandy by categories. Ingenuity allows these things. But then there is an out, and that is that it is conceivable in such a case that rather than face all of that trouble back and forth, it might be that the President could say, all right, I'll negotiate a voluntary export restraint agreement, and the law does allow him to do it if all this process has been followed, but only then. If injury is found, and if the ITC has recommended action, then he can do what they recom-

mend, or he can go ahead and negotiate a voluntary agreement, if he likes. He's got flexibility at that point, that's where Justice backs off and says OK now you can do it. If you wish.

There is one other case, and that is if you can prove subsidization, and you have a countervailing duty case, the law specifically allows also an OMA in that particular instance because, as I said, we're not going to hit Germany and Japan with that particular law. You're going to hit the United Kingdom and perhaps Canada and others. Korea. Which doesn't have direct impact on the United States at this time.

Now the question is if Japan were focused on, then there would be an important issue. Because the GATT is nondiscriminatory, Japan would have to acquiesce and say, OK, you don't have to hit the Europeans, just we will restrain.

Now they might not want to do that because that gives the Europeans a free ride. So they might say we'll do it if they do it, too. It could happen. It's a negotiating situation.

The Europeans are not going to be very sympathetic to any pressure on them. In fact, my impression, I just came back from Brussels 2 days ago, is that they're ready to lock teeth on this issue on any American arm that tries to reach them, and as you well know, political relations with Europe are frayed already pretty badly, so it's not a good time to have another tension in an area with such big employment consequences.

So the escape clause avenue may have been the best route for the industry and for the unions, given our present law, given what the law allows, but it leaves many big questions to be resolved early next year, and I don't envy the person who has to negotiate this.

DOMESTIC CONTENT LEGISLATION

Now are there other remedies? Some people in Congress have proposed domestic content legislation on the grounds that this is done by other countries. It is true that many countries have domestic content legislation. However, it is not true that this is in operation in any other home markets that are major exporters to the United States. It's in the other countries, developing countries, primarily, but not in Japan, not in Germany, France, Italy, the United Kingdom.

In other words, not in our major trading partners in autos. So if you hit on domestic content, you're hitting people who are not relevant to the import problem, and you're going to hit people who are going to get very angry about it.

There are special import restrictions in other nations that I don't need to catalog here, but it has been done elsewhere. For example, in the brief submitted by the United Auto Workers to the International Trade Commission. There's a very good catalog in the back of it that somebody can easily put in the record here. It's a publicly available document.

There are restrictions, particularly in developing countries. And I want to point out that these countries feel they have not benefited greatly from past negotiations. Therefore, they don't like to liberalize their own restrictions. And sometimes that's very frustrating to the United States. Indeed, I have tried to persuade

developing country governments to change some of these policies when I have been serving various administrations, and had ill luck.

But one has to remember, before we get too excited that the principal growth market not only for exports of U.S. food but for many capital goods and engineering and construction services, are these countries. In other words, we have a favorable balance of trade by far with most of them. So to get nasty with them is not necessarily going to help our farmers and our capital goods industry. It's an unbalanced situation.

Now let me turn now to the question of foreign investment. We're asking the foreign companies, particularly the Japanese, to invest here. Now it is true that there have been official pressures on U.S. companies to produce abroad and threats that they would suffer impeded access if they didn't, in earlier years particularly. And indeed, there have been many official incentives to get our people to go abroad, or even across the border to the north, to go to Ontario, as you well know.

So these issues of incentives and penalties are around, no question. And so our multinational enterprises may have gone a little further overseas than they would otherwise have done, who knows.

But many of our union leaders, particularly the AFL–CIO itself has argued bitterly against this, saying that the march abroad because of policy in other nations was a bad thing for American labor.

Now, if we ask the Japanese and others to come here as good corporate citizens, that's going to cut both ways. That will encourage other governments to do more of the same, and the march abroad will be greater in some other industries.

It's a very tricky problem, that one. I don't know how I would approach, let's say, Mr. Kirkland and explain what I wanted to do about that, because it does cut both ways. A very difficult problem.

Now, I think business judgment regarding foreign investment should include what I would call the good corporate citizenship role. And it is surprising to me that Japanese producers have not weighed that factor more heavily in their attitude toward the U.S. market.

On the other hand, the economic factors have to be reasonably favorable. Now, if I am outside looking into the United States—and I think this reflects the thinking abroad, if I have it right talking to people in different industries, in different companies in this industry—what cannot readily be seen is, what is the structure of the U.S. industry in the world context in 3 or 4 years or in 5 or 10 years, the question that Senator Stevenson was asking: Where are we going?

If the world car concept develops, then components will be produced at various points in the world, and we're not sure where those points will be. But assembly will be market related. We know that enormous capital requirements, as discussed this morning, are involved; and that smaller producers are not going to survive, basically. We know that almost certainly there will be a consolidation of the world industry into fewer producers.

It's a big question mark in my mind. Ms. Keller led to that. There's a big question mark in my mind whether we will have

more than one producer in the United States. It's very unclear that more than one can survive.

The question then will be how many producers in the world, and what will the competition be among them. If we bring the foreign producers in here, it may be that the second company or the third company is not a U.S. company; it may be a foreign-owned company.

Senator RIEGLE. Incidentally, I might just say in passing that, you know, then in terms of being hemmed in by the law, then we get hemmed in by a different law.

Dr. MALMGREN. That's right.

Senator RIEGLE. Because then the antitrust law——

Dr. MALMGREN. Exactly. You're coming to the very point I was making.

Senator RIEGLE. Somebody may bring an action to break up the remaining company.

Dr. MALMGREN. You're coming to the very point I was going to make, that—in fact, in my statement I say that our Justice Department might hardly recognize such a world, and indeed, they'll probably try to break it up.

So we run again into the problem of competition policy. We can't do it on the import side, and now we run smack into it with the natural evolution of the industry.

Now, it is clear that to get efficiency up and to go to robotization and all that with componentry from around the world, that you're going to need a lot of capital, a world network; and not too many companies are going to be able to survive within that framework.

If we look at basically the problems of the industry, they far transcend the import problems. It seems to me, if I can go beyond this and if I were looking at it as an outsider, I would say the Chrysler legislation, amongst other things, called for a major look at the whole industry: Where are we going? There was mandated to the President a major reassessment.

I have the impression—I don't always know everything that's going on in the administration, but I have the impression, let's say, that the current draft or at least the first phase of that study focuses on imports and hardly anything else. In other words, it's myopic.

I worry that it may continue on that basis. And in my view, it means that probably, if you want a real good long-range view, it's going to have to be done in the Congress, because I don't think, given the bureaucratic turf problems, the problems of those who want to control energy policy, those who have the antitrust considerations, those who have the trade policy concerns, those who don't want to fool around with tax policy, and especially they don't want to have special tax incentives for a particular industry, and so forth, that you'll never cut through all of that thicket.

You're going to have to rise above it somehow, either through a Presidential commission or a congressional inquiry or a joint inquiry—that's been done before—between the President and the Congress will be necessary. And probably it cannot be done within the system. It's something quite independent, probably a commission of some kind.

Senator RIEGLE. Do you have—can you recall one that would be the joint?

Dr. MALMGREN. I know of one, but I can't remember at the moment the one that I was thinking of. It would be—I can remember two or three, indeed, in the Johnson-Nixon period, and if you'd like I can tell the staff later on, give you some examples.

The foreign companies have to weigh these factors, though: What is the structure of industry, what will antitrust do about it, what will be the capital market's reaction to the situation, and so forth; what will be our trade policies.

In the meantime, I believe you'll get some relief because the yen is going up. And it's to me a little overdue. I believe the yen will settle in at quite a higher range than it was, say, a few months ago. That's going to ease that competitive differential, at least near term, not a lot, but a little bit. And this just in theory will ease the tension, not necessarily in the sense of turning around the Japanese impact on the market, but easing at least that argument raised by some of the companies that that's been bothering them, the exchange rate.

RECESSION

But if we look forward, we also have a new factor, the recession. There is optimism coming out of the administration again this morning and yesterday. What I see is a collapse of the automobile market. But behind that I see a collapse of the steel market that is actually deeper already. And I think that we'll see in the steel business the closing of plants—whole plants, not just furnaces—very soon on a fairly large scale.

I think we have a lot of other problems going into the recession, and they're primarily related to capital spending inadequacies of previous years. For 10 years we have not been getting our industrial structure changed. We haven't been meeting energy problems because we haven't been spending money. Our productivity's going down.

Now, if we come into the 1980's and we have this massive capital need for the whole country, all industries, autos is going to be competing against all these other sectors and against the need to change over in energy in every area. The capital needs are just mind boggling in all the different sectors, if you put them together.

Now, some people will win and some people will lose in that race. I'm not worried about GM in that race. But I sure worry about anybody else. That's why I think, you see, that there is a real problem of survival here.

In a capital market that has mind boggling capital requirements everywhere you look, not just in automobiles—steel is the best example I can give you. I mean, there it's mind-boggling; same problem.

Senator RIEGLE. And these two are connected.

Dr. MALMGREN. They're very interconnected.

If we reach out and bang the door on imports, it's very difficult, because frankly the problems in Europe in industrial structure are probably worse than they are in the United States. In steel, nonferrous metals, chemicals, textiles, the basic industries, Europe is probably in deeper trouble to start the recession with.

So if we start taking, let's say, arbitrary action without thinking it through, we're going to have quite a hassle with people that we didn't necessarily intend to have a hassle with. And at this particular time, when we have other political problems, I find that somewhat awesome.

In my view, if we did have a strategic concept of where we're going, and if the Congress had some sense of direction, and if instead of blaming somebody for not restraining imports voluntarily we really looked at the law to see what we can do, if there was a rational approach to this and a thoughtful one that covered all the different issues, not just trade, my guess is the foreign producers would, within that context, be reasonable.

You know, they would also have a longer view, and they probably would show a lot more forebearance in their policies. And my guess would be that they would be more involved in the U.S. market, because it would look more steady to them.

Right now it looks like a market rules by bureaucratic war in Washington, rather than coherence and clarity in policy.

Senator RIEGLE. Could I just interrupt you?

Dr. MALMGREN. That's really all I have to say.

Senator RIEGLE. One other observation at this point, and that is that if you look—on the Budget Committee we got into the question of comparative defense spending by major industrial nations, and last year's data shows the United States spending roughly $530 per capita on defense, and scaling down through the major allies to Japan spending about $89 per capita on defense.

And that—I don't see any way to disconnect those defense spending differentials in terms of where the capital is going from facing these basic industrial questions and industrial gaps between the nations, especially as it manifests itself on this trade deficit.

We're going to have over a $10 billion deficit with Japan in cars and trucks this year, as you know. And it just seems to me that we have to look at all of these things in context. And I just don't know how we are going to be able to continue to operate beyond our financial capacity, which I think we've been attempting to do here. I mean, the tax laws and inflation and other things have had an enormous bearing on it in terms of inadequate savings and inadequate investment and so forth.

But in terms of how one comes forward to the kind of new circumstance where we need to get, I don't know how, for example, we can avoid dealing with defense spending differentials in the context of these overall financial requirements.

Dr. MALMGREN. Well, you're touching on broader issues with which I basically agree in terms of your approach. I'm not sure—we could argue a little bit about the substance, but I know Senator Stevenson has for a time tried to get a handle on this through the International Finance Subcommittee, of this question and all the relationships between what happened on the trade front, the capital spending area, what are some ways in which there can be interaction with the export trading bill that he's got coming through as an innovative way of getting at some of the problems.

We do not seem to be able to harness ourselves when it comes to dealing with economic issues. Our policy on the yen has nothing to do with our policy on autos. And it should have some relationship.

The trade issues rarely are connected with the financial issues. People don't talk to each other that much except up here in Congress.

But in the bureaucracy, Treasury goes its way and the Trade Office goes another way. And this is the same in other capitals. So you get a lot of disconnections.

The economic role that Japan plays in aid and other areas could be stepped up. If we don't want them to spend so much in the military area, then we could easily ask that they play a bigger international role in other respects, so that the overall burden of the Western system, let's say, was equal. But we don't think that way. We don't reach beyond—we just keep chasing our tail around. And I think this does affect the capital market situation in various countries, such as Japan.

INDUSTRIAL POLICY

But we have also no connection made in our minds between the domestic problems and the international. Now you've been, both of you have been talking about what I would call the need for an industrial policy. The United States doesn't think that way normally, let's say, thinking of the 1970's. And I think it's coming, and I think you're at the forefront of it.

But it is old thinking in Europe and Japan. It is—you know, if we have a problem in an industry let's look at all aspects of that policy, that problem. And tax policy and environmental policy, standards policy, regulatory policy, distribution policy, marketing policy, competition policy, everything is all one connected whole. And logically it is.

But we don't think that way. And indeed, companies have discouraged it, because they often come in and they say: Just give me import protection this week, and then I'll work with that. And then the next week they say: Give me a financial guarantee and I'll work with that.

Now, conversely, if you do engage in industrial policy, there is one consequence that has to be thought through, and that is that it won't work without management—if you help an industry that's having problems without any oversight, the problems will continue, because the people who got into the problems in the first place are still there.

So you're going to have to have oversight. To me it's always been a matter of a deal. If you come to the Government and you want some help, then the Government should work with the industry concerned in all its aspects. But conversely, there should be an oversight role: Where are you going in the next 5 years? How are you going to use this assistance? What's your sense of direction?

Now that's what I call strategic planning. This industry has been weak on strategic planning. The Government in its response has been weak on strategic planning. It hasn't given any broad approach to this.

And I think the line of thinking you're pursuing makes a lot of sense, whether or not the industry wants it, whether or not Government can quite get itself together in the executive branch. And that's why I think that really a long-range view of where we're going and what the structure of this industry looks like and what

that means for antitrust and so forth, I think that really has to be looked at.

Senator RIEGLE. Well, you know, just with respect to the Chrysler loan guarantee package, which was largely crafted in this committee—and Senator Stevenson and I came out on different sides of that issue, although not necessarily with entirely different points of view.

But that is a sort of a micro-case where there has been an effort, albeit not perfect, to try to craft a device to provide the oversight, to set up a third party in the instance of the Loan Guarantee Board, to require certain structural changes going in as a precondition—changing the labor contract, the employee stock ownership plan, certain other things that are new devices.

And whether they will work or not, time will tell. But at least it seems to me we have sort of the first working model of an effort to try to orchestrate the transition.

And in this instance, too, it met the other test that you just required; that is, that there was a new management that was brought into Chrysler. Whether it will prove to be sufficient or not, again, time will tell. But at least there was that discontinuity as well in terms of it.

But obviously, watching the Loan Guarantee Board interact on this situation has brought about modifications in the plan, the operating plan, the one that Senator Stevenson mentioned earlier. So in effect, we are starting to pioneer at least the beginnings of this kind of machinery, at least in this instance.

But to suggest that that's enough is wrong. I mean this was strictly an emergency response. It got us over a near-term situation, and I think probably gave us a very good chance to bring this company through to a different plateau from which you have a series of options as to where it might go from there.

But in terms of the industry as a whole and how we get to an industrial policy and strategy, that debate really hasn't started in earnest as yet. And you know, I grieve about that.

And one of the things that pains me is that Senator Stevenson will be leaving the Senate at the end of this term, which is a loss that the Senate and the country can't really afford. But I think his efforts to try to focus this question and give leadership to it have really been about certainly more than half the effort in the Senate as a whole.

Dr. MALMGREN. On that point, if I may——

Senator RIEGLE. But also to strike the ominous note that we're going to have to get some more folks in this act, starting with the President, quite quickly or we're going to be in worse trouble.

Dr. MALMGREN. Let me comment on both of those points. Senator Stevenson—I've been an admirer of his for many years, and I was sorry to hear that he was going to leave the Senate, because he had been what I would call one of the innovators in dealing with the world out there and connecting it up with the U.S. economy.

And there are a lot of things that he's done in recent years, including the International Bank Reform Act and this Export Trading Company Act, which perhaps could have gone further along the lines that he wanted—it didn't quite get there, but it's

going well. I think we're going to miss that, and in the 1980's we're going to need this kind of debate.

Now, the administration and the President, I think take the traditionalist approach, which has its long history to it. But this came up in the case of steel in 1978. I was not in the administration at that time, but I was, let's say, following the issue.

And the penultimate draft of proposals to assist the steel industry prepared by the Treasury Department to the President suggested that it was not possible to just attack imports; one would have to, side by side with that, do something about capital cost recovery allowances, some concept in the environmental field that would give some ease of movement, and a few other administrative action areas that could be made, flexed up, let's say. It's my impression that all of those things were taken out in the White House and they said: Give us a clean final draft with none of that stuff in there.

So we had a trade policy, an import restrictive policy. But really, it was not very logical, because all these other things were part of the problem.

Now, it isn't obtuseness or stubbornness that leads one in that direction; it's that we never really thought through the need for an industrial policy. Our whole process of Government has been oriented in a different way.

To get a new debate going is not going to be an easy task. But the auto industry is a case that cries out for that approach. And in my view, you're not going to solve it by taking a whack at somebody on the imports side, because it really will resolve very little.

Senator RIEGLE. Why don't you go ahead.

Senator STEVENSON. Well, thank you, and you've both been charitable. But that's, to me at least, the real issue. This is not only the largest manufacturing industry in the United States, it's symptomatic of what's happening in every sector of the American economy.

It gives us an opportunity, as well as a terrible problem. The opportunity is to develop an industrial policy or strategy for the United States. Where Senator Riegle and I disagreed over Chrysler was not on the need to do something. It wasn't a simple question of bailing out or not bailing out Chrysler, though that's the way the issue was formulated by the media.

For me, at least—and I'd like to get your reactions to this—it created an opportunity to begin a new policy along the Japanese, not the British, lines, which would have taken advantage of the opportunity to supply considerable Government financial assistance, not to Chrysler, but for adjustment: to transfer the assets, retrain the personnel, and redirect productive capacity toward industries for which there will be large markets in the future.

You've heard my questions. I still don't have any very clear picture of where we're going to be as soon as 1985. There are some—and maybe you can respond to this—who estimate that the way the world is going, the world supply of automobiles for export will exceed demand by half a million cars by 1985.

In the meantime, we in the United States are reduced to one plant for the production of passenger rail equipment—German-owned—and we're reduced to two bus manufacturers. And I find

competitive problems in all sectors indicated by some of our studies, even in technology-intensive industries like genetic engineering. We may have invented the whole science, but the Japanese may be the first to exploit it.

I think we have to do a better job of peering into the future and with cooperation among industry and government, universities and labor—including a little labor-management cooperation—we have to start redirecting our efforts toward the future, instead of, as the British have with British Leyland, toward maintenance of the status quo.

Are there any estimates of production capacity for automobiles by the mid-1980's? Is there going to be an export glut of half a million cars by then?

Dr. MALMGREN. It depends on world market demand, because there are many emerging countries that are buying cars, you've got to remember that.

World income grows very fast in the emerging world. We don't know whether that growth can sustain itself, given the recycling problem, but at least in the last decade the indications are that that is a big market out there. Korea is already servicing Southeast Asia, and we haven't seen Korea here, but it's coming in due course. That's part of your future.

Senator STEVENSON. Production will be coming onstream, but the market, at least in the LDC's, may not materialize?

Dr. MALMGREN. Well, it will materialize one way or another. Whether it's just that you have assembly in developing countries, or whether you bring it from Korea or somewhere else, that market will grow. Japan's capacity is a question mark, and there are various estimates, but it is quite possible that, say, Japan's capacity this year may be something like 11 million units, if I recall correctly, by 1982, quite probably 13 million units, so you have an increase going on there.

In a fairly stable home base, where the home base is somewhere around 5 million units, if I recall, so then that's basically going out into the world someplace.

Now it's possible that there will be growth in the European market. I have a tendency to doubt that because the Europeans are, if anything getting more restrictive right now. But, you know, it's going to be an overhang situation probably.

CAPITAL MODERNIZATION

Now that leads you into this period of capital modernization where you're looking at an overhang in any industry, then you say, do I really put money in Ford? I mean not only do I have a soft situation now, but in 1985, I'm not sure.

Conversely, looking into the future, as you've pointed out, what kind of plants would you get if you start getting foreign producers to put their plants in here. What we have done in recent years is made some breakthroughs, including with semiconductors, integrated circuits, and memories. We are using that a little bit here and there, but the Japanese have managed to take the memories and put them into robotics, and they're moving very fast with it.

Where we have been lagging behind—I'm not so sure it's in pure research and development in this country. It's more in applied

research and development, and particularly research and development relating to the process of production and not just the end product. We're so product-oriented that we forget how you put it together is very vital. And that's where Japan has been moving right along, and I fear for what can be done in the production side in this industry in 1985, or thereafter, unless our people think very far forward.

Now there is one other aspect and that's energy. There's wishful thinking that somehow the energy problem will go away. But we know it's a tight fit through the 1980's, maybe worse, but we have one odd element here, which I think the auto companies again are not looking at. I think the oil companies even sometimes don't see it, and that is the political stability of the Persian Gulf is not great. I've done a lot of work on that recently, and I'm now becoming convinced that we have a very volatile situation.

So an investor looking at that, then the auto thing gets even more hairy. So this forward look, we don't know. We know capacity is expanding, especially in Japan, and I think, for example, some of our companies are really worried about that specific thing, with a lot of examination of where the factories are, and what the scale seems to be. They're getting very nervous about that.

But, so far, anyway, it hasn't bothered GM and I think the answer is because they are big enough scale to stay a little ahead, probably.

Dr. BALDWIN. It seems to me it's going to be very hard for us to break into the LDC market. It's a highly protected market. They've done the same thing that we are talking about with the domestic content rule, without using such a rule. What they do is put a very high tariff on finished automobiles, and a low one on knocked-down automobiles, so you get foreign auto industries to export disassembled autos that are then put together locally. Of course, I think they very much want to hold on to this market. They're not going to give it up unless we make concessions in some of the areas where they have export potentials, some of those very labor-intensive sectors that we have difficulty with here.

Another point I want to make is that when you introduce import quotas you generally do not begin with a general quota that applies to everyone. Invariably you're going to have to put it on the major existing producers or set it up so it falls mainly on the Japanese.

What begins to happen then is that you may stop the surge of Japanese cars, but there is a vacuum created in the market. The Europeans are likely to begin to fill that market. This happened in shoes. The Italians enormously increased their exports to us after we put quotas on footwear imports from Taiwan and South Korea. If auto quotas are imposed on Japan, then you'll get greater auto exports from Korea and Europe, or the Japanese will move to other countries and begin to invest.

Senator RIEGLE. I think it's a general proposition. What you say may make sense, but I think we are talking here about a problem that is very largely a transitional problem. The fact of the matter is Chrysler will have 900,000 units of four-cylinder front-wheel-drive production ready to go starting in about the second or third week of August of this year. Ford and GM both have smaller cars in their product mix for the coming year, so that if you are able to

even push some of today's sales forward 5, 6, 7 months, I mean you begin to have an effect. I mean it's not as if—I don't know that you have to treat this problem in a generic sense. I mean I think it makes more sense to treat it as it is, as a one of a kind problem.

I don't know of another situation quite like the auto problem at the moment, like it's apt to be for the next, say, 18 months to 2 years.

Dr. BALDWIN. Thus far I agree that the auto industry has been posing the problem as a need for temporary protection. I certainly heartily approve of framing it that way. We do, however, have the experience that once you start protecting, that you've got to continue that protection because, for example, some companies keep lagging behind and insist upon continued help.

Senator RIEGLE. Maybe there should be a quid pro quo. In other words, I'm not suggesting—I would argue against somebody suggesting that if you provide a form of protection that you don't ask for something in return. I think you ask for a lot in return. I think that's where the goal-setting comes in.

I think the question is here that you give something in order to get something. I mean why can't it be viewed in that framework?

I'll tell you this, if Lyndon Johnson were President today, in my view, and he wanted to solve this problem, antitrust legislation notwithstanding, Strauss went over and negotiated a voluntary agreement on television sets, as I'm sure you know, not all that long ago.

All I'm saying is that when the administration has a desire to be ingenuous and creative and solve a problem, it can be done.

By the same token, if people basically want to sit around and wring their hands and say that nothing can be done, that there's this thing hamstringing and that thing hamstringing it, we drift.

Dr. BALDWIN. You're so right, that it does have to be done at a Presidential level. Say you go through the ITC case, and then come out with a quota. Now they don't have the power to extract some quid pro quo. All they can do is recommend import relief.

If you want to get that kind of total package, it has to be done outside of these kind of established mechanisms that we have.

Senator RIEGLE. Do you mind if I ask just one question here on the antitrust thing? Because I think that's maybe been inflated beyond its true size in terms of the degree to which it is a rock hard impediment, because I've seen us work around it before.

So let me just ask, who would take the action? Who would bring the action?

Dr. MALMGREN. You mean against the U.S. official, for example? Well, the antitrust division has been saying repeatedly that it would hold ——

Senator RIEGLE. So the Attorney General would sue the President if the President ——

Dr. MALMGREN. Well, in the steel case, you know, that came up in the late 1960's or early 1970's, Consumers Union brought it, but the parties sued were the Assistant Secretary of State and certain other officials. Very specific people. That's the way that law works. So that's what gives pause to any official who says, well, thank you very much, I'm not going into that can of worms. So it becomes very personal, this problem.

If the President does something or the Attorney General shows leeway, it's a different ball game. But individual officials are not really in a good position to take risks in this.

Now let me say that in the past, although the law is structured this way, the law is itself always to a degree ambiguous about what its intentions are. That's why you have courts and lawyers out there making a lot of money. And it's why you have to keep legislating all the time, to clean up the debris.

In this field, in the past, you're quite right, I mean I did serve under President Johnson, and there were occasions when things mysteriously materialized, and who knows how they happened? There were restrictions on footwear from Korea that just appeared at the appropriate moment.

Now, how that happened, who knows? There was a unilateral action, and it seemed to be about the right level and the U.S. industry looked in there and said it seems OK to me.

I'm not sure what specifically took place. Currently the Administration can't seem to be able to do that. I understand why, but the question then is up to the Congress to somehow deal with that problem, that very specific narrow issue, because there's no use to blame an official in the executive branch of being difficult if he's being told that he will go into some very deep legal proceeding personally if he sits around and talks about it.

So it's a very awkward situation, and I think probably the administration on the trade part of this has worked very hard, and I think, to be quite honest, I believe the Japanese side has worked very hard to try to unravel and undo some of the problems and to move forward. But to get anything other than a formal restraint, such as through this escape clause procedure, it's just very hard to do.

ANTITRUST ISSUE IS A RED HERRING

Senator RIEGLE. Well, let me just say on that, that you and I have a disagreement, and I think the President uniquely does have a responsibility. I think it's one that he doesn't yet understand and he hasn't moved to exercise. I think the antitrust issue is essentially a red herring, no disrespect to you.

Dr. MALMGREN. I'm not a lawyer. I won't defend it.

Senator RIEGLE. I understand you're not, but I think that has to be given some weight as well. But I think the issue is a red herring. I think it's thrown out as a way to basically justify doing very little, and to continue to drift. I think it's a tough issue. I think it's beyond the scope of the folks today at the top level who ought to be looking at this. It doesn't fit what they know, and it's not a comfortable problem, and basically I think it's a lot easier to shove the antitrust argument forward and do nothing. And I'm not here advocating we just take short run action, because if that's all we did, and we didn't really address these fundmental issues at the same time, so that we were building in a strategy that met the short term, the intermediate term and the long term, you know, we wouldn't have done anything at all, anyway.

But you can't—our problem here is we really don't have any of the three pieces in place yet, and I don't think you can basically hang your hat on one part and say that the others aren't necessary. I think they've got to be faced.

I have no doubt in my mind that if Lyndon Johnson were President today, or if Adlai Stevenson were President today—this Adlai Stevenson were President today—that a way could be found to work this out. And I think it could be done without rupturing our relationships with Japan. I think they are astonished, frankly, I think the Japanese Government and manufacturers are astonished that there hasn't been an initiative taken to work this thing out.

Unless my information is wrong, Great Britain has found a way to do this. They have found a way to do this in parallel, I might say, with written law, with written trade law, and it's worked very nicely. It's worked nicely for them and for Japan.

The notion that somehow they can do it in terms of a parallel understanding and we cannot, I think that really insults our intelligence, to assume that. And I think whatever gets thrown up in the way whether it's the notion that the Attorney General is going to go in and throw handcuffs on the President if he starts to pursue some kind of orderly marketing agreement, I think is a dodge. I mean the fact of the matter is we have not come to grips with it and we are in worse trouble today than we were a few months ago, and we'll continue until we do come to grips with it.

Dr. MALMGREN. I don't disagree with you. I'm saying that that is a hitch which is very difficult for an official to deal with.

Senator RIEGLE. I don't disagree with that. I don't know that you could solve this problem if you were an official in the trade area as such. I think you need some help.

Dr. MALMGREN. Well, there are some points I made when you were out that someone on your staff should appraise you of regarding what the Japanese signals have been, because I think my reading of that is pretty accurate. I think the signals have been there, that there could be cooperation, if only there were someone to talk to, whatever that cooperation needs.

It's also my experience in trade policy, which goes back a long time now—I'm beginning to feel like an old timer—but it goes back sufficiently far that I have felt whenever there was a big problem with another country, if we had a clear idea of what it is we wanted to do during the transition, then there would be cooperation. It sometimes was unilateral forebearance, let's put it that way. There was a sense of what makes sense in the marketplace.

But if you don't know what you're going to do, and you have no idea how you're going to use the transition, then why should anybody cooperate? You know, that's not in their interest. So there has to be some vision, and with that, I believe you will get the kind of cooperation and orderly adjustment, because it suits everybody then to get on with the job of gradually building a sound market in the 1980's, rather than tripping over each other, racing to keep alive and survive the next 3 years.

[The statement follows:]

STATEMENT OF HARALD B. MALMGREN

I am honored that you have asked me to comment on the present predicament of the American automotive industry. In the letter to me from Senator Stevenson and Senator Riegle regarding the scope of today's hearings, you asked me to discuss what can and what cannot be done to ease the competitive conditions for the domestic auto industry within the rules of international commercial good behavior.

Senator Riegle has, I know, been trying very hard to find some way to ease the adjustment difficulties in our domestic industry, and I am well aware that many

members of the House and Senate have become very worried, both about the high level of unemployment and about the future viability of our major motor vehicle producers.

Naturally, the rising share of imports in domestic sales has caught attention, and much recent Congressional commentary has focused on the role of imports. Since imports from Japan have been especially strong, particular attention has focused on imports from this source. One of our most outstanding labor leaders, Mr. Douglas Fraser, has repeatedly called for action by Japanese producers to moderate the flow of exports and to bring about investment in production facilities in the U.S. The Administration has tried to respond to the pleas of Mr. Fraser by urging Japanese producers in particular to undertake new investments in production facilities in the U.S., to acquire a greater share of their parts in the U.S., and to liberalize access to the Japanese market for U.S. automotive exports. There has been some progress in this regard. The Japanese Government has just agreed on a package of import liberalization measures, and a Japanese group is coming to the U.S. soon to look at parts acquisition. What the Administration has not been willing to do is to press for Japanese export restrictions.

As an outsider with some experience in this field, let me first observe that there is undoubtedly some controversy among Executive Branch officials about what should be done in the next two or three years. Some officials worry about achieving our energy conservation objectives without unlimited access to imports. Some officials worry about the inflationary problems that might arise if imports are curtailed. Some worry about the numerous trade demands placed on the Japanese government in recent years and the possibility of a bad political reaction sooner or later if the U.S. keeps asking for unilateral actions by Japan. Some officials worry about possible retaliation, or the high price of compensation which might be required by other nations if we restrict imports.

But amongst the preoccupations, antitrust policy and the general trade policy implications have perhaps been the principal factors affecting Administration policy on automotive imports.

The situation appears to me to be this: the Japanese government and perhaps even the major Japanese producers seem to be willing to consider export limitations, but the U.S. Government is unwilling to discuss them. I am told that when this idea has come up between governments, American officials have said that they cannot discuss any form of trade restraint, or that they can "neither encourage nor discourage" such a line of thinking on the part of Japanese authorities. Behind this wall of silence are, I gather, a number of warnings from our Department of Justice to other U.S. agencies that any discussion by U.S. officials or private persons which might lead to limitation of exports to the U.S. could constitute a violation of our antitrust and other competition laws. Obviously that is a strong deterrent. Moreover, unilateral actions by Japanese manufacturers to curtail their U.S. sales could also run afoul of our competition laws.

This is not an entirely new problem. In the 1960's and early 1970's, officials of the State Department were accused of conspiring to restrain trade when they helped to develop a voluntary export restraint agreement to limit imports of iron and steel products from Japan—at a time when our domestic industry felt that it was being disrupted by imports. That case took a number of twists and turns, and the Congress had to write into the Trade Act of 1974 a retroactive provision to deal specifically with this issue. In the mid-1970's, the Japanese steel producers, European steel producers, and Japanese and European governments appeared to favor a negotiated orderly marketing agreement on steel with the U.S., but the U.S. Government was forced to reject the idea.

Small wonder, then, that the Administration has been silent on the issue of Japanese export automotive restraints. Nor is it any easy matter for Japanese producers to consider. As for the Japanese Government, I am not a lawyer, but it is conceivable that the Japanese Government has some power to limit exports, but even then it would be unable to determine U.S. official thinking about the appropriate action because U.S. officials would be prevented from discussing matter.

There is a long history between Congress and the Executive Branch regarding those specific occasions when the President is empowered to discuss import restrictions, or restraints on exports to the U.S. As you well know, the U.S. Constitution reserves to Congress the power to regulate foreign commerce. Therefore the President can act only if the Congress grants him specific authority to act. On several occasions in recent decades there have been bills before Congress granting broad discretion to the President to negotiate or otherwise implement import restrictions when imports threatened to disrupt or emperil domestic producers, but the Congress itself has chosen not to enact such general discretionary proposals into law. Rather, after many years of gradual rewriting of our trade laws by the Congress there are

still only a few specific instances in which the President may act to limit imports, and these have been carefully stipulated in trade legislation. You will recall, for example, the fact that the courts struck down the general import surcharges ordered by the President as part of the August, 1971, emergency economic actions. The courts ruled that the President did not have the power to impose such import restrictive action.

Similarly, our antitrust and othe competition laws work in the opposite direction. Indeed, one official of the Justice Department said in a public statement, referring to the import relief laws, that there was "a tension between the policies reflected in these laws and the policies contained within the antitrust laws." The antitrust laws promote open competition and efficient allocation of resources without regards to, or respect of national boundaries, so long as the activities in question affect U.S. commerce. Our import relief laws on the other had provide for restriction of import competition flowing from certain kinds of injurious foreign competition, which are spelled out. The Antitrust Division of the Justice Department explicitly regards these import relief provisions as exceptions to the broad antitrust policies laid down by Congress.

These questions are at the heart of the present resistance of the Executive Branch to the plea for import relief for automotive products: What is explicitly provided for in the import relief laws the Executive Branch can work with, but as for other ideas, the present laws do not allow improvisation.

What then is allowed under our present trade law? Boiled down, and without legal jargon, let me summarize what is permitted by Congress:

(1) If an industry seeks import relief under the so-called "escape clause," and if the International Trade Commission (ITC) finds after an investigation that imports are a substantial cause of serious injury, then the ITC may recommend restrictions such as a rise in traiffs or quantitative limits on imports. The President may implement such recommendations, or he may decide on an alternative course, such as negotiation of "orderly marketing agreements" with selected countries. This, for example, was done in the cases of TV's imported from Japan and footwear from Taiwan and Korea.

(2) If an industry complains, and it can be shown that imports are being "dump" in the U.S., and if the ITC finds that there is material injury from the dumped imports, then antidumping duties may be levied, or a price agreement can be negotiated to eliminate the dumping margins.

(3) If an industry complains about foreign government subsidies, and it can be demonstrated that such subsidies exist, and if the ITC finds that there is material injury, then countervailing duties must be assessed, or an agreement may be negotiated with the relevant governments controlling their exports to the U.S.

(4) If an industry can demonstrate unfair practices in import trading activities, such as patent infringement or some form of conspiratorial behavior, the ITC can order an embargo, or it may negotiate some kind of order restraining the unfair or anticompetitive practices.

(5) If Communist or non-market economies are involved, special powers to regulate trade are delegated to the President.

(6) If there is an overriding national security interest, or emergency, or trading with an enemy is involved, the President has special powers.

(7) If there is provision elsewhere, as in the Agricultural Adjustment Act of 1956, to limit imports in relation to domestic agricultural programs, the President can seek a multilateral negotiation (this was the authority for textiles and textile products).

These authorized exceptions are carefully drafted in elaborate legal detail, with substantial legislative history to give further guidance. For automotive products, (1), (2), and (3) are relevant. Can these provisions be used in the automotive area? The U.S. Treasury investigated claims of automotive dumping a few years ago and found the claims unsubstantiated, although there were some price adjustments made at the time. As for subsidies, the case would be hard to make against Japan or Germany, but perhaps something could be done about troubled auto producers in other nations that benefit from special government assistance. The impact of U.S. imports would however be minor.

This leaves the escape clause provision open, and that is the avenue chosen by the UAW, when on June 12 they filed for import relief. That case will in the normal course of events take six months before the ITC, and if the ITC finds serious injury or threat of serious injury, then the President could act any time thereafter up mid-February, 1981.

Can anything legally be done sooner? Not much. The Congress could ask the ITC to expedite the case, and perhaps gain a month or two, but the job of analysis in

this case—the biggest ever before the ITC—is so great that a very fast inquiry would be almost impossible.

Let me turn then to the international considerations. The U.S. import relief laws are consistent with U.S. international trade obligations, and indeed they have been drafted to ensure conformity. The Congress spent months last year developing the Trade Act of 1979 to implement the international accords negotiated in the Multilateral Trade Negotiations.

Under the international rules, import relief actions are allowed, but they must pass through the kinds of tests stipulated in our present law. Antidumping and countervailing duty actions can, for example, be taken if the tests are met, and there is no need to compensate other nations or become subject to retaliation.

The escape clause provision is rather different. Here, the GATT provides that a nation may, because of domestic problems, raise the level of protection, if serious injury can be shown. However, the items affected will have been subject to trade negotiations over the years, and the current level of protection will have been set as a result of international agreement. Other countries will have paid for the present level of protection with concessions on their part. If the tariffs are now raised, or quotas applied, other nations then have the right to request compensation or, failing agreement on the appropriate compensation, take retaliatory action. The compensation or retaliation would ordinarily not be in the same product areas.

In other words, the GATT allows a nation to raise its import barriers when there is a case of serious injury, and when a government feels a period of protection would help that nation's producers and workers get over their difficulties. But, and this is a big but, the government undertaking such action may be asked to pay for it in new concessions to other nations, or suffer reduced access to other markets through retaliation.

In the case of automotive products, the UAW has chosen a sound course in working through the escape clause procedure. The escape clause provision was designed for this kind of transitional difficulty which the industry and its workers seem to be facing. However, the U.S. later might have to pay, and such payment would one way or another have to be made by other U.S. industries and workers, who would experience increased imports or reduced export opportunities. The amount of "payment" would not be small. We are talking about trade coverage that might be in the 15 to 20 billion dollar range. In theory, the President could, under the escape clause procedure, negotiate a voluntary orderly marketing agreement with Japan, with Japan agreeing not to seek compensation. But Japan would also have to agree to let other nations continue to supply the U.S. unhindered. The GATT provides that escape clause action be non-discriminatory, and the UAW request addresses that by asking for restrictions on all the major suppliers except Canada. Japan might not be willing to let the European manufacturers have a free ride.

The European producers, and their governments, are not likely to be sympathetic, since their exports have not been rising in the same way as Japanese exports to the U.S. They could resist restriction, throwing the U.S. into a very complex and unpleasant negotiation, with high stakes for other American interests.

Thus, I believe the escape clause avenue may have been the best route given our present law, but it leaves many big questions to be resolved early next year.

Are there other remedies? Legislative action by Congress to restrict imports, for example by domestic content requirements, would not be allowed under the GATT. Other countries could and probably would insist on compensation or retaliation. It is true that there are domestic content requirements in many countries—but not in the home markets of the major suppliers to the U.S.

There are special import restrictions, especially against Japan, in some European countries, but these date back many years and have not really been negotiated away, or else they are a result of a combined private industry and government "understandings" on allowable levels of imports. They do have the effect of reducing Japanese access to some of the European markets, and thereby encouraging greater concentration on selling in the U.S.

The ways in which the restrictions against Japan are handled would probably not pass muster with our Justice Department, if the U.S. were to do the same thing. One wonders indeed how the antitrust officials in Europe manage to accept and live with the particular "understandings" that are utilized to control imports there. Be that as it may, we cannot blame the Japanese for what the Europeans choose to do—but we can focus our policy concerns on European practices, which indirectly affect the U.S. The escape clause case could provide some leverage in this respect, if the ITC rules favorably on the UAW petition.

I do not intend to list here the particular automotive import restrictions in various markets around the world. The escape clause petition of the UAW,

presented by the well-known trade lawyer, Eugene Stewart, does this, and I expect that various pieces of testimony before Congress have also covered this territory.

The major restrictions are in developing countries, but these countries in many cases have not negotiated their barriers down, and even now refuse to bring their trade practices into conformity with recent international trade agreements. They feel they have not benefitted adequately from the global trade negotiations of recent decades, and they are often therefore unwilling to consider liberalization of their own trade policies. Many of them do not belong to the GATT. But, lest we overreact to their stubborness, it should be remembered that the U.S. exports to most of these nations much more than it imports from them. Moreover, they have become the principal growth markets not only for exports of food but many capital goods and engineering and construction services.

Let me turn now to the question of foreign investment in the U.S. It has been the experience of U.S. international companies that when they have achieved very large positions in various markets around the world they have found it advisable to develop a local presence. The reasons are many—partly economic to be sure. But the image of local participation, of good corporate citizenship in other nations, has also been a factor in expanding production abroad. There have also been quiet official pressures to produce abroad, or suffer impeded access, just as there have been official incentives to build new facilities abroad. So our multinational enterprises have expanded their activities abroad, and it would appear that this has involved even further expansion of U.S. exports in many cases. However, many of our union leaders have bitterly denounced this march abraod. We are now asking the Japanese and others to come here, as good corporate citizens, but this has to cut both ways. It will teach other nations to force our domestic producers who export to do more of their production outside the U.S.

Business judgment should include the good corporate citizenship consideration, and it is surprising that Japanese producers have not weighed this factor more heavily. On the other hand, the economic factors have to be reasonably favorable.

What we cannot now readily see is what the structure of the world industry will be in 3 or 4 years, or in 5 or 10 years. If the "world car" concept develops, components will be produced at various points in the world and assembled in a number of markets. We can also expect that the enormous capital requirements for modernization of production facilities, development of more fuel-efficient engines and vehicles, and alternative modes of transport all will hurt the small producers. They won't do well, unless they specialize in components or novelty or special purpose vehicles. In fact, some analysts believe that the world industry must inevitably be squeezed down to a half dozen or at most eight producers—perhaps not more than two in the U.S. Our Justice Department might hardly recognize such a world—and might well try to break it up. Yet it could be a way forward, given the capital needs. Or we could perhaps see a few giant assembly companies, highly automated or "robotized," using components from many smaller companies. Frankly, I do not think we have thought through where we are going.

Japanese investment in new production facilities would not affect demand for U.S. workers in the next two or three years, because it would take that long to get the plants going. When we focus on foreign investment we have to take a longer view, of where we think the U.S. industry will be in the mid-1980's. If the future U.S. models are successful in their downsizing and efficiency, do we really want additional production by additional producers inside the U.S.? Do we know whether U.S. producers would then transfer jobs and do more value added abroad and concentrate on assembly here, in such a case?

The real problems of our industry are broader than the import problem. They lie in the area of tax treatment of capital spending, of regulatory policies, of confusion in energy and urban transport policies. Our present focus on imports is out of frustration with the rest of these issues.

It seems to me that the special Chrysler legislation provided an opportunity for a new Executive Branch and Congressional look at the future structure of the U.S. industry, and indeed the future structure of the international industry. The Chrysler legislation even mandated a major reassessment by the Executive Branch, but I am not hopeful that such a major new look will be taken. Already, I have the impression that the Department of Transportation is focussing on short-run trade problems without adequate regard to the broader questions. The ITC will certainly have to take a long-range view, if it wants to determine whether there is a real trade problem in the next few years, as contrasted with the glaring need for change in domestic policy constraints. Perhaps the Congress ought to set about its own long-range inquiry.

It will be difficult for the U.S. government to get the Japanese to invest here in major facilities, and difficult to get foreign acceptance of U.S. trade restrictions, without a new national view of where we ourselves are going.

Already, not only is Chrysler in great difficulty, but Ford has had to announce cutbacks in their capital spending plans. Japanese production capacity appears to be growing rapidly with 1982 capacity likely to approach 13 million units. Japanese exports seem now to be on a trend exceeding production for domestic use, which was not the case in the earlier 1970's. Yet expansion from a strong home base must still seem safer than moving out to produce in a world marketplace where the future structure of the industry is not known, and where no serious examination of structural change is taking place to guide government policies. What will be our future antitrust and concentration policies, or our import policies regarding world car components, or our urban policies, or our energy policies?

In the near term, there will be some modest relief this year because of the recent appreciation of the yen. That appreciation in my judgment will go further, to the 200 to 210 yen to the dollar range. That will reduce the alleged production cost advantage of Japanese producers and probably raise the price of imports.

In this connection, it is partly our own broad economic policies that got the yen so far down in previous months. We urge the Japanese to expand their economy with stimultive policies, and this helped pull the world economy along. But Japanese interest rates should have been raised much earlier, as the rest of the world went up, but Japan stuck to its easy money approach—following our encouragement of emphasis on growth. The yen fared poorly, not surprisingly. This was not just a matter of Japan's extreme dependence on imported oil, in other words. Macroeconomic adjustment policies were a big factor.

Looking forward, we are at the beginnings of a deep and perhaps prolonged recession. The automobile market has collasped. The steel market has probably now reached an even worse stage of collapse. Consumer credit has been stretched to the limits and debt management will be strained by a squeeze on real incomes. Little can be done to stimulate construction or other capital spending until next year, when our tax laws can be reexamined by Congress. We enter this recession with a record behind us of a decade of unusually slow capital formation. Our productivity has been moving in a negative direction. Energy problems have made much existing capacity obsolete, and dictate massive new investments to transform our present industrial structure. When we do start to invest heavily to get our economy back on track, the levels of capital spending required will be enormous. But we have several months, maybe a year or more, of serious trouble to cross before we can hope for investment to take off.

Europe is, in my judgment, in trouble too. Its industrial problems may even be worse.

If we reach out and bang the door on imports, disregarding the rules we ourselves negotiated, and which the Congress has written into our law, then we can expect worse from our trading partners, who have problems of their own. I am frankly not afraid of tit for tat retaliation so much as I am afraid of unraveling economic cooperation among the Western industrialized countries—in steel, autos, chemicals, textiles, and other rules to the winds—we need it to protect our own interests at home and abroad. And we need it to keep some degree of harmony in our relations with the other free world democracies, at a time when our relations are severely strained in the political area.

We have an automotive industry problem. We need to devise policies to deal ith it. But trade is not the only, or even the major problem. It is our own conclusion, indecision, and inadequacy of strategic planning about the U.S. in a global context that is giving us our trouble. Japan was in a way lucky. They are so oil dependent they had to conserve earlier than the rest of us. So trouble sometimes can breed innovation. It is time for us to look at the whole package of issues. In that context, with a wider range of adaptive policies, our trading partners might even show forebearance, cooperation, and even greater corporate good citizenship in the U.S. Arbitrary trade measures will not create that kind of climate, but instead will generate broader economic confrontation in the West, which we can ill afford.

Senator RIEGLE. Well, let me thank you both. We may have additional questions for the record that we'd like to have you respond to, but I appreciate again your patience today and your contribution. Let us enter into the record an article called "Global Auto Battle."

[Additional material received for the record follows:]

[From Dun's Review, June 1980]

Global Auto Battle

WITHIN FIVE YEARS, THERE IS LIKELY TO BE A MAJOR SHAKEOUT IN THE WORLD AUTO INDUSTRY, SAYS EXPERT MICHAEL HINKS-EDWARDS. THIS WILL CAUSE A SHARP RISE IN PROTECTIONISM

With the U.S. auto industry in one of its worst slumps since World War II, the United Auto Workers Union and some of the companies have called for protectionist measures to shield Detroit from an avalanche of imports, mainly Japanese. A similar situation is boiling up in Europe. Due to slumping sales and rising output around the globe, the situation is likely to get even worse by 1985 and could set off an auto trade war, according to Michael Hinks-Edwards, one of Europe's top auto experts.

A Briton who has worked for British Steel and as a civil servant, economist Hinks-Edwards is affiliated with Euro-finance, a Paris-based research organization owned by a consortium of European banks. European Editor Jean Ross-Skinner talked with Hinks-Edwards about the forces that are generating the protectionist wave, its likely shape, and its implications. Here are his views:

What leads you to the conclusion that the mid-1980's will see a sharp rise in protectionism in world auto markets?

Quite simply, looking ahead five years, world car import-export aspirations don't add up. The projected output for export in 1985 totals nearly 6 million units (versus 5 million today), while we foresee a plausible import volume of 5.5 million. So the world could be short of a "home" for half-a-million cars.

Will the Japanese be the leading source of the increase in exports, as they have been in the 1970's?

Yes, in that Japan's total exports are projected at a minimum to increase from 3 million today to 4 million by 1985—two-thirds of the total production forecast. In contrast, U.S. exports are likely to rise from 200,000 to only 500,000—though there is a possibility, not included in our figuring, that General Motors may be gearing up for a major export drive that could push total U.S. exports to 1 million by 1985; if it does, God knows what will happen.

What about the European producers?

West European exports could, we think, actually fall by nearly a third to just over 1 million—in fact, Europe, traditionally a major net exporter of cars, could become a net importer.

So something's got to give. What's your scenario?

First, there's a strong threat of increased protectionism in the U.S. and Europe. The bandwagon is already rolling. This would squeeze exports to these two hitherto free markets for autos. The Japanese market is already closed, as are the Communist markets. That leaves, broadly, the Third World, where protectionism is already widespread. Nonetheless, we believe that what we call the "fringe" markets—broadly, the Third World, not including Latin America—could be crucial in resolving the problem. These markets are usually treated by forecasters as a statistical dustbin, though they have nearly 10 percent of world sales and are expanding fast.

What auto companies are in the best position in these so-called fringe markets?

The truly global companies that already produce there—General Motors, Ford, Volkswagen, and Fiat. Instead of exporting, they can step up local production in these areas. The partially global firms—Renault, Peugeot, Toyota and Nissan—should get some of this market. It's the remaining, nationally-based and export-reliant firms, which include Chrysler, British Leyland, Daimler-Benz, BMW, Volvo, Daihatsu, Fuji, Honda Mitsubishi, Suzuki and Hyundai, that as a group could suffer most unless they change course fast.

There are a lot of Japanese companies in that last category.

Yes. Increased protectionism could hurt them, and they may be forced to build more overseas plants and forge more links with foreign automakers. Certainly, the only way those 1985 figures could be squared relatively painlessly would be an increase in the international sale of auto components and more intercompany collaboration. Meantime, though, protectionist threats could well turn into action.

How do you see protectionism shaping up in the major markets?

I don't foresee any change at all in Japan. The market is almost totally protected now, because by the time a foreign car reaches the final customer it is twice the price of the home product. This is because of the inefficient distribution system, which has many more layers than those in the U.S. or Europe and partly because you can't get dealers without paying enormous margins. Moreover, it's damn near impossible for a company to set up its own distribution system. The net result is that last year Japan imported only 50,000 cars while exporting 3 million.

Couldn't this improve?

I don't think so. If they are importing 200,000 cars by 1985 I'll eat my hat—unless there's some kind of multinational type of arrangement with, for example, Toyo Kogyo making millions of engines for Ford, exporting them to the U.S., and then importing the finished product from the U.S.

Mightn't the fact that their own trade barriers leave the Japanese so wide open to retribution lead them to ease up?

I doubt it, because the Japanese reaction to such criticism thus far has been, "Okay. If you don't like our exports, we'll come and build assembly plants." And in Europe, at least, the result is cries of horror from the domestic industry—at which point the Japanese say, "What can we do then?"

Even without impediments to imports, won't there be buyer resistance to foreign cars on the part of the Japanese?

Yes. Beyond a very small market for specialty cars, Japanese workers are very loyal to their company's product.

What about workers outside the auto industry?

It's hard to be completely outside the auto industry in Japan, since it could be your company's plastic, tires or glass that's in the car. At Nissan, I was told there is no company pressure on employees to buy Nissan. But as they themselves pointed out, nobody buys anything else. No, I simply don't see much chance of the Japanese market opening up in any way.

What is the U.S. outlook?

To me, the surprising thing is the number of people jumping on the protectionist bandwagon. Not just the United Autoworkers, but Ford and Chrysler have come out for classical-style controls like quotas, despite the inevitable schizophrenia because of these companies' desire to import. For example, Chrysler is making money on its Mitsubishi imports but not on its own cars. GM and Ford are rapidly expanding their links with Isuzu and Toyo Kogyo respectively, with component supply deals for the things they lack right now: front-wheel drive joints, small engines and so on.

So some mental acrobatics are required to say, "We're not having your cars but we want your engines." Moreover, Ford, GM and Volkswagen are bringing an increasing flow of components into the U.S. from Latin America. How can Ford rationalize its demand for import controls when it's a big importer itself. Remember, it was bringing in a lot of European-built Fiestas for a time. Still, none of this has deterred Chrysler and Ford, and protectionist pressures are very strong.

How will the Carter Administration react?

I understand that right now there is no support for import controls in the Administration. However, this could change. Auto imports were slightly over 2 million units last year. But today, people are talking of 2.75 million this year and it could well go over 3 million—it's never been easier to sell into the U.S.

Now if imports go on rising over the 3 million mark, and unemployment in Michigan doubles, I am sure the situation will change. Particularly if Chrysler nears collapse. As I see it, Chrysler is the key to the whole picture, because a Chrysler collapse could lead to an emotional reaction against imports, with the real reason for the company's failure being forgotten.

What form might this reaction take?

Well, one Ford suggestion is that each foreign auto company be given a quota 35 percent below 1979 sales, with any excess exports carrying a mandatory 75 percent local content—a scheme that would not hit just the Japanese. But quotas are a crude weapon and I don't really see the U.S. going that far. You've got to have General Motors on your side for that, and with almost 65 percent of the market for domestic cars, GM is unlikely to climb on the protectionist bandwagon.

Assuming the worst, the likeliest U.S. response would be to threaten the Japanese, behind the scenes, with immediate quotas. To head them off, the Japanese government would then be likely to impose some kind of export restrictions on its auto companies—probably restricting them to current levels.

Then you don't expect a cutback in Japanese exports to the U.S.?

It's very difficult to force a pullback, partly because this would be hitting at their U.S. dealers, your own people. That's why when you put the boot in you must do it quickly, before imports become a major factor, as the French did when Japanese sales reached 3 percent of the market.

What about Europe?

Protectionism has made some headway already here, at least against the Japanese. Italy has a virtual ban on Japanese car imports, while Britain and France have already pressured the Japanese, probably using the threat of quotas, into orderly marketing arrangements that curb any major sales boost. This trend could well spread, for the Japanese are pushing hard into Germany, where they have 7 percent of the market and are aiming for 12 percent soon.

German industry claims that most of the lost sales thus far have been by French and Italian exporters into Germany, but that could soon change. It's not inconceivable that even the free-trade Germans could themselves use the quota threat to win their own orderly marketing deal with Japan. Moreover, even countries without domestic automakers, like Holland, Austria and Belgium, are quite likely to be pushed into similar action by the threat of job losses in their assembly industry.

You forecast increasing curbs on auto imports within the European Economic Community. This would be a marked departure from the fundamental EEC principle of a single internal market.

Such internal curbs are an even bigger threat in Europe today than anti-Japanese action, which has, after all, already gone a long way. I think here the British are the catalyst. I don't think anyone would claim that the EEC was designed to cut U.K. auto production by 40 percent since 1973. But that's what's happended, with British Leyland in bad trouble, Chrysler sold to Peugeot, which has reduced production, and GM's Vauxhall also being trimmed back. It's too fast for anyone to absorb.

What's likely to happen?

There's a tough mood growing, and British government circles are starting to be swayed. The feeling is that now is the time to put the boot in not just against the Japanese but against Continental manufacturers. Recently, the Trade Secretary complained about imports into the EEC from East Europe—Fiat is the biggest factor here because of its colloboration with Russia and Poland. Fiat is also importing Brazilian-made cars. Ford brings in a lot of cars form Spain, which will join the EEC in 1983, and also from Germany and Belgium.

Wouldn't any U.K. barriers against Continental cars violate EEC law?

Not necessarily, Britain could use the old technique of threatening quotas unless behind-the-scenes curbs were agreed upon. Then there's the oil card—Britain could be very tough in threatening to cut the volume of U.K. oil going to the Continent unless the pressure came off the British car market. Of course, it's no use brandishing the threat of quotas unless in the last resort you are prepared to use them.

But the present mood in the U.K. is such that I believe the government might be prepared to violate the EEC treaty if necessary, particularly when France is already doing so in barring British lamb exports. However, I would expect the EEC partners to head off any British quotas by informal restraints.

Spain's auto industry is strong, growing and heavily protected. How will Spain's forthcoming entry into the EEC affect the situation?

Spain's the one relatively bright spot, in that approaching EEC membership is forcing it to open its market up a bit. All the same, we beleive that Spain will substantially increase its share of total West European car sales in the early 1980's—as indeed will France. This would leave Britain and West Germany with a falling share of that market.

Will the EEC Commission act?

You could well see EEC pressures on the Japanese for voluntary restraints. But I see no way that they could do much about the internal EEC friction.

What about Third World protectionsim?

It is, of course, pretty widespread and increasing, with most governments demanding a high rate of locally-made content in the finished car, local assembly and a favorable balance of a foreign company's ratio of exports to imports. This policy has served countries like Brazil, Mexico and Spain well, as the British have noticed.

This is why, as I said before, the truly global automakers, with plants throughout the Third World, will not be the sufferers in the export squeeze. The future lies with those companies that can supply these key markets locally, and also use them as low-cost bases for high-volume production of components for their global assembly operations—as, for example, Fiat is using Poland, and GM, Ford and Volkswagon are using Latin America.

What is the outlook for those nationally-based, export-reliant automakers you listed earlier?

Well, Chrysler is the most vulnerable, and the prospects for British Leyland in its present shape are poor. As for some of the others, we would not be surprised to see more and more collaboration. We are already starting to count Volvo as part of Renault, Alfa Romeo as part of Nissan, Isuzu as part of GM, Toyo Kogyo of Ford, Lancia of Fiat, Leyland of Honda and so on.

So I think that along with the probable increase in protectionism there will also be steady increase in collaborative deals, and in the share of the world auto market taken by a big and growing trade in components—on which it is very hard to impose protectionist curbs.

Probably, too, the Japanese will be forced to step up substantially their overseas manufacturing. However, although the Japanese companies are overly-reliant on exports, they also have the skill in selling overseas, which will help cushion them.

This strength springs mainly from the way they find and reward their dealers. Unlike the Americans and Europeans, who think short-term, they take a five-to-ten year look at profits. This has made them masters of Southeast Asia, is helping them to make inroads into Africa, the Middle East and Saudi Arabia.

U.S. COUNCIL FOR AN OPEN WORLD ECONOMY,
Alexandria, Va., June 25, 1980.

STATEMENT BY DAVID J. STEINBERG, PRESIDENT, U.S. COUNCIL FOR AN OPEN WORLD ECONOMY

The U.S. Council for an Open World Economy is a private, nonprofit organization engaged in research and public education on the merits and problems of achieving an open international economic system in the overall public interest. The views expressed here are those of Mr. Steinberg and not necessarily in every detail those of the Council or its Board of Trustees. However, they basically reflect the Council's view of such issues.

America should opt for sound strategy, not simplistic gimmickry, in tackling the troubles of its automobile industry and the unemployment of over 150,000 auto workers. The government's response should fully reflect the policy sophistication, and the economic and technological capabilities, befitting a highly advanced industrial economy. It should avoid measures to which underdeveloped counties (and too often some developed countries) are inclined to resort in efforts to establish or assist certain industries—measures such as import controls or insistence that foreign manufacturers successful in exporting equipment to the consumer country make these items in whole or in part in the consumer country itself.

The basic cause of the U.S. auto industry's troubles is not imports but the industry's sluggishness in shifting to large-scale production of fuel-efficient cars. The industry is now moving vigorously to correct this mistake. Government should make every effort to facilitate this process (to the extent that government help is needed at all) through a coherent auto-industry adjustment strategy as part of a coherent transportation strategy embracing all pertinent areas of public policy including energy, the environment, tax policy and ensuring equivalent or better job opportunities (perhaps in other tranportation-related production) for workers whose jobs in automobile production may no longer be sustainable. Government should re-examine all policies materially affecting the industry's ability to adjust to the new realities, to determine if there are any statutes or regulations that inexcusably impede this process. Any inequities revealed should immediately be corrected.

Government should not, by legislation or other means, require or pressure foreign governments or foreign automobile producers (Japan is the current focus of attention) to curtail their shipments of cars to the United States, restricting not only the consumer's freedom of choice but also the nation's progress toward greater gasoline efficiency. In any case, it is hardly certain that U.S. consumers denied freedom of choice by these import curbs would, even for the most part, buy American-made cars they did not rate as high by fuel-efficiency or other standards. U.S. production of fuel-efficient cars is already at capacity and would not benefit from these import controls. Nor should government, by legislation or other means, require or pressure foreign automobile manufacturers to establish U.S. plants from which to supply the U.S. market, or to use certain percentages of U.S.-made components in the cars they sell here from whatever source.

If economic considerations warrant such production changes by foreign auto makers, all well and good. But politically pressured shifts of this kind would create distortions in world auto production and trade, in fact a can of worms leading sooner or later to foreign retaliation or emulation—ultimately, perhaps, adversely has a strong competitive advantage. The fact that some foreign governments already require domestic-content inputs in U.S.-supplied equipment is no reason for the United States to broaden the practice. Instead the time has come to mount a strategy to get such measures terminated.

One of the distortions resulting from the politically pressured creation of foreign auto plants in the United States could be expansion of this country's auto industry to levels unjustified in the not too distant future by the realities of revolutionized consumer demand in a dramatically changing energy environment. In any event, by the time these foreign plants come into production in the United States, the U.S.-owned domestic auto industry will have (certainly should have) fully converted to the fuel-efficiency standards so long delayed, and the present turmoil in the domestic industry will have ended. Current unemployment in the U.S. auto industry will not be alleviated significantly, if at all, by foreign investment in U.S. auto production. New plants take time.

The strategy needed should, among other aims, look toward the development of foreign markets (including Japan) for new types of U.S. automobiles now in production or in protest. Its ultimate goal, clear and deliberate, should be world-wide free and equitable trade in automotive vehicles and components. The U.S. government should program negotiation of an automotive free-trade arrangement, and the U.S. automotive industry should immediately crank a free-trade premise into its decision making. The costs and benefits of whatever aid is included in the government's auto-production policy should be publicly explained and systematically reassessed. The government should elicit a firm commitment from the industry concerning the use the industry plans to make of the subsidies which government help of any kind entails. The industry's overall plan should be subject to government approval, and the industry should be held fully accountable for its implementation as a condition for getting help at public expense. The long era of pig-in-a-poke aid to industries seeking government help—including import controls without coherent import-adjustment strategies—must end.

If the nation has a coherent, systemically reviewed petroleum strategy, as I have long advocated, instead of the gimmickry of oil import quotas dating back to the 1950's and oil depletion allowances going back well before that, today's energy crisis and auto crisis might have been prevented or at least alleviated. The nation's policy apparatus remains poorly prepared for the industrial-development, free-trade and energy-reform strategies on which our national sights should be clearly and firmly focused. The fact that the Executive Branch has only recently undertaken a study of the auto industry's problems is but one example of the government's unpreparedness in industrial policy. Many in the long list of other examples result in trade-policy distortions that are costly to the nation in financial and other terms.

Overall, America urgently needs a coherent free-trade strategy, and a domestic-development strategy—including a full-employment, high-productivity, energy efficiency and anti-inflation policy—to backstop it.

Dr. MALMGREN. The commission that I was referring to, one of the members, if you're interested, was the National Resources Commission, set up by a law introduced by Senator Mansfield. Secretary of the Treasury William Simon was chairman, but it was a joint congressional-Presidential inquiry into national resources. It was done in the 1976–1977 period.

Senator STEVENSON. We'll take a look at that.

The committee will stand adjourned.

[Whereupon, at 1:10 p.m., the hearing was adjourned.]

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