The annual report of the GATT secretariat on international trade is published today.

The relationship of trade and monetary developments, the emergence of a major imbalance in the main trade flows in 1972 and a movement toward a better balance in 1973, the reversal of the downward price trend in commodity markets, and the continued growth of inflationary pressures in virtually all industrial countries are the main themes of International Trade - 1972. The report also presents some forecasts of trade developments in the coming months.

Principal conclusions

Principal conclusions of the report, discussed in more detail below, are:

(i) The significant acceleration in the volume growth of international trade (+8% in 1972, as against +6% in 1971) is largely attributable to the upswing in economic activity in the United States, followed by a similar strengthening of demand in other industrial countries.

(ii) World commodity output (+5% as against +3½% in 1971) did not fully match the increase in demand which resulted in a strengthening of inflationary pressures in all the main economies.

(iii) Since there were appreciable differences in the pressures of demand among the main trading nations, a major disequilibrium of trade balances developed in the course of the year, and was further aggravated by sharp changes in the terms of trade.

International Trade - 1972 is available in English, French and Spanish editions, price US$9.00 or Sw F 27, from the GATT secretariat, Villa Le Bocage, Palais des Nations, CH 1211 Geneva 10.
(iv) The rapid increase in world prices, most pronounced in the primary product markets, was due to shortfalls in production in the face of rapidly rising demand, accentuated by efforts at replenishment or increase of inventories and, to some extent, also by speculative hedging in the face of monetary uncertainty.

For 1973:

(i) In the first half of 1973, economic and trade expansion continued to accelerate, despite the endemic monetary instability, as the pressure of demand, fuelled by anticipation of further inflation, strengthened and became more uniform in nearly all industrial countries.

(ii) Present trends point to a continuing improvement of the United States trade balance and a complete disappearance of the trade surplus of Japan. On the other hand, the trade surpluses of France and the Federal Republic of Germany are not likely to diminish in 1973.

(iii) Inflation is considered to be the most urgent problem besetting international trade. "The two major dangers the world economy will have to face in the coming twelve months are the continuation of world-wide inflation, and the risks arising from insufficient international co-ordination of national measures to combat it".

Significant acceleration in the volume growth of international trade

The dollar value of world exports increased by more than 13% in 1972, compared with 11% in 1971. Expressed at constant exchange rates, the increase was only of the order of 12%, as against 9% in 1971. The volume growth, at about 8%, was close to the average of the twelve preceding years, but represented a significant acceleration from the 6% recorded in 1971.

The acceleration of world commodity output, to about 5%, compared with 3% in 1971, comprised some decline in agricultural output, a moderate expansion in mining production, and a near-doubling of the rate of manufacturing output.

A large increase occurred in the volume of international trade in agricultural products; in contrast, the volume increase in trade in manufactures was less than in the previous boom years of 1968 and 1969. Low levels of stocks, and production bottlenecks in certain key sectors, prevented the volume of world trade from expanding in step with world demand and making a more significant contribution to the global effort against inflation.

Growing disequilibrium in trade balances in 1972

The spread of the rates of growth of export earnings between the major groups of countries was "surprisingly narrow" in 1972. Expressed in dollars, the exports of industrial countries, developing countries and of the Eastern trading area all increased by 18 to 19%.
On the import side, the spread was somewhat wider, as the fast growth in industrial areas, and an even faster one in the Eastern trading area, contrasted with absolute declines in the imports of Australia, New Zealand and South Africa and a relatively slow growth in those of the developing areas as a group.

The disequilibrium in trade balances in 1972 was brought about by a massive increase in the United States trade deficit and a sharp turn-about in the United Kingdom’s trade surplus, with corresponding substantial rises in the surpluses of Japan, continental Western Europe and several developing countries.

**Rapid increase in world prices**

A substantial increase in the unit value of world exports expressed in dollars was to be expected after the Smithsonian Agreement of December 1971, but it would also have been normal for unit values expressed in national currencies to stagnate or even to decline. Actually, they did weaken somewhat in the early part of 1972 but in the latter part of the year export unit values in most countries resumed their rapid growth, and the rise accelerated further in early 1973. While export prices of manufactures increased by only 9%, i.e. by slightly more than the extent of the dollar depreciation, prices of primary commodities showed an increase by about 18% between the depressed closing months of 1971 and the end of 1972, and the upsurge continued at an accelerating pace into the first half of 1973.

In view of the GATT economists, although the bulk of the deterioration of the trade balances of the United States and the United Kingdom appears to reflect changes in their trade with other industrial countries, the imbalance was aggravated by the sluggish growth of the imports of developing areas at a time when their export earnings were expanding very rapidly. The broad changes in consolidated trade balances show a substantial reduction of the surplus of industrial areas with the rest of the world.

Correspondingly, the aggregate trade balance of the developed non-industrial countries and of the developing areas improved markedly, whereas that of the Eastern trading area deteriorated.

**Despite the endemic money instability, economic and trade expansion continued to accelerate in the first half of 1973, in an increasingly pronounced atmosphere of inflation.**

The report shows that the monetary uncertainty does not seem to have had any adverse impact so far on the development of real demand and output, employment, and the expansion of international trade.

With inflation proceeding rapidly in all industrial countries participating in a simultaneous economic upswing, the additional transaction costs caused by the monetary crisis have been easily absorbed by enterprises, importers and exporters.
During the first half of 1973, the current dollar value of world exports appears to have increased at an annual rate of about 40%, and the volume increase approached an annual rate of 15%.

Even if this rate slows down in the second half of 1973, as it is likely to do, for the year as a whole the volume increase of world exports is likely to exceed 12%. World output is likely to show an increase of more than 7%, matching the record year of 1951.

"Everything thus seems to point to an exceptionally vigorous expansion of demand, output and trade, in spite of the monetary crisis, and to a most welcome reduction of the relatively high unemployment rates which prevailed in many countries throughout most of 1972."

Present prospects for international trade

In the view of the GATT economists, three questions arise for the future:

- the effects of parity changes and the partial return to equilibrium;
- the problem of inflation;
- questions arising from the fight against inflation.

To what extent has the second round of parity changes, which started in the early months of 1973, speeded up the adjustment process? By July, the average depreciation of the dollar vis-à-vis other currencies eventually reached more than one fifth and the effective appreciation of the German mark, the Swiss franc and the yen was of a similar order of magnitude.

"In these conditions, it is hardly surprising that the trade figures and the estimates of current account balances available for the first half of 1973 already show rapid progress towards equilibrium."

The trade deficit of the United States reached $1.6 billion at an annual rate in the first half of 1973, as against $7.3 billion in 1972. Quarter to quarter developments indicate a rapidly continuing improvement.

"Although the value of agricultural exports may decrease in the second half of 1973, the trend of manufactured exports appears to be such that the trade deficit in the second half-year is unlikely to exceed that of the first half-year, bringing the expected yearly total trade deficit into the neighbourhood of $1.5 billion, i.e. perhaps one fifth of last year's deficit and below the deficit of 1971, with a possibility of an even better performance."

The most rapid adjustment among the surplus countries appears to be taking place in Japan. Depending on the behaviour of primary product prices, a more or less marked further reduction of the surplus, even its complete disappearance, in the second half of 1973 and/or the first half of 1974 appears likely.

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The generalized inflation has, however, reduced the importance of price competition, notably for investment goods.

As long as this situation persists, and despite the recent deterioration in the terms of trade, there is little chance of a decline in the merchandise trade surplus of the Federal Republic of Germany, which for the year as a whole will substantially exceed the 1972 figure "though the latest appreciation of the German mark is likely to increase further the deficit on invisibles".

For Italy, "with Italian products highly competitive on international markets at present parities, one could reasonably expect a renewed increase of the trade and current account surplus in the twelve months to come".

"Among all the major countries, France experienced in the past three years the smallest fluctuations in the overall rate of growth and in the merchandise trade surplus. If anything, the trade surplus and even more the surplus on current account could increase further in the near future".

The combined current account surplus of the three main continental EEC countries (and probably of continental Europe as a whole) was thus not reduced in the first half of 1973 and, in the view of the GATT economists, is unlikely to be in the second half of this year. At the same time, there has been a rapid deterioration of the position of the United Kingdom, where an abnormally large trade surplus earned in the second half of 1971 turned into an increasing deficit, aggravated by the deterioration of its terms of trade.

The dangers of continued inflation

The report points out that all these forecasts for the development of trade are based on the assumption that the present inflationary explosion is going to be subdued gradually, without sharp setbacks occurring in the international money and commodity markets.

"It is still an open question whether an individual country can adjust to a continuing inflation of 10% or more per annum without sacrificing growth in the long run. And it is all the more doubtful that similar adjustment would be possible for world economy as a whole. If that is not possible, the recurrence of attempts to flee from money into real values could not fail significantly to reduce the efficiency, and increase the instability, of the world economy."

The opposite danger, the report suggests, is that insufficiently co-ordinated national action to combat inflation might produce a spreading and cumulative deflationary effect capable of setting back world trade, production and employment. Although even drastic deflationary measures taken by individual countries are unlikely to have adverse effect on the world economy, they could produce an overkill if introduced simultaneously by a number of important countries.
The GATT economists believe that there should be close international co-
ordination in formulating and administering national policies to combat inflation,
and that trade policy should if possible be used as an anti-inflationary
instrument.

The explosion of commodity prices

According to the GATT economists, the explosion of commodity prices may
well prove to be the crucial economic development of 1973.

The commodity boom is having far-reaching repercussions in several direc-
tions, and raises some basic problems for the medium and long run. It constitutes
a further, and powerful, inflationary impulse, primarily for the industrial
economies. It is not beneficial, however, for all the developing countries.
Those which have a deficit in basic foodstuffs and/or other essential primary
products and which for various reasons, generally unrelated to the current
monetary instability, have been unable to participate in the current export
boom have been, by the same token, hard hit by the inflation of prices of their
imports.

Between the last quarter of 1971 and the second quarter of 1973, according
to the United Nations index, prices of primary products (in dollar terms)
increased by more than two-fifths. The largest price increases took place in
the case of agricultural products. Prices of fishmeal, wool and cocoa rose
between two and three times, those of rubber and soya beans almost doubled and
prices of wheat, maize, sugar and beef increased 60-70%. Price increases ranging
between 40 and 50% were recorded for rice, coffee, and groundnuts. For most
minerals and non-ferrous metals the price increase was less than 40%, while for
a few commodities, such as tea and butter, there was hardly any price increase
even in dollar terms.

The report underlines that these price increases are attributable rather to
shortage of supply than to speculation. Supply bottlenecks became evident in
some primary commodities and, in others, the stock levels were clearly too low
in relation to possible variations in world output.

"To minimize the danger of situations of this sort recurring in the future,
there is a clear need for the recognition of international responsibility for
trade, production and stock-keeping decisions in the primary sector".

The impact of parity changes on costs and prices in the industrial countries

International Trade 1972 notes the substantial effect of changes in parities
on costs and prices in the industrial countries.

By mid-1973 the parities of the yen and several continental Western European
currencies had appreciated considerably in relation to the dollar. If, however,
one introduces as a weighting element the relative importance of individual

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trade partners, the effective appreciation of the yen is greater than that of the European currencies, because the European countries have intensive trade relations with each other.

The report shows the marked impact of parity changes on wage costs and export prices.

The appreciation of the yen, the Swiss franc and the German mark, notably vis-à-vis the dollar, has made a major contribution to the closing of the gap between hourly earnings in manufacturing. The ratio of United States hourly earnings to those in Japan has moved from 5 to 1 in 1968 to 2.3 to 1 in 1973. The corresponding figures for the United States - the Federal Republic of Germany were 2.5 and 1.2, for the United States - Switzerland 2.4 and 1.4. On the other hand, the dollar wage levels in the United Kingdom and Italy increased more moderately because of exchange rate developments.

It is a safe assumption that, by now, the differentials in nominal wages in some industries as between the United States and the Federal Republic of Germany or Switzerland have narrowed down sufficiently to be smaller than the differentials in labour productivity. The report shows that the ratio of United States export prices to those of its major competitors, after rising by 20% between 1953 and 1969, had fallen well below its 1953 level by the middle of 1973: in other words, United States export prices are now probably more competitive than at any time in the last twenty years.

Evolution of trade of developing countries

Following the upsurge in commodity prices and the continued strong demand for manufactures, the dollar value of exports of developing areas taken together increased by more than 12% in 1972, according to very preliminary estimates. It would seem, however, that the volume increase was of the order of 6 to 7% only, "a good but by no means outstanding performance".

As the global imports of the developing areas increased by about 14% in value, the apparent c.i.f.-f.o.b. trade balance of these areas combined appears to have shown a small surplus, for the first time since the Korean War. This surplus largely reflects the great diversity of the trading results of the various countries. The bulk of the increment in export earnings accrued to a relatively small number of countries, many of which, notably the oil exporters, were already in a strong balance-of-payments position. In these countries a rise in export earnings is not automatically followed by a commensurate increase in imports. Second, in a number of countries the abrupt increase in export earnings came quite unexpectedly. Severely hit by the recessionary tendencies of 1971, these countries trimmed their imports, which, given the usual time-lag, failed to respond promptly to the improvement in their external position. The ensuing involuntary accumulation of reserves, to the extent that it accrued in dollars or sterling, turned out to cause an asset loss for the countries concerned. Third, quite a large number of countries
continued to find themselves in an extremely exposed balance-of-payments position and had to curtail or even reduce their import bill even if their exports were doing better, or at least less badly, than previously.

For the coming months, the report foresees a substantial increase in the import demand of developing areas.

**Eastern trading area**

In 1972 the foreign trade of the Eastern trading area showed a much faster increase in imports (+22% in current dollars) than in exports (+18½%).

The growth of imports originating within the area was less rapid than that of imports from the rest of the world, due to the sharp rise in imports from developed market economies.

The strong rise (+40% in current dollars) of imports into the Soviet Union from developed market economies was partly attributable to a sharp increase in imports of grain. Two-fifths of the increment in imports by the Soviet Union was accounted for by a substantial increase in imports of other products, in particular machinery and industrial consumer goods.

Imports from developed market economies into Poland and Romania increased by 60% and 30% respectively.

The report examines the causes and the nature of the instability of Soviet grain output. The steady rise in Soviet consumption of wheat flour, and rapidly growing requirements for feed grain, suggest that any coincidence of adverse weather conditions in several of the major grain growing areas of the Soviet Union, as occurred in 1972, could again lead in any of the coming years to large import requirements.

The report underlines that the Eastern trading area's export surplus in petroleum and petroleum products declined in 1972 for the second consecutive year due to the growing difficulties of maintaining an adequate expansion of production.

China's imports from developed market economies increased by 13½% in current dollars in 1972. Exports to those countries increased more sharply, by 37%.
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aIncluding fuels and non-ferrous metals.

Note: For sources and methods, see Appendix to International Trade - 1972.