THE COSTLY TRUTH ABOUT AUTO IMPORT QUOTAS

Imports into the U.S. of foreign automobiles, mainly from Japan, have been restricted since April 1981 by a so-called "voluntary restraint agreement." The quotas were imposed in response to pleas by the U.S. auto industry that it needed time to grow strong enough to compete with the imports on the free market. The quotas have not come cheap. Last year alone, it is estimated that Americans paid an extra $5 billion because of the import limits. At the same time, the U.S. auto industry had its best sales year since 1979--earning a record $10 billion profit.

The import restrictions are due to expire at the end of this March. The United Autoworkers Union, Chrysler and Ford want the quotas continued. General Motors, on the other hand, opposes extension, and the Reagan Administration seems to be leaning in this direction. Were the quotas to be removed, the winner would be the U.S. consumer. Winning too would be the U.S. auto industry, which would become more competitive.

The "voluntary" limit on cars imported from Japan was negotiated by the Reagan Administration at the urging of the then-ailing auto industry. From 1981 through 1983 the Japanese were allowed to ship 1.68 million cars annually to the U.S.; last year the ceiling was 1.85 million. By restricting the number of imported cars, Washington made it possible for the auto companies to raise prices without fear of losing business to less expensive competitors. Wharton Econometrics calculates that the average price per new car has risen by $2,600 since the market restrictions were imposed. Brookings Institution economist Robert Crandall estimates that $400 of this price hike per U.S.-made car was possible only because quotas reduced competition. With 1984 sales of nearly 8 million U.S. cars, the quotas took $3.2 billion out of the pockets of consumers and gave it to the auto industry. Crandall further estimates that the low supply of imported cars mandated by the quotas added $1,000 to the pricetag of every Japanese car sold in the U.S., a total of $1.85 billion in extra consumer costs. The total 1984 bill for U.S. consumers due to auto trade restraints: $5 billion.

Some argue that quotas should be extended because the U.S. auto industry is still not economically sound. This is a strange argument.

The 8 million American-made cars sold in 1984 represent the best yearly sales since 1979. Ford showed a thumping 26 percent sales increase over 1983; Chrysler sales were up 17.3 percent; and General Motors rose 13.2 percent. Total industry profits jumped from an already record $6.1 billion in 1983 to $10 billion in 1984. And these record profits were achieved while selling 2 million fewer cars than in the record sales year of 1977. This means that the record profits were due to the higher prices charged as a result of import restrictions. It certainly is not a weak industry that can make more money by selling fewer products.

Others argue that quotas must be extended to allow U.S. automakers to become "competitive" with the Japanese. This is an old protectionist refrain, refuted by the facts. History shows that trade protection removes the incentives for companies to make the difficult decisions needed to become more cost competitive. It is doubtful, for example, that the recent wage settlements and executive bonuses at U.S. auto companies would have been quite as generous had quotas not protected U.S. automakers from the Japanese.

Currently, the Japanese can produce a subcompact car for around $2,000 less than the Americans. This is not due merely to less expensive Japanese labor. University of Michigan professor David Cole estimates that it takes 200 hours of labor to produce a U.S. car compared to 100 hours of labor per Japanese car. There is little indication that Chrysler or Ford, the companies seeking an extension of quotas, are narrowing this gap significantly. GM, on the other hand, which seeks repeal of the quotas, has taken a major step towards matching the Japanese. Its new $5 billion Saturn Corporation will compete head-to-head with Japanese small cars. GM plans to design the most efficient assembly line possible. At least one U.S. auto company seems to understand that bold, innovative moves are the key to successful competition, not trade protection and government favors.

Retaining auto quotas contributes to the dangerous trend towards trade protectionism. Currently the U.S. is negotiating with the Japanese to lower barriers to such U.S. goods as farm products and telecommunications equipment. The Administration is also seeking to open Japan's markets U.S. to services and to remove quotas against U.S. goods. Continuing the auto quotas could sabotage these efforts.

If auto quotas are extended, they threaten to become permanent. They would become a "tax" levied by automobile companies on the U.S. consumer. If the American auto industry is to be competitive, then competition must be allowed. Notes GM Chairman Roger B. Smith: "The discipline of worldwide competition...speeds up the pace of technological innovation and industrial modernization, which means growth and more and better jobs." The case is clear. Auto quotas should go.

Edward L. Hudgins, Ph.D.
Walker Fellow in Economics

For further information:

Robert W. Crandall, "Import Quotas and the Automobile Industry: The Costs of Protectionism," The Brookings Review, Summer 1984.
Roger B. Smith, "It's Time to End the Auto Quotas," The Washington Post, January 30, 1985, p. A19.
Edward Miller, "U.S. Car Makers Post Another Good Year," The Washington Post, January 5, 1985, p. F1.