THE ECONOMIC IMPACT OF RESTRAINTS
ON FOREIGN TRAVEL

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ON FOREIGN TRAVEL

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CHAPTER I

INTRODUCTION

The Travel Account in the U. S. Balance of Payments

On New Year's Day, 1968, President Johnson issued a statement calling for greatly increased efforts to reduce the deficit in the U. S. Balance of Payments. In this statement, the President called for restraints in four specific areas: direct investment abroad by U. S. firms, foreign lending by U. S. financial institutions, overseas expenditures by the Federal Government, and travel by U. S. citizens outside the Western Hemisphere.

Concerning international travel the President in this January 1 statement asked:

> ... the American people to defer for the next two years all nonessential travel outside the Western Hemisphere. (1)

The recurrent deficit of the U. S. Balance of Payments in the travel sector prompted the Administration's request for citizens to limit their travel overseas. Since the Federal Government began compiling statistics on travel to and from the United States (estimates since about 1870, annual figures since 1919) the United States has consistently registered an unfavorable balance in the Travel Account. The size of the annual U. S. travel deficit since 1960, as published by the U. S. Commerce Department is shown in Table I.

International travel expenditures, in essence, are imports of a

TABLE I

U. S. TRAVEL SURPLUS (+) OR DEFICIT (-) IN THE YEARS 1960-67
(IN MILLIONS OF DOLLARS)*

Year	Canada	Mexico	Other Western Hemisphere	Other Overseas	Transportation	Total
1960	+ 89	-157	-125	-638	-399	-1,230
1961	+ 24	-158	-118	-586	-397	-1,235
1962	- 87	-153	-123	-619	-462	-1,444
1963	-150	-159	- 89	-701	-497	-1,596
1964	-102	-148	- 86	-668	-495	-1,499
1965	-110	-150	- 88	-710	-555	-1,613
1966	- 92	-139	- 99	-754	-560	-1,644
1967	-495	-133	-102	-819	-595	-2,144

*Survey of Current Business. U. S. Department of Commerce, Vol. 40-48, #6, June 1960-68.

service to the people of a country and, as such, necessitate flows of monetary payments as would any other import or export. International travel is a significant item in world commerce today, accounting for $12.0 billion out of $165 billion of this world trade in 1966 (2). According to provisional estimates of the International Union of Official Travel Organizations (IUOTO), the world figures for receipts from international travel, excluding transportation, amounted to about $12.7 billion from 128 million arrivals in 1966 (3).

The travel sector aggregates different activities such as transportation, purchase of non-business imports by travelers and services en route such as hotel and food consumption abroad. It does not include business expenditures incurred while staying abroad such as the purchase or lease of real estate. The travel account reflects only one modest segment of a nation's current accounts, but it is traditionally reported separately and therefore attracts special attention instead of being considered just as one item in a larger balance.

An example of the interrelatedness of the travel sector with other trade items is its impact on the airline industry. During 1967, the "transportation deficit", which constitutes the excess of air fares paid to foreign flag carriers over the fares paid to U. S. flag carriers in international travel was $580 million. But in the same year foreign airlines purchased $921 million of U. S. manufactured equipment. Along with these purchases, European airlines spent $192 million on staff, advertising, airport charges and commissions in this country (4).

Boeing Aircraft projected that a two year reduction of U. S. travel overseas would mean a loss of $391 million in aircraft sales to foreign carriers. Also there would be a $205 million loss in sales to U. S. flag carriers (5).

The total net passenger ticket sales in the U. S. of 17 European airlines during the period 1946-66 was $2,079 million. In the same period these airlines purchased $2,572 million in aircraft engines and spare parts, for a favorable trade balance to the U. S. of $493 million (6). During the two decades, these airlines further spent $1,640 million on promotion, advertising, and rental of facilities in the U. S. (7). Thus, these airlines spent $2.1 billion more in the U. S. than they earned in passenger ticket sales in dollars during this twenty year period.

The problem of interrelated factors in the Balance of Payments is also aggravated by insufficient data with which to estimate, with any degree of accuracy, the net magnitudes of the transfers attributable to the travel sector.

Methodology

Even though international travel is becoming an increasingly more important aspect, accounting for over 7% of world trade, there is still a lack of reliable data available which would enable us to carry out a statistically relevant analysis. Due to the lack of sufficient data we will analyse the travel sector and the administrative proposals by looking at some of the factors affecting international travel. The greater part of the quantitative data concerning international travel is found in the Commerce Department's "Surveys of Current Business" (June issues since 1956), the Organization for Economic Co-operation and Development's Tourism in OECD Member Countries (annual), and the

House Ways and Means Committee Hearings on the Administrative proposals on international travel held in February 1968.

International travel statistics suffer not only in their incompleteness, but also, in the nonuniformity of coverage and tabulation by the individual countries which makes comparisons difficult. Statistics in the travel area are almost nonexistent in most of the world outside Europe and North America. But even in the developed countries the data are inadequate in both figures for volume of travelers and in the amount of receipts and expenditures.

International arrivals are either recorded at the frontier or in all or some types of accommodations. Frontier counts prove satisfactory in isolated countries (Japan, Britain, and to some extent, the U. S.). In Europe, due to the close proximity of the countries, there arises the problem of day excursionists or commuting workers who may cross national borders. A figure based on frontier crossings inflates the extent of foreign travel (Denmark, West Germany, Sweden, France, Spain). Other European countries use hotel records (Holland, Switzerland, Luxembourg, Austria) to tabulate foreign arrivals. In this case the statistics are not always collected for the same categories of accommodations. Some countries only keep records of arrivals in classified hotels whereas others also include all or some of the "additional accommodations" (youth hostels, tent camps, rooms in private homes, etc.). The statistics collected by the various countries through these systems are not easily comparable. When different sources are used, disparity may result.

The figures for receipts and expenditures also call for reservations as to their uniformity. Some countries arrive at these figures by estimates based mainly on sample surveys whereas others compile them on the basis of bank returns.

In many countries bank records are the main, even sole, supplier of data on the receipts and expenditures of the travel accounts. But bank records are not always able to segregate payments for international travel. They also fail to account for the amount of national currency spent abroad which is reimported into the country of origin by foreign tourists. Typically, estimates by bank records are on the low side and this is especially true where there are travel restraints in effect. We will consider the problems associated with travel restraints in Chapter III when we analyse the Administrative proposals and travel restraints in general.

Estimates based on a sampling procedure tend to be more accurate than relying on bank records to determine the receipts and expenditures of international travelers. The sampling technique requires a fairly large sample, so as to eliminate errors due to the variability of expenditures by individual tourists. The U. S. follows this method which is carried out by the Balance of Payments division of the Commerce Department. The division distributes between 20 and 30 thousand questionnaires to returning citizens, but only about 30% are returned and the Department of Commerce admits these may be off by as much as 10%.

A Committee appointed by the Budget Bureau in 1965 (8) to review the balance of payments statistics found the rate of return too low to inspire confidence without a systematic sampling of the nature of the non-response segment of the travelers. The Committee recommended a complete overhauling of the Commerce Department's statistical research along with the acquisition of data processing equipment and more staff. The data on border crossings were found to be inadequate and the Committee found "serious shortcomings" in the Mexican border figures.

The Interim Report of Working Party I of the President's Industry-Government Special Task Force on travel stated:

> It was the concensus of members working on statistical material that the statistics in the travel field, especially from the U. S. Government, leave a great deal to be desired. Major decisions of national policy are being made on the basis of statistics that expert observers believe to have a high degree of error ... the samples taken by the Department of Commerce for calculating the inbound and outbound volume of travel expenditures from which the so called "travel deficit" is derived are regarded by your Working Party as inadequate, neither well balanced nor large enough, suffering from undue time lag, and using antiquated sampling and tabulating methods. (9)

Plan of Study

To examine the probable effects of the Administration's proposals to curtail foreign travel we shall first examine some of the factors influencing the level of international travel. We will be especially interested in the influence of income levels, the price of foreign travel, and the important role of transportation costs on foreign travel. Then we can analyse the various techniques of interference with a free travel market. The British example will give us some insight into the effectiveness of travel controls in an advanced country. We can then review the Administration's proposals against this framework as to their possible effect on reducing foreign travel expenditures.

CHAPTER II

THE TRAVEL ECONOMY

Travel is as old as humanity, but the concept of a travel industry developed only recently. The Odyssey is a fascinating report of world travels and the intellectual impact of European scholars taking the "Grand Tour" (term first used in 1670) was important at that time; but modern travel arrangements had to wait for the development of railroads and steamships. In 1820 some 2,000 U. S. citizens traveled to Europe and by 1836 (the first year of steamship service on the Atlantic) this figure had increased to over 6,000. By 1841 an Englishman, Thomas Cook, had developed all-inclusive excursion tours which only the wealthy could afford. World-wide mass travel is a modern phenomenon due as much to the automobile and the jet plane as to the rising incomes of the middle class in an industrialized society.

Domestic Travel

In nearly every industrial country, domestic travel accounts for the bulk of travel expenditures. Some 70-80% of total world expenditures on tourism is spent by people on business or vacation travel within their own country. The relative significance of domestic travel depends on the size of the country. In the U. S., 117.5 million citizens spent $22.93 billion on domestic travel in 1966, as compared with the 3 million U. S. travelers spending $2.7 billion on international travel in the same period (10).

TABLE II

DISTANCE OF TRIPS TAKEN BY U. S. CITIZENS IN 1963*

(Numbers in millions. Based on interviews with nationwide probability sample of about 6,000 households concerning all trips taken between January 1 and December 31, 1963.)

Distance	Trips		Travelers	
	Number	Percent	Number	Percent
Total	257	100	487	100
Under 100 miles	119	46	224	46
100 to 199 miles	73	28	141	29
200 to 499 miles	41	16	78	16
500 or more miles	19	8	34	7
Outside the U. S.	5	2	10	2

*Source: Dept. of Commerce, Bureau of the Census, 1963 Census of Transportation, Vol. I, Transportation Survey.

"International travel" statistics may give a misleading impression when we think of the international traveler as a world globetrotter. The bulk of international travel consists of short-term border crossings by neighbors. In small nations any trip of some consequence may cross frontiers, but even in the U. S. the majority of international travel expenditures (35% of total in 1967) were concentrated in neighboring Canada ($1,070 million) and Mexico ($590 million). At the same time U. S. travelers spent $243 million in the nearby West Indies (11).

The greater part of the localized international travel transactions take place in North America and Western Europe where members of the Organization for Economic Co-operation and Development account for 73%

(9.25 million) of international travel in 1966 ($12,700 million) (12). Thus countries involving less than one-fifth of the world's population are mainly involved in international travel. The OECD Member countries also accounted for 50% of the expenditures in nonmember countries (40% from the U. S. alone) (13). The high correlation of national income and foreign travel is illustrated in a 1965 study by the International Union of Official Travel Organizations showing that only twelve of the OECD countries accounted for the bulk of world travel.

TABLE III

THE PRINCIPAL COUNTRIES OF ORIGIN IN FOREIGN TRAVEL DURING 1965*

Country of Origin	Number of foreign travelers (thousands)**	Number of foreign travelers who go overseas (thousands)**
USA	21,689	9,763
Germany	21,637	389
France	9,966	474
United Kingdom	7,528	883
Canada	6,671	871
Netherlands	4,075	98
Belgium/Lux	3,787	50
Italy	3,139	153
Switzerland	2,079	95
Austria	2,079	41
Sweden	1,430	60
Denmark	1,366	30
Total	85,566	12,912

*Travel Agent, Vol. 71, #5, Jan. 29, 1968, page 8.

**Data are for each individual arrival. The data have not been adjusted for type of stay and repeated trips.

As can be seen by Table III, most of the international tourist traffic originated by Europeans stayed in Europe. While the U. S. and Germany generated almost equal numbers of international travelers, the U. S. sent 45% of its travelers outside North America while Germany sent only 1.8% outside Europe. In comparison Canada sent 13.1% and Great Britain 11.7% of its citizens undertaking foreign travel outside their regional areas. The higher disposable income of the U. S. accounts for its high overseas travel.

Income Elasticity of Foreign Travel

In the countries where national income is highest, international travel expenditures have tended to increase more quickly than private disposable income in the period 1956-65. In this period, Germany's travel expenditures abroad increased nearly three and a half times more than private disposable income. In France, Belgium, the Netherlands, and Sweden the increase was between two and a half and three times more rapid. In the U. S., the United Kingdom, Switzerland, and Canada it was less than twice as much. See Table IV.

In a comparison of the world figures for growth rates of international tourist expenditures with national incomes from 1958 through 1966, we also find a comparable pattern. Over the last decade the former has increased on average at twice the rate of the latter: at 12% and 6% compound respectively (Table V).

On this basis, it appears that since 1958 every one per cent rise in world national income has been accompanied by an increase in international travel expenditure of between 1.5 and 2 per cent.

TABLE IV

THE PROPENSITY TO SPEND ABROAD ON FOREIGN TRAVEL IN SELECTED COUNTRIES DURING THE PERIOD 1956 - 1965*

Country	Increase 1956-65 Disposable Income %	Increase 1956-65 Tourist Expend- iture Abroad %	Tourist expend- iture Abroad As Percentage of Disposable Income 1956	1965	Propensity to Spend Abroad
Germany	+121	+410	0.8	1.8	3.4
France	+141	+409	0.7	1.4	2.9
Belgium	+ 69	+186	1.3	2.3	2.7
Netherlands	+115	+298	1.3	2.4	2.6
Sweden	+ 87	+241	1.0	1.7	2.5
United Kingdom	+ 70	+125	0.9	1.2	1.8
United States	+ 95	+ 91	0.4	0.5	1.5
Switzerland	+104	+139	1.8	2.1	1.3
Canada	+ 74	+ 56	0.8	2.4	2.2

Note: The propensity to spend abroad is the ratio between the rate of increase in tourist expenditure abroad and the rate of increase in disposable income in the country concerned.

The base year of 1966 is used in calculating the Disposable Income and Tourist Expenditure Abroad percentage increases.

*Source: Tourism in OECD Member Countries 1967, pg. 20.

TABLE V

TOTAL WORLD VOLUME OF INTERNATIONAL TOURIST EXPENDITURE AND ITS RELATION TO NATIONAL INCOMES AND MERCHANDISE EXPORTS

Year	Tourist Expenditure Billion $	Tourist Expenditure %	National Incomes
1958	5,460	100	100
1959	5,852	107	107
1960	6,832	125	111
1961	7,280	134	116
1962	8,008	147	122
1963	8,820	162	129
1964	10,164	186	135
1965	11,620	213	142
1966	12,992	238	149

*Source: Lloyd's Bank Review, New Series #85, July 7, 1967, p. 30.

Price Elasticity of Foreign Travel

What is the effect of price changes on travel expenditures? We need to distinguish carefully between two different though related problems. We shall first examine the impact of price changes in one country on travel expenditures in this country. Then we want to consider a change in the cost of travel for all foreign travel and its possible consequences. A study by Andreas Gerakis (*) presents the hypothesis that tourist receipts are responsive to relative price changes, particularly those which occur as a result of changes in exchange rates. He argues that there is extensive substitution between the country undertaking the exchange reform (either up or down) and neighboring countries. He analyses devaluations in France, Spain, Canada, and Yugoslavia, and the revaluations in West Germany, Finland, and the Netherlands during the ten years 1954-63.

TABLE VI

APPARENT ELASTICITY OF TOURIST RECEIPTS OF SEVEN DEVALUING AND REVALUING COUNTRIES DURING THE YEARS 1954 - 1963*

Country of Exchange Reform	Percentage Change in Relative Prices	Percentage Change in Tourist Receipts	Apparent Elasticity of Tourist Receipts
Devaluers			
France	- 9.9	+ 41.5	4.2
Spain	-16.2	+111.5	6.9
Canada	- 5.1	+ 15.1	3.0
Yugoslavia	-32.4	+101.7	3.1
Revaluers			
Finland	+12.6	- 9.1	0.7
Germany, W.	+ 5.2	- 8.0	1.5
Netherlands	+ 2.4	- 8.0	3.3

*Source: IMF Staff Papers, Vol. XII, #3, Nov. 1965, pg. 365.

As shown in Table VI, the devaluing countries experienced substantial gains in tourist receipts with the elasticity of receipts ranging from 3.0 to 6.9. The revaluers, on the other hand, experienced an elasticity range of 0.7 to 3.3. Gerakis points out, however, that the countries studied were favorably situated on the main arteries of international tourism where the possibilities of substitution are considerable. As illustrated by previous data, few countries outside the European or North American areas could expect exchange reforms to have similar effects on their tourist receipts. The case of Finland in Table VI is significant. Finland is not a main target of foreign travel and only people with a specific objective go to this country. The demand for travel to Finland is therefore highly price-inelastic.

Beside the significant effect on tourism of an exchange devaluation, there are more limited pricing measures a government can enact to change the demand for tourism in its country. Most major tourist countries in Europe have acted to stimulate tourism by keeping transportation and hotel prices low. These policies have been carried out through subsidies, loans or guarantee of loans, and interest bonus and other tax concessions to the tourist industry. Some other measures include substantial discounts by nationalized railroads to foreigners (Italy), or gasoline concessions (Italy and until late 1963 in France), or again, the remission of purchase taxes on articles bought with payment in foreign travelers checks (Britain, France). Due to the lack of data concerning these measures it is difficult to analyse their actual effect on tourist expenditures.

In our examination of the income effect on foreign travel we not only discovered considerable income elasticity but we also noted a wide disparity of impact in different countries (see Table IV). It is not possible to isolate with certainty all the influences which determine foreign travel in addition to changes in income, but the impact of overall price changes on trips abroad must be studied. To what extent will travel decisions be influenced by the cost of a trip?

We have noted already that the bulk of all travel is limited to short distances and that longer trips have become popular only in recent years. The reason for this development is twofold: Transportation costs have dropped sharply and the time spent en route to distant destinations has been cut spectacularly by the jet-airplane. The relative importance of these two factors can not be estimated since they developed simultaneously. We can, however, set up a framework that will help us in understanding the demand and supply of travel services.

Not all travelers will react to a price change in the same manner. In small, crowded countries most demand for travel may be directed abroad and the only substitute for a foreign trip will be to stay at home. Such a lack of alternative will render travel relatively price inelastic. A large nation may be able to substitute domestic travel for trips abroad. In this case the elasticity effect of travel to alternate areas that was observed by Gerakis may well hold.

An estimate of price elasticity even for one country is made more difficult by the obvious fact that travel decisions are made for many different motives. Businessmen decide their trips on the basis of the needs of their firm: any small difference in the cost of such a trip will probably not be the determining factor in deciding if the trip is to be taken. In contrast, an immigrant with a low income can make a trip home only after he has saved the necessary funds. A price increase to people in this category will likely force postponement and cancellation of many travel plans. The different impacts of a price change on various groups is a result of travel not being a homogeneous product.

We can break down those interested in going abroad into three categories differentiated by income level: the high income group buys luxury travel, the low income group is mainly concerned with traveling at the minimum cost, and a middle income group whose travel plans are more flexible. High income travelers include most businessmen and others whose travel costs are not paid from their own funds. Their demand for travel may be assumed to be highly inelastic. The low income category includes students and foreign born. Their travel demand is probably price elastic since many would not be able to go when the cost exceeds their modes and savings. The middle income group includes many travelers who buy package tours for vacation travel. The demand of this group can easily be switched to other forms of activity or areas of travel if the cost of a trip were to increase. This is especially so as travel by tours is not only satisfied but created by the seller of the service, the travel agent. Even with unfavorable price developments the agent will do whatever possible to avoid a trend away from foreign travel, his main source of income.

The result of this discussion can now be shown graphically. Figure 1 uses the same scale throughout showing the demand for each income category separately and in aggregate form. This analysis will be for price changes in the long run.

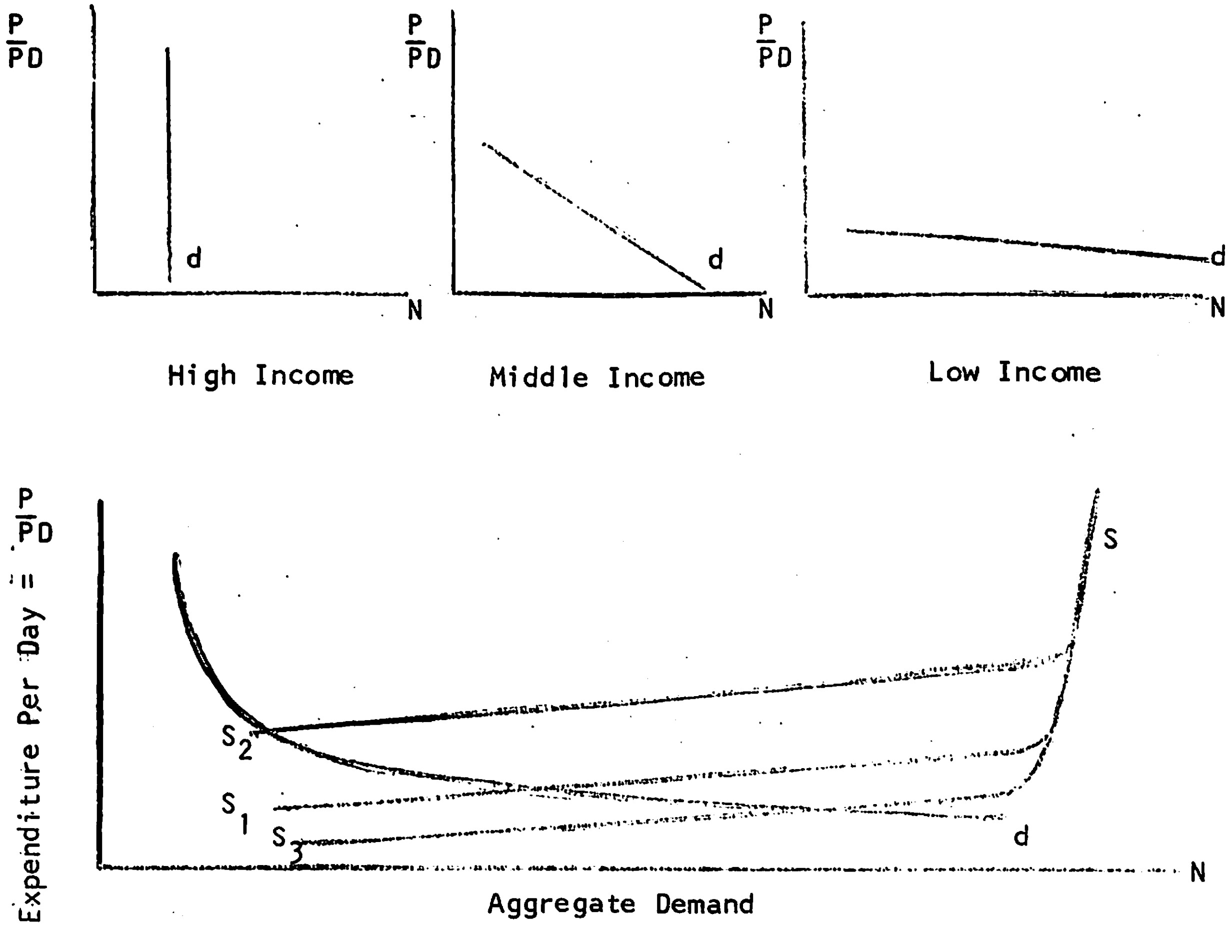

Figure 1. Demand and Supply in the Travel Market.

The travel industry has high fixed costs in the short run making it desirable for suppliers to try and maintain capacity use of their existing facilities. Beyond this capacity no price increase will cause a significant rise in the supply. The actual location of the supply curve is determined by variable and marginal cost which are assumed to be close together. A significant shift of this curve up or down will eliminate or permit the travel by the poor without much impact on other groups of travelers. The apparent ease with which the large number of middle income vacationers can be switched to other activities is probably nullified by the efforts of the travel industry in promoting demand in its packaged tours.

The Role of Transportation Costs

Changing transportation costs have a strong impact on trans-Atlantic traffic. The first major breakthrough came in the 1949-50 winter with the introduction of a 10-20% reduction in off-season rates by the airlines. A year later, the steamship companies followed suit, granting discounts varying between 5 and 20%. In April of 1952 the airlines inaugurated tourist class which was 32% lower than the first class fare. In that year east-bound air traffic rose 35% and sea traffic rose 21%. During the ensuing years, the number of travelers carried grew at a somewhat slower rate, but they increased another 15% subsequent to the inauguration by the airlines in April 1958 of economy class, which was approximately 20% cheaper than the tourist fare. From the time it was initiated, economy fare became the most fully utilized of any type of air transportation across the Atlantic.

This trend in lower air fares can be seen in Figure 2. Since 1946, the average fare per passenger mile has gone down from 8.31 cents to 5.17 cents, a drop of 38%.

Reduced air fares make it possible for more people of modest means to travel abroad. Increased travel by these lower income groups has decreased the average expenditure on trips to Europe since 1956 as shown in Figure 3.

Part of the reduction in total expenditures is due to the increased use of reduced excursion and charter fares for 2-3 week tours. These package tours have suited the paid vacation time of American families. The reduced cost of air travel has brought a trip to Europe not only within the budget of the middle class but the speed of the ocean crossing makes it possible to take a trip during the annual vacation time.

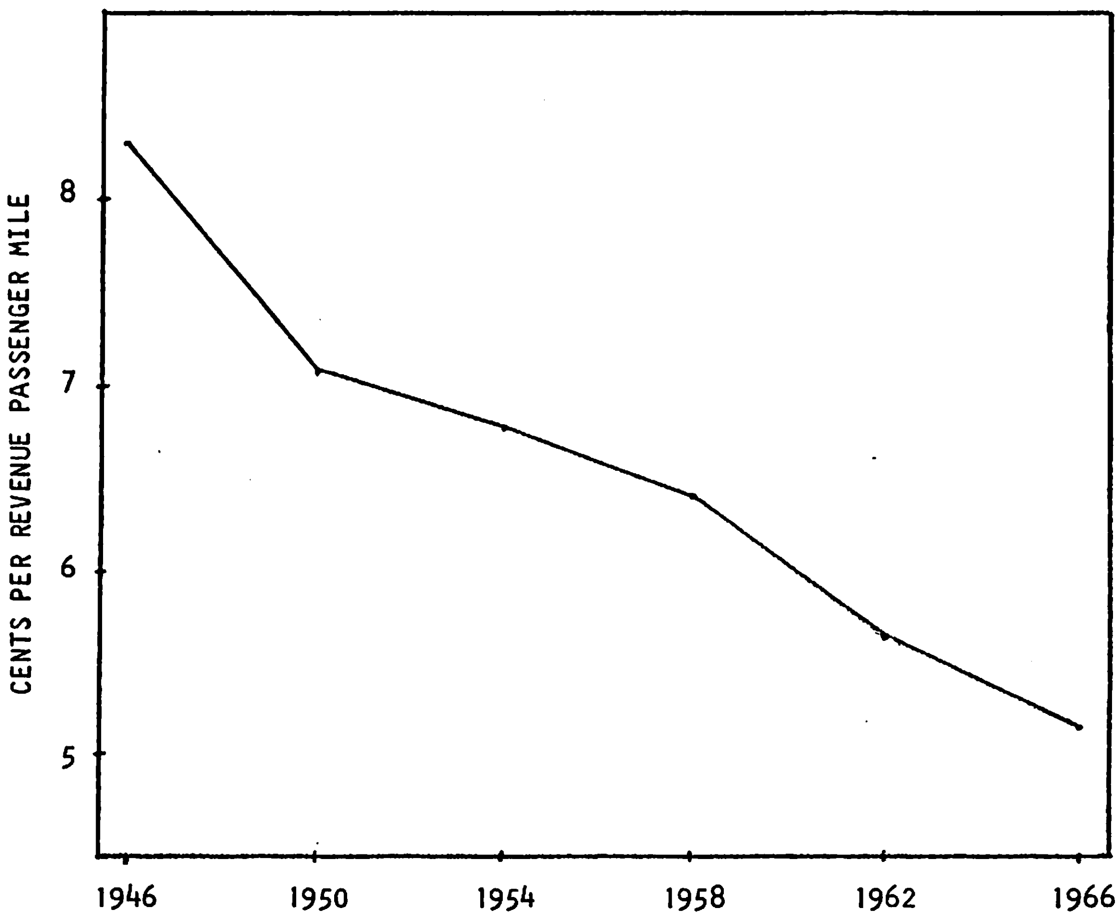

Figure 2. Downward Trend of Revenue Passenger Mile Yields for U. S. Scheduled Airlines in the Period 1946-1966.*

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*Source: The Promise of International Air Commerce, Air Transportation Association of America, p. 10.

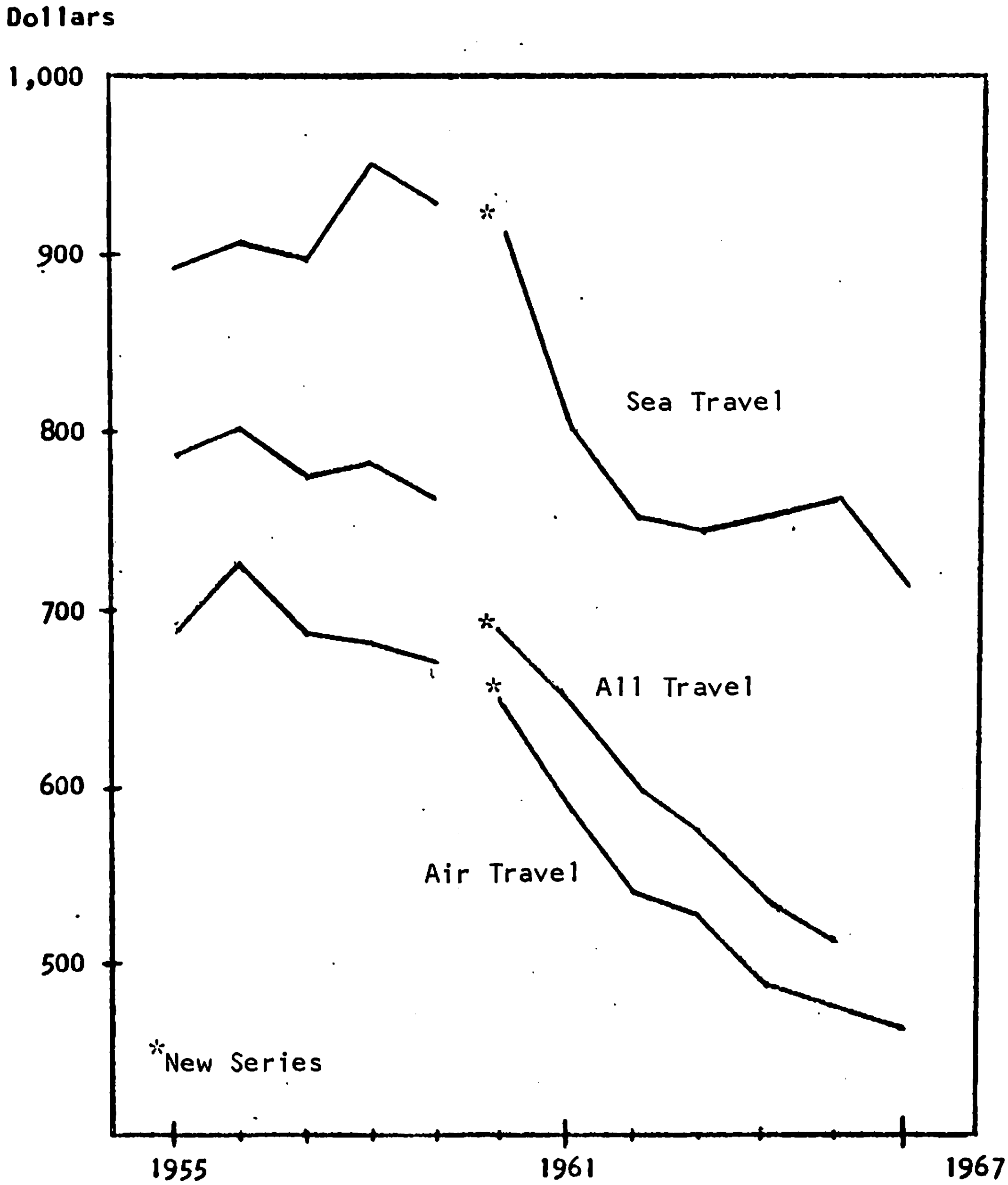

Figure 3. Average Expenditure Per Trip of U. S. Travelers to the European and Mediterrean Area During the Period 1955-1966.*

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*Source: Survey of Current Business, Vol. 47, #6, pg. 13.

The reduction in the cost of air transportation becomes even more significant when we contrast it with the rapidly rising level of consumer prices as shown in Figure 4.

As shown in Figure 4, the average cost of international air travel today is 27% below the cost in 1950. By comparison, the U. S. consumer price index is 31% above the 1950 figure. This downward trend in prices (along with shorter periods of travel time) accounts for the increased use of air transport from just over 50% in 1950 to 83% in 1965.

Other Factors Influencing American Travel Abroad

Even when a person has the means and the time for travel, it does not necessarily follow that he will travel. Ethnic background, tourist facilities, political crises, and special events are additional determinants of travel. Many of our overseas travelers are foreign born (18% in 1967) and much of our travel is directed to countries where a large percentage of our immigration originated (Ireland, Italy, Germany, and Great Britain). We not only have strong family ties with these countries but business and cultural ties as well. These countries are also best equipped in the type of facilities such as hotel, restaurant, entertainment, and historic sights that create tourist traffic.

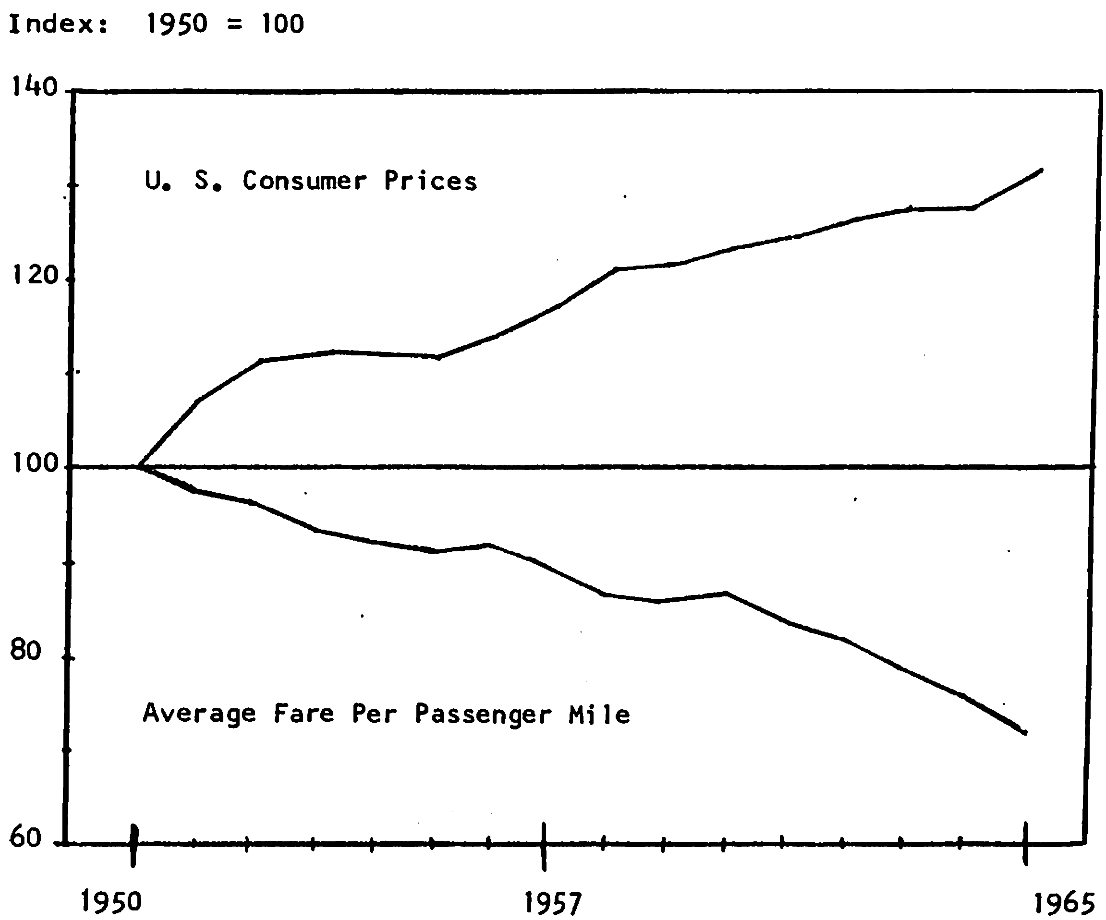

Figure 4. Comparative Price Changes of U. S. Flag Airline Rates Vs. Consumer Prices During the Period 1950-1965.*

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*Source: The Promise of International Air Commerce, Air Transportation Association of America, pg. 11.

CHAPTER III

TRAVEL RESTRAINTS

History

Travel restrictions have always been quite common in underdeveloped countries. Only in the chaos of the Great Depression in the 30's were they instituted in the developed industrial countries of Europe. Through the early 1950's travel allowances were the rule (with the exception of Portugal, Switzerland, and Belgium). The amounts granted to would-be travelers varied greatly from one country to another and depended partly on destination. Somewhat more liberal travel allowances were negotiated on a strictly bilateral basis, for example, between Britain and Sweden. On the other hand, there were no automatic travel allowances at all in Greece, Turkey, and Iceland, nor in any of the Eastern European countries; any application for currency had to be fully documented.

The turning point in Europe came with the setting up of the European Payments Union in 1950. The aim of the EPU was to replace postwar bilateral trade with multilateral trade and payments. In tourism this goal was reached through gradual uniform increases in travel allowances and elimination of travel restrictions in most Western European countries. However, the rest of the world remains even today under the harness of exchange control and other restrictive practices.

Forms of Travel Restraints

Travel restrictions are used by governments as means to limit expenditures abroad. These restrictions can take several forms, which are designed not to raise revenue but to limit foreign expenditures by limiting international travel.

The simplest, and most effective way to restrict foreign travel is a law ordering citizens to obtain a government permit before leaving the country. The government, in this way, can control the movement of its people and regulate foreign expenditures to what it considers essential travel.

Indirect monetary controls are more common. A "head tax" is the easiest to administer, as a flat rate is charged on each citizen when leaving the country. The head tax can be in the form of a visa tax, exit tax, or embarkation tax. A ticket tax is a tax on the purchase of transportation tickets and penalizes those who travel furthest away from the home country. In some instances ticket taxes are really "user taxes" with the receipts earmarked for transportation facilities. Custom measures can also be used to reduce the amount of goods brought back into a country and thus reduce the amount of foreign expenditure.

The common monetary control is a limit of funds in any form, that can be taken out of the country. These amounts are entered into the passport and can only be sold by approved banks. Any excess is smuggling. Another form of monetary control is the expenditure tax. It can either be based on the total amount of currency taken out of the country, expenditure per day, or on the income of the travelers.

Some travel restrictions in force January 1, 1968 in the developed countries of the world are shown in Table VII.

TABLE VII

FOREIGN TRAVEL RESTRAINTS ON RESIDENTS OF SELECTED INDUSTRIAL COUNTRIES, JANUARY 1, 1968*

Country	Allowance in foreign exchange[1]	Additional allowance per journey in own currency
Italy	$800 (500,000 lire) per journey	$80 (50,000 lire)
Japan	$500 per journey	$56 (20,000 yen)
Netherlands	Unlimited ($1,243 granted automatically and additional amounts granted on request)	Unlimited
Sweden	Unlimited ($1,160 granted automatically and additional amounts on request)	Unlimited
United Kingdom	$120 (50 pounds)	$36 (15 pounds)

*Source: <u>House Ways and Means Committee Hearings</u>, 90th Cong., 2nd Sess., p. 270.

[1]When the allowance is limited, travel tickets (return and circular) can generally be paid for without reducing the travel allowance.

More stringent restrictions are practiced in the underdeveloped and communist bloc countries. In the Philippines, for example, the foreign currency allowance for travel is limited and a head tax graduated by distance is levied. In the Soviet bloc countries only small tourist allowances are granted, and then, only to politically reliable citizens.

Due to recurrent deficits in the balance of payments the British government in 1966 instituted travel restrictions of 50 pounds ($120) which is presently the most severe restraint of the major industrial countries. The British example gives us some insight into the effectiveness of travel controls in an advanced industrial nation where the people can afford to travel.

When the restrictions were introduced the British government estimated they might save up to 50 million pounds of foreign exchange a year. Before 1966 the British had been increasing their spending on overseas trips by about 25 million pounds each year. In 1966 the rise slowed to 11 million pounds (14). As shown in Figure 5 this was the first departure from the normal rise in expenditures since 1962.

But the reduction in expenditures could not have been due to the £50 curb, which began only during November 1966. The general slowdown in the British economy at that time appears to be a more plausible cause for the trend. On closer inspection it was found that the greatest decline in overseas trips were in the low-cost tours that are well within the £50 limit (15). This confirms the statement that the level of income has a great effect on foreign travel. The total saving of foreign exchange attributable to the £50 limit was estimated at £20 million a year. Not included in the £20 million are allowances for

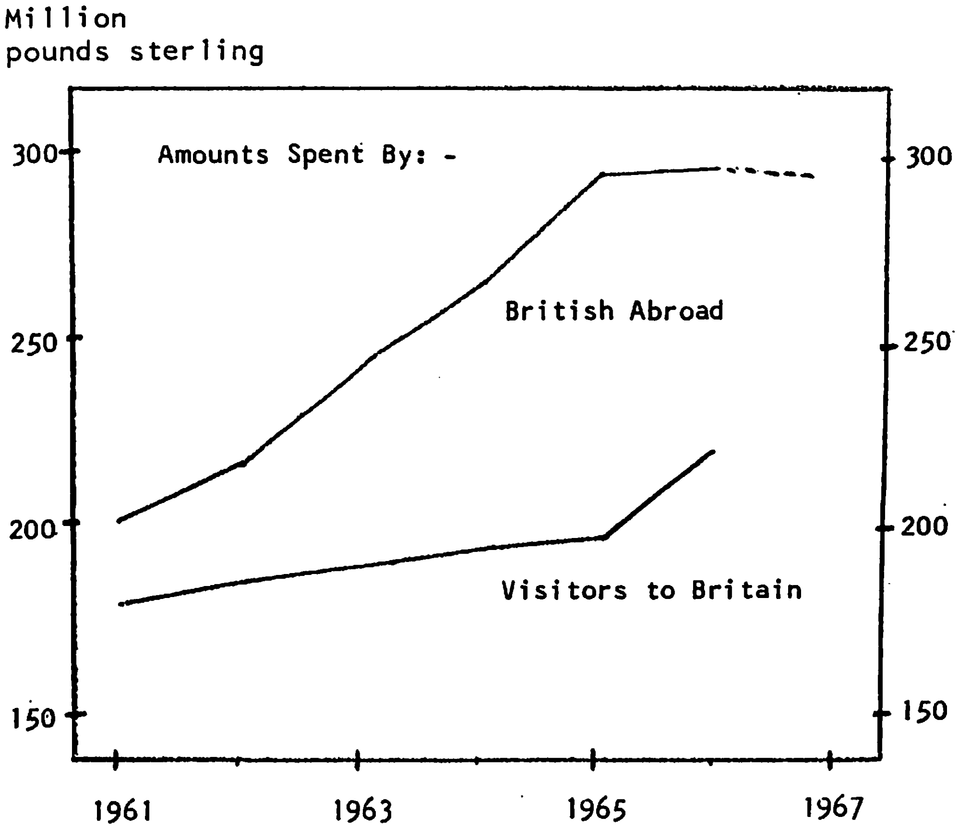

Figure 5. Relation of Spending on Foreign Travel Expenditures by the British to Expenditures of Visitors to Britain in the Years 1961-1966.*

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*Source: The Economist, New Series #85, March 16, 1968, pg. 83.

avoidance and evasion of the travel restriction. In 1967 the British increased their travel to American shores by 18%, no doubt spurred on by Expo 67 (16). The small allowance seems hardly sufficient for such an expensive trip.

Administration Proposals of 1968

In a message before the Joint Session of the Congress on January 17, 1968, the President of the United States presented a plea to reduce "nonessential travel" outside the Western Hemisphere in the following terms (18):

> ... we are hoping that we can reduce it (the travel deficit) by 500 million dollars without unduly penalizing the travel of teachers, students, business people who have essential and necessary travel, or people who have relatives abroad whom they want to see. (17)

The Treasury Department was directed by the President to formulate measures to carry out his request, and it presented its recommendations to the House Ways and Means Committee on February 5, 1968 with a four point proposal:

a) A reduction in the duty free allowance of travelers from $100 to $10 for U. S. residents returning from countries other than Mexico, Canada, and the Caribbean area.

b) A reduction in the gift exemption for parcels arriving by mail from $10 to $1.

c) A 5% ticket tax on the cost of air and (temporarily) steamship travel to points outside the Western Hemisphere.

d) A temporary (1968 and 1969 seasons) graduated tax on the expenditures of people traveling outside the Western Hemisphere. The first $7 per day expenditure would be exempt with the next $8 per day taxed at a 15% rate and the remainder over $15 per day taxed at a 30% rate. Students and business people staying abroad for more than 120 days would be exempt from the expenditure tax.

The Duty Free Allowance

The present tourist exemptions granted to returning U. S. residents permit the importation duty free of foreign acquisitions not exceeding a total retail value of $100 from any area or country (Virgin Islands excepted with $200 limit). The Administration's proposal would reduce the duty-free exemptions to $10 for U. S. residents returning to the U. S. from any place other than Canada, Mexico, and the Caribbean area. Foreign acquisitions accompanying the returning U. S. residents valued in excess of the $10 exemption would be dutiable at a flat 25% of the wholesale value, up to a $500 valuation. Articles exceeding $500 in value would be dutiable at the standard rates of duty.

During 1967, the total value of foreign acquisitions made by returning U. S. residents was estimated in excess of $362 million (19). Of this total, acquisitions from Canada, Mexico, and the Caribbean accounted for a little over $162 million, leaving approximately $200 million from other countries. Approximately $110 million was brought in by persons whose purchases totaled less than $100 per person, while approximately $90 million was brought in by persons whose purchases exceeded the present duty-free exemption.

The Treasury believed that the reduction of the duty-free exemption to $10 would result in a $50 million reduction in purchases (20) with $45 million coming from the persons now bringing in less than the $100 exemption and $5 million from persons who even now exceed the duty-free exemption.

In 1961 Congress reduced the amount of duty-free merchandise brought in by international travelers from $500 to $100 wholesale. The Department of Commerce reported that this reduction "had a definite influence in reducing the average outlays in Europe"(21). From the available data we can not ascertain if this was the case as there are other factors that had the effect of reducing expenditures.

Part of this decrease can be explained by an increased proportion of travelers who go by air. Air travelers, as we have seen in previous data, stay on the average a shorter period of time and spend less per trip than sea travelers. The increased air traffic has been accompanied by a decline in the use of first class air travel (with its 66 pound free baggage limit) and by an increased use of economy class (with only a 44 pound limit). Continued expansion of charter flights, with its low rates, has increased the share of lower income groups who travel.

Assuming that the reduction in the duty-free limit from $500 to $100 was actually successful in reducing expenditures, we must not jump to the conclusion that a reduction to $10 would have the same effect. Expenditures over $100 most likely include a large share of goods purchased abroad only because they are cheaper in the country of origin. If the normal duty is levied on these goods the price advantage will be eliminated and the same goods can be purchased at home more conveniently. The under $100 purchases, on the other hand, are generally more of a souvenir nature and purchased as gifts or momentos of the trip. In this case, the price considerations would be secondary as the duty on the low value of purchases would be small. This measure would not reduce expenditures at a proportionate rate and would only burden the Customs inspection procedures. It might also be mentioned that this proposal would be a direct violation of an agreement reached between OECD member countries in a Council meeting on July 20, 1965 which recommended to member governments that the minimum duty free allowance be $50 (22).

The Foreign Gift Provision

The second Customs proposal would reduce the $10 duty-free gift provision for articles arriving in the mail from abroad to $1. The $50 gift exemption for servicemen in combat areas would be retained. The Treasury claims that the elimination of the $10 gift exemption, and a more intensive processing by customs would result in a decline in the number of such parcels. Many such parcels are actually purchased by U. S. residents and sometimes should have been valued at more than $10. In order to minimize the increased customs workload resulting from the change, a flat 25% duty was proposed to be levied on noncommercial mail valued between $10 retail and $250 wholesale. A $2 charge to be levied on all mail valued at $10 or less retail. Articles valued at $1 or less would continue to be free of duty as it would be impractical to assess duty on such articles which comprised approximately 25 million parcels received in 1967. It is estimated that 55 million parcels arrived in the U. S. in 1967 (23). Of this 55 million total, an estimated 11 million parcels were gifts or purported gifts said to be valued at less than $10, 4 million were gifts valued at less than $50 from servicemen in combat areas, and 25 million were "flats" (periodicals, newspapers, samples, etc.). Of the remaining 15 million parcels duty was assessed on 1.6 million parcels. However, the Administration believes that approximately one-third of the 15 million parcels would have been dutiable if adequate manpower had been available to handle them properly. If the gift exemption were eliminated it is estimated 4 million parcels would be discouraged for a foreign expenditure curtailment of approximately $28 million. The application of a flat rate of duty to the remaining parcels, by simplifying Customs administrative tasks, would allow Customs to assess more parcels. The resulting efficiency, it is believed, would achieve an additional $12 million in duties and a reduction in foreign acquisitions by $40 million (24).

The total proposed saving of foreign exchange would be an estimated $60 million. To achieve this saving there would need to be an increase in the manpower and facilities which would cost an estimated $3.43 million (25). These measures may be quite beneficial but it is hard to see how these savings can be attained by a Customs office that is not able to enforce the present higher duty levels. The problem is apparently not the size of the gift exemption but it's abuse. Nothing prevents the customs office from managing its task more efficiently. If more personnel would result in much high tax collections the customs office should have taken the necessary steps to do so. No new law is required for the proper enforcement of existing laws.

While the travel tax consisted of four main parts, the major area of controversy concerned the two tax proposals. The taxes consisted of a 5% ticket tax and a temporary graduated tax on expenditures for travel outside the Western Hemisphere.

The 5% Ticket Tax

The 5% ticket tax is an extension of the present 5% ticket tax on the cost of domestic airline travel to cover international airline tickets purchased in the U. S. It also includes a temporary extension (through two high seasons) of the tax to cover the cost of ship travel to destinations outside the Western Hemisphere. The 5% tax originated in a 15% tax on all passenger tickets by air, rail, ship, and bus during World War II (26). At the end of the war the international ticket tax was removed and the domestic tax was reduced to 10%. In 1961 the domestic tax was removed from all but airline travel and this tax was reduced to the present 5%. This 5% tax was retained as an airline user charge for the federal airways system. The U. S. Government has a policy of long standing to discourage the unilateral imposition of user charges upon international operations. It was felt that without a co-ordinated approach each country might well establish charges wholly on the basis of ability to pay and without reference to costs fairly chargeable to the facilities being furnished. The 5% ticket tax would be a violation of this principle against unilateral action. The tax would be an easy one to administer; it would yield substantial revenue, if foreign travel is price-inelastic at the 5% level. In line with the earlier model demand would probably be elastic if the tax is high enough. If it is too low to make any difference it fails to save foreign exchange; if it is high enough to reflect the elasticity of the demand it would do two things: it would prevent the low income groups from going abroad contrary to the avowed intentions of the proposal, or it would divert departures through Canada or Mexico to avoid the tax.

The Expenditure Tax

When analysing the ticket tax it is best to view it in conjunction with the expenditure tax, as together they add to the overall increase in the cost of a trip. The expenditure tax was the major Administration proposal to reduce the "travel deficit" as it was intended to achieve the greatest saving in international payments. This measure was also the element most open to question as to its possible effects. The tax as proposed would have applied to the 1968 and 1969 travel seasons on expenditures in excess of $7 per day of travel — with the first $8 of the excess over \$7 taxed at a 15% rate and the remaining amount over \$15 per day at a 30% rate. Expenditures would not include the cost of transportation to and from the travelers foreign destination, as that would be covered under the 5% ticket tax. Exemptions to the tax would be limited to people going abroad for 120 days, or more, in connection with business or education.

The expenditure tax would be paid before departing in an amount equal to the tax the traveler expects to owe. He would file a statement with Customs indicating how much money and travelers checks he is taking with him and upon his return he would then file a formal tax return with the Internal Revenue Service within 60 days of his return home. One can only imagine the added confusion that would be a result of this proposal with the already chaotic conditions existing in the airports today at rush hours. The Administration estimates the added cost of administering the expenditure tax would be \$1.43 million for Customs and \$7.3 million for the IRS (27).

Our estimate of the effects of the travel tax will be based on the model for price elasticity of the demand for travel developed in Chapter II. Passport office statistics in Table VIII present some information concerning the occupations of applicants for passports. Unfortunately the evidence does not permit us to conclude the nature of foreign travel of the applicant. The businessman may be going abroad on business or he may be on a vacation trip. Many students are likely to be young people travelling with their parents but are classified as students because they are still in high school. The housewife category is completely amorphous which may account for the large number of women under this all-inclusive heading.

TABLE VIII

STATED OCCUPATIONS OF APPLICANTS FOR U. S. PASSPORTS DURING 1967*

Occupation	Applicants
Students	292,070
Retired	91,990
Clerk-Secretaries	67,620
Teachers	88,490
Independent Business and Professional Men	498,720
Religious	16,630
Housewives	304,270
Skilled Workers	93,140
Unskilled Workers	9,540

*Source: House Ways and Means Committee Hearings, (90th Cong., 2nd Sess.), pg. 975.

TABLE IX

STATED PURPOSE OF APPLICATIONS FOR U. S. PASSPORTS DURING 1967*

Travel Object	Applicants
Pleasure	670,880
Personal Reasons	638,790
Business	140,700
Education	61,207
Religion	7,750
Scientific	2,280
Health	2,720

*Source: House Ways and Means Committee Hearings, (90th Cong., 2nd Sess.), pg. 975.

The passport office also provides the figures in Table IX. They are no more enlightening than the previous table. Forty percent of the passport applicants simply refused to tell why they wanted to travel and they are grouped together under the heading "Personal Reasons." The large size of this residual item renders the data almost useless.

Table X shows the results of a survey of approximately 1% of U. S. overseas air travelers carried out by the New York Port Authority. We are are inclined to consider it far more reliable than the data provided by the passport office. The evidence gathered by the Port of New York Authority which is in charge of the New York airports was based on scientific sampling methods and presents the best available evidence. The relative share of the groups involved in travel is not completely inconsistent with the data presented by the department of commerce in the following discussion.

The high income group whose travel is sufficiently price inelastic not to be influenced by a travel tax includes the business people who constitute 24% of the travel to Europe and have the highest daily expenditure average ($32.50) (30). This group also spends the least time abroad of all the groups. The travel tax does not affect this group to any great extent as the businessmen will go where their business needs them. The other high income travelers are the tourists with incomes over $20,000 a year who constitute one-third of all overseas travel, but who account for one-half of all overseas expenditures on foriegn travel (31). The high income group is accustomed to traveling, and at its accustomed level of comfort. They will not alter their travel expenditures as they can either afford the tax or can circumvent the tax with funds in foreign banks. If not, they may shift their travels to nontaxed areas (Acapulco,

TABLE X

EXPENDITURE PROFILE OF U. S. TRAVELERS TO EUROPE ON SCHEDULED FLIGHTS (12 MONTH PERIOD ENDING APRIL 30, 1967) WITH RESPONSE OF TWO-THIRDS OF TOTAL*

Purpose of Trip	Number	%	Expenditures (thousands)	Avg. Expenditures	Avg. Trip Time in Days	Avg. Per Diem Expenditure
Business	1,610	30%	$1,319	$819	25.2	$32.50
Vacation	2,484	46	2,061	830	29.4	28.23
Visiting	867	16	438	515	33.7	15.28
Study	233	4	215	922	61.7	14.94
Other	201	4	155	711	52.7	14.63
Total	5,395	100%	$4,188	$766	31.1	$24.95

*Source: House Ways and Means Committee Hearings, (90th Cong., 2nd Sess.), pg. 756.

Bahamas) and spend the same as usual, which would not result in a significant foreign expenditure saving in this group.

The low income travelers whose plans can be altered by a tax are essentially foreign born citizens returning to visit family and friends. Travelers going to visit friends and relatives are estimated to be 18% of all travelers to Europe in 1967. As a group they spend less than $10 per day but stay over 50 days (28). The reason for the low daily expenditures is that they generally stay with friends and relatives while visiting. The travel taxes would not be a high deterent to this group, as the total tax would be about $45 (including the ticket tax) for about 5% average tax. This would not alter the demand of this group to any great extent.

Another element of the low income travelers, due to their low daily expenditures, is the student-teacher group which represents about 5% of the total travelers to Europe in 1967. About 20% of the students stay for year-long enrollment and would be exempt from the tax. The Council on International Educational Exchange estimates the U. S. teacher stays on an average of 35 days abroad and spends an average of $535 (29). But still, as in the case of the foreign born, the total tax would be 4-6% of total expenditures. The marginal increase in the cost of the trip would not deter many of this group as they go to Europe to study what is unique there and not found at home.

The middle class travelers are the majority taking a trip to Europe (45%) and go mainly with a package tour. The American Society of Travel Agents found this group spent an average of 26.8 days abroad with an average per diem expenditure of $27.36 (32). The Treasury Department estimated they spend 33 days and at a cost of $16.73 per day

(33) which is probably not as accurate due to the aggregating of too many lower income groups in this figure. Gateway Tours and Globus found in a survey spanning 4 years that 82% of their customers stayed in Europe between 15 and 21 days.

Expected Effects of the Travel Controls

If we use the ASTA figures we find the total tax load would be at least $162.00, which would result in an overall tax load of almost 15% to the cost of trips for this group. This would result in many in the middle income group deciding the added cost makes the trip too costly and would deter their taking the trip. But when buying package tours this group can be strongly influenced by the travel agent. In many cases the tour chosen is really the one "sold" by the travel agent. If the cost of a trip becomes too expensive due to a travel tax the agent can repackage the tour, making it a day shorter or he can steer the customer to tours in areas not affected by the tax. The result of the tax on this group would not be so much a reduction in foreign travel expenditures as a diverting to destinations not covered by the tax.

We must also realize the considerable problems of enforcement associated with travel controls in an advanced nation. After the President's plea on January 1, 1968 for a voluntary reduction in overseas travel a substantial increase occurred in passport applications in January and February 1968 before leveling off to the normal pattern in the following months of 1968. The foreign expenditures of these travelers also continued at the normal rate of growth of the previous post war years.

The U. S. experiment with prohibition in the 1920's seems to have shown that Americans may choose to evade regulations which they regard as unreasonable infringements on their personal life. Those with personal cash balances in Europe, or access to corporate cash overseas, or friends who can "loan" them the funds can escape paying the tax and continue to spend large sums on overseas travel. There can also arise black market situations whereby the unauthorized dealers supplement the foreign currency at a premium. For example, Italy in 1955 received $368 million in foreign tourist receipts but only $212 million passed through the banks, leaving about $160 million in unofficial transactions (34).

CHAPTER IV

SUMMARY AND CONCLUSION

The Administration on February 5, 1968 presented to the House Ways and Means Committee proposals to reduce the foreign exchange costs of Americans traveling abroad by $500 million. The basis for this request is found in the Travel Account which has consistently registered an unfavorable balance since the Federal government began compiling statistics on travel in 1919.

This spending on international travel is to a large extent a function of a few variables. The main factor is the ability of the people of a nation to afford travel. Foreign travel has been very income elastic, particularly in the advanced industrial nations of Europe and North America. Most "international travel" takesplace among neighboring countries. Only the people of the U. S. spend over $1 billion across the seas.

There is also evidence that the demand for travel is price elastic. The two major cost elements in a trip abroad are the transportation costs and expenditures in the country of destination. Of particular significance to U. S. overseas travel is the high elasticity of demand associated with the lowering of air transportation costs. Low cost group fares have put international travel in the reach of the middle income families in the United States.

A third factor contributing to expanding middle class travel in

Europe is the reduction of time enroute due to the rising speed of modern planes. It has made overseas trips practical even for short vacations. While total overseas travel expenditures have been climbing, the average expenditure per person has been declining due to shorter stays. Personal expenditures have also been reduced on a daily basis since lower income groups can make such trips.

Secretary Fowler in presenting the Treasury proposals stated the aim of the Administration proposals. He hoped to achieve a balance of payments savings with a minimum of trip cancellations. The Treasury expected to effect a $500 million saving based on the President's plea for reduced foreign travel along with two customs changes and two new tax measures. The Treasury estimated a $100 million saving based on the appeal of the President's request, but no such reduction materialized in 1968.

The Customs measures were expected to save a further $100 million. A reduction in the duty-free limit from $100. to $10. would save little foreign exchange since many purchases in this category are probably price inelastic. The duty on the low value of these purchases would have little effect. The second custom proposal would have reduced the $10. duty-free gift provision for gifts arriving from abroad to $1. This measure might have caused some saving but the effect would be due to better enforcement practices rather than the change in the limit.

The 5% ticket tax would have been an extension of the present 5% ticket tax on the cost of domestic airline travel to cover international airline tickets purchased in the U. S. A 5% ticket tax on foreign travel would have been easy to administer but would have been concentrated on low income travelers whom the Treasury did not want to prevent from going abroad. The expenditure tax was the major Administration proposal to reduce the "travel deficit." To get a true picture of the effects of the tax we must first disaggregate foreign travel into the travel groups with similar characteristics of travel demand. In doing so, it was found there were few reliable and consistent statistics in the breakdown of these groups for an empirical analysis. The analysis does indicate that the tax would be most effective with a group we did not want to prevent from traveling. It seems likely that the result of the price elasticity in this group would be a diversion rather than a reduction of expenditures on foreign travel. The result of the entire package of pnoposals would not have been as significant as anticipated by the Administration.

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