Session 4

SUMMARY

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COMMENTS

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One problem for many conferences like this one is theoretical and policy papers related to each other only after the manner of our waking and our dreaming lives, as Lord Keynes said in 1936 about the price-theory and monetary-theory sections of the textbooks of that day. Another problem is that authors may ride their own hobby-horses of the moment with only peripheral adaptation to the conference theme, leaving it to generalists and summarizers to make useful compounds of oil and water. In addition, we have a special problem this time because some of the papers were largely complete before the G-5 intervention of September 22-23, 1985 to bring the dollar down. And so, while I am glad to be here, I would prefer being here at some other time.

Perhaps I might begin by confessing a couple of my own biases, so that you know the points from which I am starting. These are three in number. (1) I think the recent destabilizing run-up of the U.S. dollar was caused by the combination of "supply side" fiscal looseness and "monetarist" monetary tightness. It would, I think, have corrected itself in some degree, perhaps even without great disorder, from some combination of lower interest rates and higher inflation in the U.S., higher interest rates and higher disinflation elsewhere, and a replay of the late 1960s, when the world became temporarily surfeited with "dollar overhang." (2) I think the U.S. trade imbalance is largely an old-fashioned microeconomic phenomenon. It results from uncompetitively high wage rates, uncompetitively high profit margins, uncompetitively low productivity growth rates, and uncompetitively low concern with product quality following a near-generation of "dollar-shortage" after 1945. It won't be solved until these matters are somehow resolved, unless of course the protectionists have their way. (3) My third bias is against "Pumping up demand" as the sovereign remedy for recessions. Pumping up demand, I fear, only makes "it" happen again—"it" being a price rise to re-create unemployment of the heels of whatever increased demand may have done to reduce it.

So much for Bronfenbrenner, and now for our papers. The first trio relates to industrial countries (other than Japan)—Professor Gordon on the U.S. and particularly the Reagan budget deficits, Professor Pollard on the U.K. and particularly its real-investment shortfall, and Professor Bruno on international stagflation.

I liked Professor Gordon's "double-hump" analysis of the current American situation, analogous to Sir John Hicks' analysis of the Great Depression of the 1930s. But I fear that Professor Gordon did not change my mind on the importance of the deficit in conjunction with the anti-inflation stance of the Federal Reserve. I too have been impressed with the case made by his Northwestern University colleague Robert Eisner for looking at the deficit not only relative to the GNP but also with allowance for the wealth effects of both inflation and high nominal interest rates upon the value of the government assets.

But I don't think that the international financial market participants have pondered Professor Eisner's essay, or that his analysis would in any case have great bearing on the day-to-day supply and demand for various currencies, American or otherwise. And incidentally, Professor Gordon also failed to convince me that Japan, in particular, was being fiscally tight, in view of its own deficits as proportions of either public spending or GNP. (What is his criterion of fiscal tightness?)

Toward the end of his paper, Professor Gordon lists a number of scenarios for the near-future course of the dollar on the international markets and the solution for its alleged misalignment with the U.S. trade deficit. (These do not include the massive interventions that have actually occurred.) He himself suggests that the rest of the world might rectify the American trade imbalance by large-scale expansion on their own, rather than by urging or forcing contraction on the U.S. I agree that this might work, and also be compatible with a strong dollar. I do not, however, see any particular advantage in such a policy for America's trading partners, or for Japan in particular. (Why should Japan increase inflationary pressure just to bring down its current-account surplus with the U.S., or to pull a few of the teeth of the American protectionist movement?)[1]

Of Professor Gordon's alternatives in the absence of intervention—or *with* intervention, if the cheaper dollar requires renewed capital controls in Japan and elsewhere—one would be to await a replay of the late 1960s. With the world awash with dollars, the dollar would have to come down, whatever happened to the American deficit. But when this would happen I cannot forecast, and neither could I dare to predict a "soft landing" when it does happen.

Professor Pollard is, I am quite sure, correct to diagnose the "British disease" as largely a paucity of real investment in real plant and equipment. I should also add, a paucity of what Americans call "green field" investment in completely new plant as distinguished from "band-aid" investment in keeping obsolete equipment operating not too much below rated capacity. But I should have liked to see Professor Pollard take one important step further, and inquire further why Britons (and others) were not more willing to invest larger sums in British industry. My suspicion is that he might have had difficulty absolving Britain's costly welfare state institutions, Britain's ostensibly progressive tax system, and Britain's "bloody-minded" trade-union movement from a considerable share of the responsibility—which is not to say that they are the whole story.

Professor Bruno's "stagflation" paper is technically and analytically the most ambitious and the most difficult of the papers we have had before us in the past two days. I cannot claim to have understood it at all fully in the time available to us, but I hope I am not alone in this confession. What I would have liked to see added at some point might be a brief statement of how Professor Bruno thinks his model differs from and improves upon the other "international" and "linkage" macro-models to which we have been exposed in recent years; perhaps such a statement might have replaced, or relegated to footnotes and appendices, some details of the model itself, which (I notice) involves an "adaptive expectations" lag

[1] Professor Gordon was correct to insist (in our symposium discussion) that the bilateral U.S.-Japanese trade deficit could be eliminated and even reversed with no fall in U.S. dollar wages and labor costs, either absolutely or relatively to Japanese yen ones. (At the 1930 exchange rate of ¥2 to the dollar, those Japanese workers still employed would be tyccons and the trade deficit would be all the other way!) But if we limit ourselves to "reasonable" or "defensible" exchange rates, I think my statement holds.

structure of a sort my rational-expectations friends have been assuring me is both unreliable and outmoded.

There seems to be a basic agreement between Professors Bruno and Gordon. In particular, the two agree that such countries as Germany and Japan should go all out for "reflation" and demand expansion, without further disinflation. As I have said in admitting my own biases, I am not clear how "it"—meaning under-employment inflation—is to be kept from happening once again, as it has done so many times already in so many countries.

And having personally been much impressed with the Mckinnon proposal for *An International Standard for Monetary Stabilization* (1984), I would have liked to see it mentioned here.

We have two "LDC" papers from Asian countries, one from Professor Hong of Seoul, Korea, and the other from Professor Kuntjoro-Jakti from Jakarta, Indonesia. Both are descriptive and institutional, taking the opportunity to explain to the wider world the problems of the Asian LDCs, sometimes regarded as a homogeneous and formless mass by the general public of the so-called advanced countries—Europe and North America more than Japan or Australia.

I liked the Korean paper better than the Indonesian one, because it was more comparative. Professor Hong does the best job I have yet seen in distinguishing, in the space of a single essay, the four Asian NICs from each other. And while Westerners still occasionally think of all four as havens of Free Enterprise, Professor Hong makes a good case that three of the four (South Korea, Taiwan, and Singapore) are in fact over-regulated and over-protected: his South Korea is more like the world of Chalmers Johnson's *MITI and the Japanese Miracle* (1982) than postwar Japan ever was. But Professor Hong spends more time proposing more and more regulation for Hong Kong than he spends on deregulation of the other three. I am not clear why this is. The Republic of Korea, for example, may have developed over the 30 years since the Korean War a bureaucracy honest, intelligent, and perspicacious enough to internalize the externalities, extend the economic horizons, and otherwise out-perform the Korean market on many occasions. But can Hong Kong do the same in the dozen years remaining before the city goes behind the bamboo semi-curtain of the People's Repeblic of China? And can we anticipate from the numerous resident representatives of the PRC the tolerance of economic policies amounting to much more than preparation for coordination with the Chinese system, for the primary benefit of China rather than Hong Kong? A free market is one thing; a "heretical" variant of planning is another.

LDC spokesmen can be counted on to complain against the West, and Professor Hong is no exception. His principal complaint relates to the transfer of advanced technology, or rather, its non-transfer to the four NICs of Asia.

None can be surprised if a company, having developed and applied some technological improvement at some cost in R&D expenses, is disinterested in selling that technology cheaply to potential competitors, either next door or across the Pacific Ocean. (I hear that many American companies now regret having sold technology to Japan in the 1950s so cheaply as MITI persuaded them to do—and in some cases, having sold it at all, on any terms whatever!) Lenin is quoted as saying that capitalists would gladly sell him all the rope he needed to hang them, but does Professor Hong expect equal foolhardiness 60 years after Lenin's death? At least, Lenin and his successors—and likewise, low-wage and weak-union

countries—can legitimately be kept waiting until patents expire!

But Professor Hong seems to be accusing "the West" of collusion or unholy alliance in refusing to the NICs access to technology on any terms. (I won't sell my technology to the Republic of Korea if you won't sell yours to the Republic of China.) A negative is unprovable, the logic textbooks say, and I do not want to be understood as denying the existence of collusion in refusing technology transfer, but Professor Hong has not shouldered the burden of proving to us that such cases *do* exist and *are* important. Such is apparently a widespread NICs view, but why should it spread further?

Professor Kuntjoro-Jakti presents us with what are actually two papers in one, with his summary and conclusions related only loosely with his expository account of Indonesia's present difficulties. Given my ignorance of Indonesian conditions, I shall concentrate upon Professor Kuntjoro-Jakti's conclusions, but cannot resist noting that an OPEC member expecting world sympathy reminds me of the man who, having murdered his parents, asks for a light sentence because he is now an orphan!

Professor Kuntjoro-Jakti goes beyond Professor Hong in blaming industrial countries and their governments for refusal to share technology with Socialist countries and in military matters, I presume he means that governments have failed to require companies, who do own technology, to license it to LDC producers on easy terms. In Anglo-American law and politics, however, government intervention to force technology transfer constitutes illegal confiscation unless it is done as an aspect of criminal punishment. Japan with its famous *gyōsei-shidō* may be different, but even as a foreigner I make bold to suggest that the administrative guidance to license valuable technology would only be accepted, if at all, for a very large *quid pro quo*, which might not be worth giving.

Professor Kuntjoro-Jakti also takes the position that LDCs should remain free to restrict international transactions in services. He means, I suppose, such services as insurance and accountancy, when sold by corporations or corporation-sized partnerships. (This whole subject of trade in services may come up in the next GATT meeting.) Professor Kuntjoro-Jakti, presumably interested in keeping multinational service companies from monopolizing LDC markets before LDC companies can compete with them, inquires whether it can be proved that free trade in services aids the importing country. I cannot prove that it does, but on the other hand I see no significant difference between trade in goods and trade in services. If "infant-industry" protection is sensible for certain goods, it may also sensible for certain services. My personal view is that the case for infant-industry protection depends on auguments about the socialization of risk and about badly-functioning capital markets in the presence of risk and uncertainty. The goods-services distinction, in other words, is out of place.

We come at long last to the two specifically Japanese papers, which are related very differently to the grand theme of this symposium.

The first author is Professor Nakatani. He addresses himself at once to the basic question of what Japanese policy should be in the present situation, both from the interest of the world as a whole and of Japan as one important country in it. His title is "Towards the New International Economic Order," but I am glad to say that Professor Nakatani makes more sense than UNCTAD. On the other hand, his argument is less massive and ambitious than the *Brandt Report* of 1980.

Professor Nakatani thinks Japan should join in the provision of "international public

goods," in which he includes "defense, an international monetary system, and leadership in getting approval . . . concerning basic philosophy about how to integrate the world economy." I recall Professor Charles Kindleberger expressing somewhat the same idea in discussing the pre-1914 gold standard. Without using the term "international public goods," he said that Great Britain had supplied them and thus enabled the gold-standard system to work. These "goods" were two in number: willingness to let interest rates rise to attract "gold from the moon" if necessary for full sterling convertibility, and willingness to practice free trade, providing a market for the world's "distress goods." (I would myself add a third "international public good," namely, a willingness to tolerate inflation when British gold holdings rose above normal, rather than sterilizing the gold inflow and concentrating the whole adjustment burden on deficit countries.)

Professor Nakatani's main interest, however, is in public finance rather than monetary theory. He ascribes much of the current international economic disarray to the mal-coordination of national tax system—as between those which, like the Japanese, favor saving over investment and those which, like the American, favor investment over saving. This leads taxpayers, he believes, to over-save in Japan and over-invest in America, and sets the stage for capital flows from Japan to the U.S. He presents no evidence for the quantitative importance of this point, which is certainly valid and has largely been neglected. My own guess is that its importance is considerably less than Professor Nakatani believes, but I have no evidence either.

Based on this fundamental insight of the fiscal basis of capital flows, Professor Nakatani would like Japan to do four things:

(1) Organize a tax summit aiming at international tax-system co-ordination.

(2) Subsidize overseas production and technological transfer by Japanese companies to the LDCs.

(3) Open the Japanese market to foreign imports.

(4) Promote and finance large-scale public projects in the LDCs.

A fiscal summit may well be held, but hope for agreement seems rather Utopian in view of the great differences of opinion among both theorists and practioners on what tax systems should be—direct versus indirect taxes, "personal" versus "business" taxes, degree of progression, the legitimacy and financing of budget deficits, etc. The second Nakatani proposal, moving Japanese production to the LDCs, means at least initially a substantial worldwide efficiency loss—and also a loss of employment in Japan itself! It will also weaken the Japanese labor movement and reduce the U.S.-Japanese trade deficit, although not the U.S. trade deficit as a whole. Opening the Japanese market would, as Professor Nakatani says, mean little so long as imports are, or are thought to be, inferior or over-priced or both—unless, that is, Professor Nakatani is willing to attack organized agriculture head-on and admit foreign rice and wheat along with beef and oranges. (There is a lot of residual mercantilism in Japan, perhaps more than elsewhere, according to which countries should import only those necessities which they are physically unable to produce locally.) As for Professor Nakatani's fourth point, a bigger and better Japanese program of ODA (official development assistance), one can of course hope that Japan may do a better job than the U.S. or the international agencies have done, so that expenditures in the LDCs produce no less worthwhile results than similar expenditures might produce at home. But speaking as a Japanese resident (although an alien) I would certainly prefer a bridge over

Tokyo Bay or better housing in Osaka to Sukarnonian white elephants and sports palaces in Jakarta. I must confess that this well-intentioned "massive aid" talk, after the record of the last 30 years, reminds me of Dr. Samuel Johnson's description of second marriages—"the triumph of hope over experience."

Professor Teranishi's paper, finally, is a careful, painstaking financial history of Post-Occupation Japan. He divides it into two parts, and its most direct impact with the topics of this symposium comes at two points.

The first point of contact, which Professor Teranishi does not point out directly, arises from his analysis of the controlled financial system which prevailed until the early 1970s. This system, so far as he has been able to determine, did *not* waste or misallocate resources greatly. At any rate, it did not interfere with "miracle" growth. If I am justified in fearing that maintaining the ¥200/dollar rate will eventually require a measure of capital control, particularly exchange control, his analysis prompts the reply "what of it?" But I should perhaps warn my listeners that this optimistic conclusion about the harmlessness of capital controls will not necessarily hold for many other nations.

Professor Teranishi's second contact with our topic is more explicit. Most Japanese outside financial circles believe that Japan's export surplus led to Japan's deficits on capital account by making them affordable. Financial circles in Japan, according to Professor Teranishi, believe the causation runs primarily the other way, with Japanese growth leading to captal exports, which provided the rest of the world the wherewithal for purchase of Japanese goods. My own view has been that these two factors work together, and that little is gained by argument about which is cause and which is effect—which is chicken and which is egg. This puts me closer to Professor Teranishi than to the generality of Japanese (or American) opinion.

Much as I hope to have both understood and included in these scattered remarks the main points of all the papers, I can hardly anticipate having avoided serious errors of both omission and commission. *Moshiwake arimasen ga*—had I been able to receive some of the papers a little earlier, I might have been able to re-read them at least one additional time and avoid some of my mistakes. Trade-offs are too much with us, late and soon.

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