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AMERICAN AND EUROPEAN ECONOMIC DIVERGENCES AT CENTURIES END

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I write often for the foreign press. That gives me ample opportunity to pontificate and nag. Thus, I have been telling the Japanese that theirs is the worst macro-managed economy in the 1990s: paralysis by the bureaucratic mandarins from the Tokyo University Law School, plus the chaos of the faction-ridden Diet has perpetuated a completely unnecessary Japanese slump. And Japanese voters have passively acquiesced to the impasse.

None of that is your business or mine here today. But to sharpen my point and make it more persuasive to Japanese readers, here is how I framed the argument:

«You in Japan are now at the fork of the road. You must choose between the European pattern and the American pattern.

If the Bank of Japan persists in speaking only kitchen German à la the Bundesbank, your GDP will grow only as slowly as Germany and France are now growing. And your unemployment rate, after we correct for Japanese ability to conceal disguised unemployment, will soar toward the double-digit percentages so typical of European Union Countries.»

I went on to write: «On the other hand, there is the Nineties American pattern for you to follow. The United States was the first to recover from the global 1991 Gulf War Recession. For years we have surprised ourselves by outpacing the other leading countries of the world. Millions and tens & millions of new American jobs have been created net since the 1970s when worldwide productivity growth halved in the most advanced nations of the world - a contrast with Europe's almost stagnant job total.»

«And», I went on to boast, «all this happened while our independent Federal Reserve got rid of the 1970s'stagflation and was keeping a steadying hand on the credit throttle. U.S. inflation in the 1990s remained contained at between two and three percent per annum for the official Cost of Living Index. Since our best experts on the technical theory of index number construction tell us that the true rate of inflation is maybe 1,5 percent less than the overstated official index, American inflation behavior has pleasantly astounded us American economists.»

We pinch ourselves and say, «What went right ?»

Notice my intellectual arrogance when I leave the pages of learned journals on mathematical economics and write for the lay public. John Maynard Keynes could not have been more rashly self confident when preaching to President Franklin Roosevelt in 1933 than was Paul Anthony Samuelson nagging away at the polite Japanese.

Actually, my overdramatic dichotomy between the American and European dichotomy backfired, as I came to realize. People get tired of being nagged and of being bullied by bilateral trade wars. Right now the U.S.-Japan marriage of 50 years ago has moved into an anti-honeymoon stage. I could have called a plan to rescue Japan by any other name than American: packaged as The Pacific Rim Plan it might have gone down better, and then Japan's present faint signs of genuine recovery might have come earlier.

Let me also admit that, although I may do a little low-keyed nagging during my French visit to Toulouse, policy prescription is definitely not the main purpose of this present lecture. Instead I want to grapple with analytical diagnosis.

How did our two continents come to diverge in macroeconomic and even microeconomic behavior ? What part of that story was volitional rather than being *exogenously* dictated by trends of technology and politics ?

Naturally I do not know all the answers. And where I do have guesses, they are mostly hypotheses that cannot be self-confidently proclaimed as attested scientific findings. I'll try to confess my doubts and maybes; but remember we are all children of God and Freud, all too prone to wishful thinking.
Let me start with America where my knowledge should be least deficient. The viewpoint I'll try to talk from will not be that of an American. patriot but as a member of mainstream economic scholarship everywhere, pretending to be so to speak an observer from Mars.

I - THE NEW RUTHLESS ECONOMY

America began the 1930s as essentially pure Capitalism. I recall well this fact of my infancy and youth. But after the Great Depression and the New Deal, we went in and came out of World War II as a Mixed Economy - a Welfare State much like Europe, Britain or even Sweden. America moved politically toward the Europe that traced its roots to Otto von Bismarck and Louis Napoleon.

The early editions of my ECONOMICS were written just before my teacher Joseph Schumpeter died in 1950. He changed his brilliant mind considerably in the 15 years I knew him, and broadly I believe he agreed with my picture of the Fortune'500 Corporations as possessing much «oligopoly power» both at home and abroad. They were not run by John Kenneth Galbraith's Technostructure, but neither were they run by owner-managers. Berle-Means had corporate governance pretty much right in 1932. Managers with negligible ownership were secure and fairly autonomous in their jobs and policies because non- cohesive minorities characterized corporate shareowner democracy.

Trade unions had been unimportant in the America of the 1920s, having a foothold only in some AFL crafts. But after the Great Depression brought in Franklin Roosevelt's revolutionary New Deal, the Fortune-500 bought coexistence with their union and non-union workers by sharing some of the oligopoly rents with them. That is what was meant when my textbook first talked of good and peaceful industrial relations: white male blue collar workers in manufacturing enjoyed superior real wages in large and medium size American companies who produced mostly only for our domestic market and who were secure in their hold on those markets.

To a remarkable degree by now our Fortune-500 companies have lost their absolute-monarch status within their niches. With the evaporation of their oligopoly power, these largest corporations have become constitutional monarchs who reign only so long as they do not autonomously rule. Why this change in basic economic structure ?

The simple answer offered is that foreign competition has cut into the market power of the big three Detroit automakers; and into the power of U.S. Steel and Eastman Kodak. In the 1950s it was the Common Market miracles of growth that impinged on America and, according to this thesis nominating foreign competition as the prime mover, later it was Japan and such Pacific Rim tigers as Hong Kong, Singapore, Taiwan and Korea that eroded away the monopoly power of our largest firms.

This argument has merit but it is overly simple to impute the change mostly to new foreign competition. What is most persuasive politically to xenophobic protectionists is probably less than a third of the total explanation. New competition at home accounts for most of the change I am describing.

Steel rather than autos is most indicative. To start a fifth or ninth giant steel complex would have cost billions of dollars in the 1930s. That inhibited such threats to oligopoly power. But when technology changed, so that small electric furnaces using steel scrap could operate effectively with non-union labor, oligopoly power rapidly evaporated. Similarly, when trucks were invented, hundreds of thousands of independent drivers took away much of the business of the regulated railways with their strongly entrenched union restrictions on productivity.

As we look into the new century ahead, foreign competition will come increasingly into its own as a prime shaper of domestic market structure. There are more than a billion Chinese and Indians who work for one-tenth the European and North American real wage rates. Using mobile modern know-how, their productivity can assuredly be brought to within 25 percent of the best in the West. The same might be said for a quarter million people in what used to be the Soviet Union and its satellites. But when Europe arrives at whatever it is going, it will find America already there waiting.

Under a regime of future free trade, how can such a vast evening up in effective GNPs fail to alter domestic patterns of competition drastically? America I discern has gone earlier and farther into the new pattern than as yet France, Germany, and Europe have. Partly that is because, contrary to historical reputation, America is a less protective country than the European Union generally.

Let me make a hasty but important digression. Neither Europe nor America are likely to be able to succeed by use of autarkical protectionism in restoring real rates of GNP progress back to the growth paces of the 1950s and 1960s. International politics may well be a zero-sum game. When Bismarck goes up, Louis Napoleon must go down. Not so with economic development. After a billion Chinese live better and longer, we Americans can still expect to enjoy in the first quarter of the Twenty First Century a slowly rising standard of living at home. Economic history suggests -it can never prove anything- that going the route of isolationism and autarky hurts rather than helps the trend of average national affluence.

Now I return to, the subject of the new Ruthless Economy. World wide there has been a trend back from an uncontrolled welfare state. Margaret Thatcher in Britain was an extreme case. But the same story applies in post-Reagan America and in Most of Western Europe. Even Scandinavia, Australia, and New Zealand have been finally forced into more reliance on the market mechanism.

I am known as a do gooder. But experience has persuaded me to speak of the Limited Welfare State, which knows it must ration the less-than-50-percent of the GNP that can be efficiently available to transfer-tax payments that mitigate the inequalities sure to be meted out by a market mechanism that lacks both heart and integrated brain.

One way to, move toward the market is through privatization and deregulation. No longer can American unions count on the Federal Government as an ally that will by legislative force prevent corporations from breaking strikes by denying them the right to replace strikers permanently with willing non-union recruits.

What is the result of the new competition and the shift of voters toward the Right? In America we have witnessed the emasculation of trade unionism. At age 80 I see again what used to prevail when I was eight: few union members and scarcely any economic power possessed by collective bargaining and organized labor.

Time is scarce. Still I have to mention that nowadays corporate takeovers, mergers, and split-ups are epidemic. The CEOs of today know they can be fired tomorrow. And so it is down the line.

In the old days if you were an educated male in the corporate management bureaucracy, effectively you had lifetime tenure. As you aged and grew tired, your paycheck rose. Ail was supposed to even out on a lifetime basis non on a month to month or year to year productivity basis. Berle-Means patterns of autonomous managers today seem gone forever. The gasoline that enables corporation raiders to run their races is, often, that they cast off corporate obligations toward employees' benefits and job security. This explains, massive downscalings.

Here is the perfect example. American Tel & Tel announced its split up into three separate companies. 40,000 employees are to be discharged. The stock market reacted by sending AT&T shares way up in price. Was it bad public relations to announce, along with the downscaling news, an increase of CEO's salary by millions of dollars? Main Street cared, but Wall Street didn't. This is the same AT&T that used to be regarded as the quintessential utility monopoly with the most bureaucratic of executive hierarchy.

In the Ruthless Economy all of us feel a new anxiety. At age 57 we Harvard Business School elite graduates may be retired with short notice. And maybe we'll never have another job unless we eventually condescend to, be an assistant manager at a fast food McDonald restaurant.

II - EXPLAINING NEW AMERICAN MACROECONOMICS

Most of what I have been talking about you would put in the category of microeconomics. That was not Maynard Keynes' specialty. But I have been Machiavellian in my exposition. My purpose has been to help you understand our sea change in macroeconomics since about 1975-80.

When I spoke of more than 30 million new U.S. jobs net since then, did you think I was boasting and was being complacent? Let me set the record straight. The new jobs that Americans have been winning have tended to be mediocre rather than high-paying jobs. Average wages have been stagnating if not falling.
Inequality has increased in America since 1980. Property owners have gained a bigger share of the fruits of progress than have workers, especially unskilled and poorly- educated workers who lack human capital. Mind you, under the hypothesis I have been spelling out, these property profits and capital gains have not been the rents of monopoly and oligopoly positions. Au contraire, as we say in English. The perfection of competition has if anything improved. With the speed of light, computer driven trading does arbitrage away many temporary aberrations attributable to ignorance.

Just when technological and market-structure trends exacerbate inequality, the political swing to the right reduces the mitigating income transfers from the state. That is positive fact and not normative complaint. There is even a sniff of paradox in the fact that, when the people need social insurance most, there is less of it available. And there will be even less in the future.

The overall share in the GDP of government programs does not yet fully reflect this basic change. That is because the entitlement programs for old age pensions and medical care, legislated in the past, become ever more costly as the population ages demographically and as scientific medicine becomes ever more elaborate and successful while at the same time being released from rationing by the purse.

The proper test is not to ask whether Ronald Reagan and his successor Republicans have cut down on the total of governmental expenditures. Broadly, they have not been able to do that. It is more illuminating to extrapolate beyond 1980 what the plausible trend in total government expenditure was at that time indicated. Then measure against this what the actual upward trend has been. I think you will conclude from this exercise that the conservative revolution has had a considerable measure of success in what matters to libertarians -namely, the real total and scope of public control of America's resources is less than it was. likely to be under pre-Reagan administrations.

III - AMERICA AND EUROPE: MACRO OPPOSITES

Supply-side Reaganomics was not conservative macroeconomics. Instead of reducing budget deficits at high employment in the 1980s, its tax reductions enlarged deficits and made them chronic and structural by undertaxing the American people relative to their collective expenditure. Stupid madness? Not stupid if your sole goal is to reduce the scope of government no matter at what cost in making America, which has become unthrifty at family and corporate levels, become net even less thrifty. Putting this tourniquet around the neck of continued government expenditures is the Devil's recipe for making a low- saving society even more low saving.
At least the Reagan-Bush fiscal laxity contributed toward low American unemployment rates in the 1980s. Contrast this with the Continental pattern. Led by Germany and its austere Bundesbank, her neighbors who wanted to comply with the Maastricht timetable for a single European money and single central bank, pursued overall macro austerity that created and froze in two-digit unemployment rates.

Since 1983 at least -and that is more than 14 years ago- we have been told that currency parity of the franc with the mark necessitated contriving an inflation rate in France less than the low rate in Germany. Temporary costs in terms of extra unemployment, we were told, would be temporary and moderate - well worth the price of perpetual inflation-free prosperity cum balance-of-payments equilibrium.

This did not happen in 1983-1988. Or in 1988-1992. It still has not happened. But in the meantime longrun unemployment has grown and hardened in France. Recent statistics reported a 40 percent unemployment rate among youth under 25 years of age. And a quarter of these have been unemployed for more than a year. That bodes ill microeconomically for future French society. Basic skills are harder to, learn and teach at 33 than at 23. And Satan does find work for idle hands to do.

I have failed to, explain my message if you conclude that the fault is exclusively due to over-austere monetary and fiscal policy. Yes, in France these have been tight. And why? Ostensibly as necessary for Maastricht.

The European Union has been a great success, perhaps the most important creation of the last half century. It will be even more important in the future. But analysis shows that this has little to do with a European Parliament. Or with a future European central bank. Or with a future European currency based on pegged parities to, the mark.

Remember I am speaking not as an American patriot. Nor as a post-keynesian. Nor as a do-gooder. We in America can live well with a Maastricht that comes into, existence if that should materialize. We can live as well with the present halfway house. Or with a Europe that evolves into floating parities and sliding pegs.

It is realism and basic economic analysis which cogently suspect that one European money is a pipedream between now and 2005. Yes, Europe might sometime start off with a common peg; but soon the U. K., Italy and Spain will fall out of it. And better than 50-50 are the odds that the franc and the mark will themselves move divergently some time during the next decade. Avoiding that contingency by paying the high price of a stagnant decade is a game hardly worth the candle.

You may well reply: Yes, Professor Samuelson, you might prove right. But not making the attempt will, realistically, threaten even worse macro performance.

Before 1983 France often went through the gyrations of macro expansion, devaluation, and induced inflation without in the end achieving productivity progress and reasonably stable real GDP movements.
Those failures could turn out to be so again. Economics is not an exact science. At this point though, the American experience since 1980 may be suggestive and valuable.

IV - AMERICA'S COWED LABOR MARKET

The United States also had its bouts in 1950-1980 with stagflation and cyclical fluctuation. I used to envy Germany and its «Phillips Curve» and wish that we in America could better avoid our wage-price price-wage spiral. Now the shoe pinches on another foot. I am happier in the 1990s with the mechanics of our labor market than with that of Europe.

Earlier I spoke of the Ruthless Economy. And of the trend back toward the market and toward limits on the Welfare Transfer State. Now I need to call attention to what might be called our Cowed Labor Market. (l don't know how that translated into French. It is not mad-cow disease that is in question nor any kind of mad irrationality.)

Employers in America are tougher in bargaining, hiring, and firing than they used to be. Human charity and altruism is not what has changed. Rather it is: when you lack oligopoly power, continuing to follow your heart rather than head in human relations is a sure recipe for a short life of benevolence. After you have tapped out shareowners' wealth, the market action will have moved elsewhere anyway. Under modern market competition, social Darwinism is not a creed; nor is it public relations apologetics. Rather it is a reality.

As a humanitarian I lament that the markets for blue-collar, white- collar, and professional workers do not clear at full employment with nicely rising real wage rates and benefits. But still I would rather have people accept the jobs that can be there rather than hold out for better jobs that are just not there.

I give much causality credit for a decade of successful Federal Reserve monitoring of the real U.S. economy to the fact of America's cowed labor force. Contrast this with post- Franco Spain and its over 20 percent unemployment rates.

Right now our political parties fight over raising our minimum wage rate for $4.70 an hour to $5.60. Politically this is big news -a plus for Democratic voteseekers. Economically it is mostly only symbolic. Why? Our minimum wage rate has long been frozen far below median market wages. Your French minimum exceeds ours even though correctly calculated U.S. per capita affluence is distinctly above France's. That excess can hardly be a good thing for your stubborn youth unemployment problem: but I will not be dogmatic. America has large black, Hispanic, and other minorities: therefore it could be the case that we can least afford high minimum wage rates. (notice that I did not say «generous» standards: when too high they could end up being the reverse of generous.)

CONCLUSION

Let me wind up. Notice that I have been cautious in advising you in France to move to the American pattern in order to enjoy our scrumptious recent performance. Marie Antoinette said, «Let the poor eat cake.» Such was not feasible cofent advice. I am an economics Ph.D., and my name is not Marie. If your labor movement turns class-conscious and aggressive in trying to raise its fractional share of a fixed total, trying to imitate the letter of our strategies might fail to achieve its fruits.

Economics is more than economics. It is political economy. What will the political market bear? Your political market, not ours. Can French democracy preserve minimal programs to alleviate suffering that accompanies a privatized and deregulated market economy, while at the same time restoring the sensitivity against cost and price-level inflation associated with unemployment slack in the system?

If so, the American pattern is there for you to emulate. And in America itself, if we lose the willingness of the population to accept moderate wage jobs when they are alone available, then the present American pattern will be lost to us and we might well move back TO THE 1970s era with too much of both unemployment and unpredictable price instability.

The divergence between our continents can be reversed by a reconvergence to a common pattern. My hope is that we not revert to Europe's structural high unemployment; but rather that we'll both come to enjoy America's recent good luck.