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Article — Digitized Version

The future of a free world economy

Intereconomics

Suggested Citation: Kindleberger, Charles P. (1972) : The future of a free world economy, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 07, Iss. 2, pp. 41-44, <https://doi.org/10.1007/BF02929153>

This Version is available at:

<https://hdl.handle.net/10419/138585>

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and the volume of our exports. The employment of large numbers of guest workers resulting from this is by no means the best solution. Before World War I Hanseatic merchants always adhered to the basic rule of reinvesting abroad at least 5 p.c. of their export proceeds. I consider this a very sound rule. Today we are, perhaps, at 2.5 p.c.

Do you think that labour-intensive types of production in particular should be moved abroad?

That could be a factor for deciding to move productions which in the Federal Republic are no longer profitable because of wage increases to countries with more favourable wage conditions. But I must repeat again that businessmen are guided by a large variety of economic considerations. Take, for instance, the case of Siemens. On the one hand, the firm decided some years back to set up certain factories for the whole

world, i.e., to manufacture in one country, say Belgium, certain components for all factories in the world. On the other hand, there are some products being made in Japan and exported to the Federal Republic. There are so many interrelated factors to be taken into account that one cannot confine the appraisal to savings in wages.

Direct Investments

Which countries, do you think, will be favoured by German industry in future — industrialised or developing countries?

That is a well warranted question. In years past a number of firms which planned well ahead for preference engaged in developing countries, their reasoning being that in these they could still gain a relatively large share of the market at an early stage and expand as the volume of economic activity grew, whereas in countries like the USA they would never command more

than a tiny share of the market. In the meantime much water has been poured into the wine because so many uncertainties and hazards have arisen in the developing countries concerning the tangible assets, remittance of earnings, etc. There is now much more interest in investing in the industrial countries proper and the market share is no longer the main issue.

Do you believe that encouragement of direct investment in developing countries may provide some redress?

Such encouragement has always been given and will, I think, continue to be given and can partly offset the existing misgivings. But many developing countries have themselves to blame for this tendency if investments to their benefit are put in jeopardy by political and economic experiments which deter independent businessmen who are used to realistic assessment.

The Future of a Free World Economy

Professor Charles P. Kindleberger, Cambridge, Mass.

Professor Kindleberger, no doubt the Nixon Economic Revolution had led to a very dangerous "money-and-trade war". How do you evaluate President Nixon's economic program?

It seems to me that President Nixon is attempting to correct a situation of crisis at home and in the international position of the United States.

Regarding the internal program of price-and-wage controls,

economists in the United States entertain a wide spectrum of opinion. Milton Friedman at one extreme believes they cannot be effective. Kenneth Galbraith at the other end has argued in their favour for some years, and believes they should be permanent. My view is that both extreme doctrinaire views are wrong. An incomes and price policy is useful in the short run for breaking up a dynamic process of wages

and prices chasing one another. They can serve to halt the edging out of the Phillips curve, if you use that technical sort of language. But they cannot last. The disequilibrium system does not behave well over time.

On the external front President Nixon's aim was to work out a series of structural changes, mainly in exchange rates and tariffs, with the hope that after that the international trade and

monetary mechanism will work smoothly again. And this was done on December 19, 1971.

Harmonisation of National Monetary Policies

On the question of the main lines of reforms, which are needed in order to put the international monetary system on a sound footing in the long run, a widening of the parity margins has been decided upon in Washington and a supplantation of the dollar as a reserve currency by Special Drawing Rights (SDRs) has been suggested. Will this be sufficient to assure more monetary stability?

I am quite sceptical about both reforms you mentioned. In the first place, the wider the parity margins the more we approach the flexible exchange rate system. This is undesirable because it breaks up trade. I know that many economists do not agree with me, but I think that the events of the last months have shown that floating is no solution.

As far as the replacement of the dollar by Special Drawing Rights is concerned, I would think that this is a step which does not guarantee success. It might work and it may be worth trying, particularly because many countries think that it is undesirable to continue to have the dollar as reserve currency. But it seems to me that the most important thing we need in order to reform the international monetary system is to recognise that in one world capital and money market we cannot have two or more monetary policies. Nations will have to evolve methods in order to arrive at a compromise world level of interest rates from which each country will be able to depart only within narrow limits.

It is when the United States lowers its interest rates and Germany or other countries hold them up that we get these enor-

mous capital movements that disturb the system. These movements are not the fault of the dollar as a reserve currency but a function of our misunderstanding of the way the system must operate. Unless we break up the world money and capital market, which I do not recommend, we must recognise that national monetary policies must be harmonised.

But that would mean that credit policy would not be an instrument any more for governments in their efforts to level out business cycles.

This is correct. I believe that most of our monetary troubles are a result of the attempt to use monetary policy independently by countries in spite of the fact that our capital and money markets are joined. This simply will not work. It is not so much the exchange rates and it is certainly not the political role of the dollar which are at fault. It is the operation of independent monetary policies with joint markets. Even if we get some flexibility into the monetary system and an international currency like the SDRs, countries still cannot operate the system with joined money markets and separate policies.

Chaos in the Agricultural Field

Some experts fear that the protectionist tendencies which exist now will be aggravated which would divert the free flow of trade into the narrow channels of a bilateral system. Is there a danger that the Big Slump will repeat itself?

I think that we can exclude any possibility of domestic slumps of the kind we had in the twenties and thirties. But I am concerned that there are real possibilities as you suggest of protectionist tendencies in many countries getting out of hand. Let us not forget that Denmark followed the United States with the application

of an import surtax right away. And there is no guarantee that similar measures will not be applied by other nations. This could have dangerous consequences for world trade.

Recent negotiations between the United States and the European Community show that the points of view of both regarding trade liberalisation are very far apart. How do you judge future prospects of trade liberalisation?

A Basically Mercantilistic World

We should be worried about having in the industrial field the same kind of chaos we have in the agricultural one. In the agricultural field the trade war is most obvious. The French, Germans, Danes, New Zealand, the United States, all have very strong and different views which are very difficult to compromise. The chaos in the agricultural field has resulted in the chicken war of some years ago, in several crises of the EEC, in the current difficulties between the EEC and the USA.

Part of the problem is, I believe, owing to the fact that farmers have too much political power compared with their economic power. Engel's law says that as countries develop economically the role of agriculture necessarily shrinks. But Engel's law does not apply politically. Here farmers continue to have as much power as in the past. Switzerland and the United States are two good examples for the power farmers still have in politics, in spite of their insignificant economic role. And there are other examples. It is for this reason that agriculture is such a disaster in terms of efficient allocation of resources in most countries of the world.

I see a real possibility that chaos in the agricultural trade field may extend into the in-

dustrial field, which would be a dangerous development.

How would you see the role of GATT in this context?

I think GATT needs to be strengthened. One way to strengthen it would be to put stronger people in it. Under former Secretary-General Sir Eric Wyndam White it was more effective than it is now. His retirement has been a loss for GATT. Now that a solution has been found out of the monetary crisis there could be a chance that we will do a little better on the trade side. But mind you, I am not too optimistic on this, since the world has basically become mercantilistic. Everybody wants an export surplus. Economists may not know too much but they know that not everybody can have an export surplus at the same time

unless they define this export surplus differently.

Negative Effects for Developing Countries

The UNCTAD-Secretariat has published a study on the effects of the US-import surtax and the monetary measures on the LDCs' economy and foreign trade. According to this study, a decline of exports of annually at least \$ 500 mn was expected, as long as the surtax was in force. Furthermore the de-facto devaluation of the dollar has brought another loss of currency reserves in LDCs of about \$ 950 mn. Is here not someone being punished for something he is not responsible for?

I agree with you that the economic troubles in the United States and the trade and money

conflict between the USA and Europe have a negative effect on the developing countries. The import surtax did not apply to the field of primary products. But of course the de-facto dollar devaluation does. And this hurts especially countries like Ghana and Brazil, since the coffee price is set in dollars.

It could also hurt the Organisation of Petroleum Exporting Countries (OPEC). Therefore they are demanding a pricing switch from the dollar to DM. OPEC seems to have taken the view that it can change every contract it wants because of Europe's dependence upon oil from the Middle East. And they have been able to get away with it in the past. If bargaining for Europe, I would think twice before agreeing in paying 17 p.c. more than stipulated in the contract, becau-

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V E R L A G W E L T A R C H I V G M B H - H A M B U R G

se you cannot demand fixed prices, on the one hand, and prices in the highest currency, on the other. If one has a contract in dollars, one cannot just change the contract at one's convenience.

Regarding the semi-industrialised goods from developing countries which were exported in the past to the United States, they have been affected by the import surtax. But one should not forget that the USA has been asking these countries for a long time in the past to restrict their exports of cotton textiles, since US-textile industry was not yet ready to accept a readjustment of trade as is certainly called for in the longer run. No compromise could be reached, so President Nixon acted the way he did, because of an election promise he had given to the textile industry.

Protection of Infant Industries

Will the coming UNCTAD-conference in Santiago bring a very hard confrontation between industrialised and developing countries on the question of trade liberalisation?

I see very little coming out of this conference. It must not be forgotten that the less developed countries are highly mercantilistic themselves.

But they argue that they have to protect their infant industries.

This is quite true. And they have a point in arguing like that. I think we ought to have two policies, one for the developed countries which should be liberal and one for the LDCs which might be more mercantilistic in certain fields. But countries with highly illiberal policies should know that mercantilism is a dangerous game. It is hard for the developed countries to sustain liberal policies in a world of protectionism and discrimination, but dangerous for the less

developed countries if they continue with overall illiberal policies.

The decision of the US-Senate to stop foreign aid allocations of \$ 2.9 bn for 1972 has not increased American credibility abroad. Must this decision be seen as a sign for a growing isolationist feeling in the USA?

It is one of many signs. The United States has in the past been continuously attacked at home and abroad for its foreign aid, which in the view of many leftists follows imperialist aims. So politicians are more and more inclined to withdraw foreign aid. The US-balance of payments problems — which I think are exaggerated enormously — were only the excuse to cut off foreign aid.

Growing Isolationist Feeling

I think this attitude of many American politicians is misguided. It is a mistake to react to criticism abroad in such a petulant way. It may well be true that foreign aid is less than perfect in the way it is given by the United States and the way it is used in the recipient countries. But on the whole, imperfect foreign aid is better than none at all.

Why would you say that the US-balance of payments problems are being exaggerated?

Because many of the dollars now in foreign hands will not in fact stay abroad. Many domestic and foreign corporations have borrowed dollars during the period when exchange rates were being adjusted, and the dollar was being devalued. The result is that the dollar is in a very strong technical position, with thousands of individuals and corporations who have been short of dollars about to cover. Once the market is convinced that the exchange rate is stable exchange at the new parity, long positions in yen, DM, francs and other currencies will

be closed out. Dollars will be bought from foreign central banks and used to pay off dollar loans. The present balance of payments "deficit" of the United States is by no means a real deficit. The foreign surpluses were borrowed and the greater part of the deficit was merely loaned.

US-leadership in a Free World Economy

Is in your opinion the United States still willing to play the part of active leadership in a free world economy?

I think that President Nixon and Secretary Connally are not willing to fight very hard against growing protectionist and isolationist tendencies in the USA for fear of losing some votes. Mr Connally's bargaining attitude during the realignment of exchange rates negotiations suggests to me that he is much more concerned to show a tough standpoint abroad than at home. He and President Nixon are probably thinking of President Wilson who hung on too long to international leadership in 1919 and lost the next election because of this. But I may be too pessimistic.

Could it be that the strategy of President Nixon is to first get the US-economy moving — cut down the price increases and the unemployment rate — and then resume leadership in the free world economy?

I recognise that this is a hopeful possibility. It could certainly be that he intends to give the economy a strong jolt — through a correction of the exchange rate and his income and price policy —, in order to resume leadership after stopping the domestic deterioration that was taking place. But the question is: can he put Humpty-Dumpty together again after he fell off the wall? Only time will tell!