Restructuring The International Trade System

By Isamu Miyazaki

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The economic declaration announced at the end of the 1985 Bonn Summit meeting of the industrially advanced countries set "noninflationary growth" as a world economic target and stressed that "international collaboration" was the key to achieving it. At a glance, this appears a very commonplace slogan. But it is an extremely significant statement in view of the current state of the world economy.

Optimism and time bombs

After recording zero growth in 1982, the world economy picked up and posted growth of 2.3% in 1983, expanding to 4% in 1984. World trade, too, increased, expanding over the preceding year by 2.2% in 1983 and 8.3% in 1984. Inflation remained high in many developing countries, but in the advanced countries it subsided to an average 4.8% in 1985. It is expected to be held to the 4 percent level again in 1986.

Background factors contributing to this improvement included the dissipation of the uncertainty over energy supplies which had simmered throughout the 1970s and worldwide stabilization of raw material prices. Moderate wage hikes due partly to smoother labor-management relations and extensive technical innovation in high-tech and other sectors further fed confidence that "noninflationary growth" was being realized.

However, a careful examination of the world economy today reveals lurking difficulties which preclude unconditional optimism. Former West German Chancellor Helmut Schmidt described these difficulties as "time bombs that could explode at any time." The time bombs

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mostly take the form of disparity between countries in the economic growth rate (productivity) and inflation. Their ultimate manifestation is in international payments balance.

True, in the advanced countries as a whole, business began to pick up in 1983 and inflation is still subsiding. But the trends have not been equally felt in the United States, Japan, and the European Communities (EC). Take 1984, for example, the year in which the U.S. attained its highest growth rate of the 1980s (6.8%). That year, Japan's growth rate lagged at 5.7%, and the EC's growth was only in the 2 percent range. Moreover, the economies of Japan, the U.S., and the EC all bear problems of their own.

The U.S. attained high growth even though it was saddled with twin deficits in the fiscal budget and trade. U.S. industry, from agriculture to high-technology, has lost much of its competitiveness to the high dollar. Moreover, in 1984 the U.S. became a net debtor for the first time in 71 years. It is no wonder that the U.S. Congress has before it today a full load of protectionist bills, ranging from legislation for import surcharges, to bills on import restrictions, retaliation, and reciprocity. Yet should Congress pass these into law, there is no doubt that world trade would be shackled.

Japan, meanwhile, enjoyed the second highest growth rate among the advanced countries in 1984. It was expected to take the lead in 1985. But Japan depended solely on external demand to fuel its growth, and as a result it has amassed a huge trade surplus. Needless to say, this excessive trade surplus has intensified protectionist trends among Japan's trade partners.

Partly because of the rigidity of its industrial structure, the EC's growth rate has remained low compared with those of Japan and the U.S., moving in the 2 percent range. Low economic growth means that countries cannot provide enough jobs for newcomers to the labor force, with the result that unemployment in Europe averages a high 12%, concentrated among the young. With the exception of West Germany, there are no signs of unemployment coming down. This economic environment could easily lead EC member countries to protectionism.

A sobering look at the developing world

The developing countries, too, have been rigged with time bombs. As a whole, developing countries have suffered from a slowdown in exports because of earlier economic recession in the industrially advanced countries and market restraints. Prices of primary commodities, their principal exports, are sluggish, leaving these countries' average growth rates quite low in comparison with the advanced countries. Under these circumstances, economic development has not progressed as rapidly as hoped, and aggregate debts are believed to have reached $863 billion in 1985.

The situation, of course, is not the same for all developing countries. Oil-producing countries, including members of the Organization of Petroleum Exporting Countries (OPEC), have generally been suffering from current account deficits since 1982 due to the easing supply-demand situation for oil and falling oil prices. Their domestic industrialization programs have slowed, and their demand for imports has shrunk.

In contrast, the growth rates of NICs (newly industrializing countries), particularly those in the Pacific area, have been relatively high in recent years, and industrialization has made rapid progress. However, they are heavily dependent on the U.S. and Japanese markets, and stagnant exports since the start of 1985 have cut into their growth rates.

Many African countries have not yet reached the point of economic takeoff. Their agricultural production failed to improve as hoped for, in part due to natural conditions. Famine is already a serious problem, and the population explosion and the wholesale destruction of the natural environment are reaching critical proportions. What is essential for this region is noneconomic aid.

And of course, while some liberalization has been observed in socialist countries, the principle of the planned economy still takes precedence over market mechanisms in these nations. In the Soviet Union, where agricultural and industrial production are sluggish and the people's living standards have yet to improve appreciably, the Gorbachev government's program to revitalize the economy is being watched with keen interest, both at home and among foreign observers. As for China, it is aggressively pursuing a policy of internal and external modernization. The country's growth has been so rapid that bottlenecks have formed in the transportation and energy sectors. Although the pace of growth may slow, China seems certain to achieve her target of doubling agricultural and industrial production by the year 2000.

This brief review clearly shows the differences, not only in each country's growth and inflation rates, but also in their policy priorities. These differences lead to gaps in their international balance of payments. It is natural that there should be disparities between countries in scale of trade and international payments. Yet when the deficit or surplus of a specific country becomes chronic, world trade cannot be expected to develop smoothly. The rules of GATT (General Agreement on Tariffs and Trade) are not being fully observed, and 50% of world trade is said to be controlled in one sense or another. One may hesitate to call this a "crisis," but it is certainly a grave situation. And it should put a damper on unbridled expectations that the world economy will continue placidly along the path of inflation-free growth.

From self-interest to international collaboration

Disequilibrium in the balance of international payments occurs because of disparate economic conditions. In order to redress the imbalance, an adjustment of the affected economies is essential. The question is how to go about it. Basically there are three principles that must be observed.

First, each country should exercise moderation in its economic management, keeping its own house in order through its own efforts. If in one country fiscal policy is loose, labor and management are irresponsible in their dealings with one another, and competition-restricting market practices prevail, its economy will naturally slide into chaos. Not only that, in today's increasingly interdependent world economy, the effects would inconvenience other countries. No nation should export inflation, or deflation. At the same time, however, it should be recognized that political unrest could arise in some developing countries if they are required to maintain excessively stringent economic policies for too long in order to settle accumulated foreign debts.

Secondly, in correcting disequilibriums in the balance of international payments, "freedom in principle" must be respected. Artificial restriction of imports and/or exports either by government fiat or through other organs should be avoided. World trade today is regulated by import restrictions, voluntary restraints on exports, and collateral imports. The "non-discriminatory free trade" stipulated in GATT is not being observed. And, to make matters worse, many countries are poised to impose even more stringent restrictions. The advanced countries, particularly the U.S. and trade beneficiary Japan, must shoulder much of the responsibility for rectifying this situation. These two countries are further expected to play a central role in the soon-to-start "New Round" of international tariff negotiations. Needless to say, "freedom in principle" is applicable also to capital transactions.

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Thirdly, international collaboration in economic policies must be promoted. The need for international collaboration has been stressed repeatedly, but such exhortations have not produced significant results until recently. The meeting of the finance ministers of five major countries (G-5) held in September 1985 resolved to correct the overvalued U.S. dollar through coordinated intervention in the foreign exchange market. This policy has been effective to a degree. But intervention alone cannot change the basic undertone of the market, and the effect on trade balances will be limited accordingly. In order to achieve significant results, intervention must be supported by coordination in macro-economic policies.

Such coordination should not be confined to adjusting the business climate alone. It must extend as well to the examination and adjustment of economic structure and to all factors which sustain that structure, from the relationship between domestic investment and savings to tax reform and the reorganization of corporate structure and the capital market. These, needless to say, touch not only on each country's economic system and social customs, but on economic sovereignty as well. Clearly, the implementation of policy coordination will be rife with difficulties. Yet unless countries abandon their past absorption in their own interests and promote international coordination and collaboration, the time bombs in world trade and the world economy cannot be defused. Noninflationary growth is in the very best interests of all. ●

Principal World Economic Indicators (%)

	1984	1985 (estimate)	1986 (forecast)
Growth rate: World	4.0	2.7	2.7
North	4.6	2.8	2.5
South	2.8	1.9	2.9
Unemployment: U.S.	7.5	7.3	7.4
Japan	2.7	2.6	2.7
EC	11.8	12.1	12.2
International commodity prices: Wheat	−3.1	−9.2	−4.2
Minerals	−3.1	−1.5	−0.5
Petroleum	−2.9	−3.0	−4.0
World trade			
Exports: Total exports	8.3	4.5	4.0
Primary commodities	10.1	7.9	7.6
Manufactured goods	10.5	5.7	3.4
Export prices: Primary commodities	−2.7	−6.7	1.5
Manufactured goods	−2.9	0	10.0