The Need for Far-Sighted Economic Policies

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by Mike Mansfield

A year ago U.S. and Japanese newspapers almost daily headlined articles about the falling dollar and tensions between the United States and Japan resulting from the U.S. trade deficit. Since the Japanese current account surplus evaporated and OPEC raised its prices earlier this year, newspapers have turned their attention to other things. The absence of headlines does not hide the fact that the United States' trade deficit for the first seven months was $11 billion. Part of this, of course, can be traced to the high cost of oil imports, but a very substantial part results from the United States not exporting as much as it could. Far-sighted, complementary policies by the American government and business are needed to make the U.S. economy more competitive and increase exports. The U.S. Government and business must develop better mutual understanding and closer ties. It is time for partnership to replace the past adversarial relationship. The U.S. Government should give the same sort of encouragement and support to potential U.S. exporters as other governments offer their exporters.

Our persistent trade deficit is a symptom of weaknesses in the U.S. economy. The U.S. national savings ratio, 17.7 percent in 1977, is one of the lowest among the OECD countries. By contrast, the rates for Japan and West Germany are 32.2 and 24.2, respectively. The high consumption rate in the U.S. induces imports, but more importantly reduces the investment
necessary to insure that U.S. manufactures are competitive.
The figures bear this out. In 1977, the United States invested 7.3 percent of GNP in transport, machinery and equipment. The comparable number for Japan was 13.8 percent. Not surprisingly, U.S. productivity has been growing by only about 0.3 percent annually since 1973 while Japan's has risen an average of 7.7 percent annually during the 1970's.

We need to make fundamental changes if we want to be sure that the economic future of the United States is secure. Japan and other countries are likely to become more not less competitive. The seven year plan recently published by the Japanese Economic Planning Agency states quite plainly that Japan's high savings rate should be used to finance the development of technology and the further sophistication of the country's industrial structure. It is clear that in the coming years the Japanese intend to make and export on an increasing scale highly technological and sophisticated products like computers, fine chemicals and innovative energy equipment. At the same time they will improve the goods they now produce in quantity.

At present there seems to be no consensus in the United States in support of the sort of policies that would restore balance to the economy and that would assist American firms to compete better in international markets. Business, government, labor, and the consumer lobby all too often regard each other suspiciously. In Washington there has grown up in the last fifteen years a system of trade associations and single-interest groups which have the ability to block action
but not to build the consensus necessary for effective action. The difficulty of obtaining energy legislation has dramatized the problem, but the resistance to change is general. In some cases this has manifested itself as demands for import relief. We should not delude ourselves that we can rectify our trade imbalance by resorting to protectionism or by setting up standards of "fairness" which are simply self-serving.

Prolonging the lives of moribund industries has serious adverse effects on healthy firms, consumers, and the economy as a whole. The open international trading system which we have fostered for the last 30 years places a premium on efficiency and competitiveness. Nations which choose defensive strategies are not going to flourish.

It sometimes seems that in the United States relations among the various economic sectors are regarded as a zero sum game. In Japan the assumption that labor or consumers must lose if business gains does not prevail. It is fairly well documented that the Japanese saver, by accepting low interest rates on savings accounts, and the Japanese consumer, by paying high prices, subsidized investment by big corporations during the period of post-war recovery. Nonetheless, the whole country benefited. Per capita GNP went from about $200 in the early 1950s to about $6,000 now. The Japanese experience has proved false the notion that the gain of business is necessarily a loss for someone else.

Fundamental change in the U.S. economy is far more important than tinkering with the trade policy and promotion
bureaucracies in Washington if we are to put our trade balance right. The American government, for the benefit of all, must actively encourage savings and investment and the development of competitive, remunerative industries. The first thing that must be done is to control inflation, which erodes depreciation allowances, causes uncertainty and makes fools of the thrifty. The United States should take a lesson from its competitors who long have used tax and credit policy to promote savings and investment. The Japanese Government, for example, provides tax relief of various sorts to interest income. The United States, in contrast encourages consumption by taxing dividends and interest on savings, and by allowing easy consumer credit. It is time for the United States to seriously consider such measures as:

-- Raising deposit margins and down payment requirements for consumer loans;
-- Removing the tax deduction for interest on consumer loans;
-- Eliminating the interest-rate ceiling on savings accounts; and
-- Exempting interest from small savings accounts from taxes.

A recent Business Week article pointed out that funds no longer are flowing into the stock market as they once did because of more attractive investments to elsewhere. The government could encourage increased investment in the stock market, which must remain at the heart of a sound system for financing business,
by eliminating the double taxation of corporate dividends.

There is no doubt that if we really commit ourselves to it, government, business and the whole people working together could establish an environment conducive to savings and investment. In the final analysis, however, it is up to business to take risks, develop long term investment, and do the research market development that will raise productivity and promote the competitiveness of the U.S. economy. American managers have been accused of concentrating too much on next year's or next quarter's balance sheet, at the expense of longer term projects. If American corporations are to prosper, they will have to choose strategies that will result in the greatest returns over time and not merely in the best looking bottom line in the next annual report.

One certainty American businessmen face today is that foreign competition will increase. The Japanese and the Europeans are developing ever more sophisticated products and the newly industrialized countries are making consumer goods and basic industrial materials very efficiently. If American firms are to withstand the competition at home, they will have to invest in equipment and R&D for the products of the future. A defensive strategy is not enough, however. U.S. companies no longer can afford to consider foreign markets as residual markets. American firms, like their Japanese and European competitors, can reduce unit costs and raise profits by increasing exports. I find that American corporations that have been established in Tokyo for some time are doing well.
Others can do equally well here and in other countries. The recent successful conclusion of the Tokyo Round of trade negotiations will create new opportunities. To take advantage of them, though, firms must spend the three to five years it takes to develop foreign markets and become profitable.

Americans have been living in the present too long. We have been enjoying our current affluence while hoping the future would take care of itself. Now the future is upon us and we must change. In the short run measures like those I have suggested will mean some sacrifice by consumers for the sake of greater investment by business. That is no reason not to take them; for in the long run everyone will profit from a healthier, more competitive economy. It should go without saying, however, that to insure the continuation of incentives, corporations must see that their workers and consumers share in the gains.

The choice before us is between stagnation and the investment of a larger part of our national wealth in economic rejuvenation. Americans must recognize this and build a consensus in support of the necessary fundamental changes in attitudes and economic policies.
The Federal Pickpocket

With the interest rates that banks charge their customers hitting new peaks almost daily, the time has come to remove the regulations that now limit how much banks and savings and loan associations can pay their small depositors. These regulations limit the small saver to a 5 percent rate of return while inflation is running at 12 percent or higher. And while such savers are losing 7 percent on their savings, the unregulated market for large savers — of $100,000 or more — is paying 12 percent. The large saver at least breaks even with inflation; the small saver suffers losses because of the Government’s Regulation Q.

These losses are not equitable nor do they serve any social purpose. Regulation Q was originally adopted to raise bank profits in the Great Depression. But that is hardly a legitimate goal in the present era of profitable banking. Moreover, there are no corresponding Government limits on what banks may charge or to whom they must lend. Regulation Q serves only to raise bank profits at the expense of the small saver.

Thus Washington is now sending a confused set of signals to the small saver. President Carter and other officials keep calling for more savings to promote capital investment. Yet Government rules are used to take away 7 percent of savings from most of those who heed the call. No wonder the United States has one of the world’s lowest savings rates.

Some holes have been punched in Regulation Q in recent years but they aren’t big enough. Six-month time deposits may now pay the same rate as six-month Treasury bills — but a $10,000 minimum is required and the deposits must be non-negotiable. Many small savers don’t have $10,000 and they need access to their money more urgently than large savers. Four-year time deposits have no minimum purchase requirements — but their level of interest is fixed at 1/4 percentage points below that on four-year U.S. securities.

One can hope that inflation will level off one day soon. Today’s rates of inflation, however — in combination with current Federal Reserve policies and further OPEC price increases — almost guarantee that interest rates will remain high for a long time. The injury to the small saver cannot be dismissed as a passing phase. With current regulations the injury will persist and may get worse.

The banking industry would be the first to complain if Government regulators were to limit what it charges borrowers. There is no sound reason for it to oppose the same open competition in what it pays depositors. Those who would have the Government deliberately taking income from small savers for no social purpose are merely condoning a form of pickpocketing.