

Economic revolution postponed for now

Governments have been succeeding in hiding from the consequences of industrial change. When will they begin to prepare for what lies ahead?

ODD things are happening to the world's economy, with the oddest consequences, one of which is that economists, the practitioners of the "dismal science", are now more dismal than usual. The familiar shrugging of the shoulders by which they disclaim the accuracy of their predictions is now often accompanied by protestations that they no longer understand the basis on which predictions should be made. Critics should be charitable. The conundrums which now abound betoken structural changes in the economic pattern of the world whose full effects are far from being realized.

The symptoms of impending change are striking. Here are a few. Earlier this year, it was widely expected that the dramatic decrease by about two-thirds of the international price of oil would have the effect of stimulating the economy of the industrialized West; now, after half a year, it seems more likely that economic activity will decline, which is one of the reasons why the New York Federal Reserve board, the US central bank, last week reduced the general level of interest rates to 5.5 per cent. During the same period, the value of the US dollar on the foreign exchanges has fallen, against some currencies by as much as a quarter, but there is no sign as yet that the US trade deficit, obdurately stuck above \$100,000 million a year, will be abated in the near future.

Meanwhile, the huge amount of debt run-up by the developing countries of the world with the commercial banks of the West remains substantially unchanged; after three years of fear that defaults might bring the whole house of cards crashing down, there has evolved a network of arrangements by which the debts persist (interest continues to be paid) but not even the banking community knows when, if ever, the principal will be repaid. Nevertheless, the stock markets of the world have just sustained a year-long bull market, bidding up the value of industrial stocks and shares to unprecedented levels. The proportions of people out of work in advanced societies are also unprecedented, as are the low prices of the commodities (not only oil) by which the developing countries of the world must hope to earn a living. What can be going on?

Paradox

The most sensible reading of these paradoxical events is that they mark the emergence of structural change in the pattern of economic activity on a scale that financial institutions can contemplate only in disbelief. The case of economic relations between the United States and Japan is a familiar pointer to what is happening. These years, the trade surplus of Japan amounts to roughly half of the deficit of the United States, but the effects of this imbalance are concealed by the willingness of Japanese to spend their surplus on investment in the United States, where steadily increasing proportions of industrial and commercial assets are owned by foreigners. The result is that the dollar has not depreciated against the yen by nearly as much as it would have done in normal circumstances. Japan does not seem as rich as it really is, while the true poverty of the United States is temporarily concealed. Both governments appear to benefit from these arrangements; Japan would no more welcome a more rapid increase of personal prosperity than the United

States would enjoy a reduction of living standards. But this trend can be concealed only for a time.

Much the same is true of the stratagems by which governments are seeking to conceal from themselves the patterns of impending economic change. Both in the United States and Western Europe (but also in Japan), governments spend substantial proportions of their domestic revenues on the support of agriculture, for example. In the United States, the cost will exceed \$30,000 million in the year ahead, something like a sixth of last year's budget deficit and rather more in 1987 if the US Congress manages to keep the total budget within the limits of the Gramm-Rudman Act.

The European Community's Common Agricultural Policy has the same effect. For the governments concerned, it seems preferable to sustain high-cost food production at levels the market cannot absorb (both by direct subsidy and by devices such as the artificial restraint of farm productivity such as the nonsensical European decision two weeks ago to ban the use of animal hormones — see page 762). The losers are not merely taxpayers but countries elsewhere in the world, chiefly developing countries, that might look for a more prosperous future in the development of trade in food.

Hiding

Once-prosperous governments are also bent on concealing from themselves the consequences of both the shift from manufacturing to service industries, under way for the past thirty years, and the shift, within manufacturing, from the products of heavy industry (such as steel) to those of light precision industry (such as electronics). Part of the motivation for this unwillingness to face reality is the sheer discomfort of rapid change, but there is also an underlying fear that countries such as Britain that used to be successful at heavy engineering are ill-equipped with the skills needed for survival in what has become the modern world. One glaring sign of the general fearfulness is the attempt now being made, by an alliance of European and North American electronics manufacturers and music publishers, to persuade Japanese electronics manufacturers to withhold from the market the digital audio-recording equipment they are bursting to sell. If this scheme succeeds, where will protectionism end? Persistently high unemployment, made socially just acceptable by welfare schemes (as it should be), is a mark of the mismatch between the pattern of supply and demand.

This state of affairs cannot persist indefinitely. Water will sooner or later find its own level. But the readjustment, when it comes, could be catastrophic. What will happen, for example, in the slow-moving industrial communities when it turns out that the industrial equities whose prices have been bid up over the past several months by financial institutions buying financial assets with the intention of paying the huge impending cost of people's pensions turn out to be much less valuable than now? In this period of change suspended, the more far-sighted governments should be preparing themselves for what lies ahead, chiefly by investing in the intellectual skills that will be required. For most of them, unfortunately, propping up the past is the easier choice. □