GROWTH AND STABILITY:

What the United States and Germany Can Learn From Each Other

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I am delighted to be here in Atlanta and to help celebrate not only the tenth anniversary of the German-American Chamber of Commerce but also the first official German-American Day.

There is much that the United States and Germany have in common, and that German-Americans can be proud of. Enormous opportunities exist for increased business between the two nations. Organizations, such as yours, play a pivotal role in promoting these opportunities and in bringing about greater understanding between both countries and help to enhance the opportunities for mutually beneficial business.

This evening, I would like to talk about economic growth and stability. These are the key economic objectives in both Germany and the United States. However, the relative importance given to each has at times differed between the two countries. These differences have shaped the economic policies in both countries. At times, these differences have also loomed large in the policy discussions between the U.S.

and Germany. But these days the differences seem to have shrunk to such an extent as to be almost non-existent.

This may therefore be an appropriate opportunity to look at the historical record and to ascertain what we can learn from each other.

In many respects, the recent experience of the U.S. and Germany has been similar. Both nations managed to build unprecedented prosperity in an environment of democracy and economic freedom. Both utilized the power of private enterprise in promoting this prosperity, and both countries built their economies around technological mastery and development.

In the United States, the demand pent up during the war years, along with American ingenuity and entrepreneurship, led to an era of vigorous growth in the 1950s and 1960s, while in Germany, the market-oriented vision of Ludwig Erhard combined with the influx of resources under the Marshall Plan to produce a sustained and prolonged economic expansion during that period.

Despite these similarities, the historical experience of each country had a strong influence on its economic priorities. In Germany, the bout with hyperinflation led to the primacy of price stability as an objective of economic policy, while in the U.S. the memory of the Great Depression placed a high value on economic growth.

Germans cannot forget that their currency has been debased twice in two decades: first in the hyper-inflation of the early 1920s, and then again in the 1940s. It is therefore not surprising that inflation is seen as nothing but a sign of economic, and indeed, political, difficulties.

In contrast, the Great Depression of the early 1930s shaped much of the American consciousness. Between 1929 and 1932 national income was cut in half; unemployment soared; commodity prices tumbled; agriculture was depressed; and on a single day in 1932, one-fourth of the entire state of Mississippi was auctioned off because people could not pay their bills. More than 5000 banks failed, and 9 million Americans lost their savings.

The mistakes and problems of the 1920s and '30s were avoided in both the United States and Germany in the fifties and sixties. In Germany, the currency reform of 1948 restored a stable currency and German workers, consumers and officials tenaciously defended this new-found stability -- often at the expense of great personal sacrifice.

It was clear to everyone that economic growth could be achieved only within a framework of financial stability. What followed was a period of unprecedented economic growth - the German economic miracle - as individuals applied their ingenuity first to survive and then to prosper.

To a not insignificant degree, that spurt in growth was made possible by the increased fluidity and flexibility of post-World War II economic life in Germany. Not only buildings, but social structures and careers had to be rebuilt. Millions of refugees had to be absorbed. Eventually, millions of guest workers were attracted to Germany by the opportunities available. All this contributed to structural flexibility and an openness to new ideas. Germany became a nation of new entrepreneurs, whose names started to shine alongside the names of the establishment. In short, destruction brought with it the destruction of rigid structural forms and the new-found flexibility resulted in unprecedented growth and prosperity.

However, once a certain degree of comfort was reached, a new rigidity again set in and the freewheeling spirit was curbed. Success and prosperity brought with it a more defensive economic strategy which concentrated on preserving the hard-won gains rather than aiming for new heights. Subsidies and protective legislation, such as the Ladenschlussgesetz, reduced the potential for growth more and more.

The emphasis on stability has not been unwelcome to the average German. If asked what should be the uppermost economic goal, the typical German would probably respond: price stability. This is also the only statutory goal of the Bundesbank.

The average person in Germany is comfortable in his familiar environment and sees little reason to rock the boat. A consequence of this attitude is often a consensus approach to resolving economic and political problems, which is observable in business and governmental practices.

On the other hand, such practices may retard change and adaptation and suppress innovation and enterprise.

In the modern age, rapid economic advance often results from the seemingly chaotic developments in different industries and sectors of the economy that are integrated by a creative mind and form the basis for a whole new industry.

Let us look at the industrial structure that has evolved in Germany. It is still very dependent on subsidized heavy industries and has been slow in incorporating high technology production. A few large enterprises dominate the country's industrial base.

We should recognize that many of these firms expend considerable energies on internal product development in order to retain this know-how and leadership position. This, however, also results in long lead times for new products, which can only be introduced by firms whose size enables them to support the developmental effort. The result is slower growth for companies and further reinforcement of larger sized firms. Large German firms perform well in stable markets, but where markets are dynamic and characterized by rapid change, they sometimes find it difficult to adapt quickly.

There are a number of small and mid-sized firms in Germany that are highly efficient, aggressive, and innovative - but their energy is often stymied by high taxes and rigid laws and regulations that preserve the status-quo.

The German emphasis on stability goes hand-in-hand with relatively fewer social problems. Crime, drugs, and other abuses are not as pronounced in West Germany as in the United States. The streets are safer. To an extent, high mobility in the U.S. works against socio-economic stability. Research has shown that a high degree of residential mobility leads to high crime. In the United States, on the average, persons move once every five years, whereas in Germany such mobility is not the norm. The result is more stable and safer neighborhoods, but also less labor mobility and higher unemployment - which presents its own social problems.

By contrast, the U.S. has generally pursued a policy which gives economic growth a high priority. This preference is clearly enshrined in the "Full Employment and Balanced Growth Act of 1978", which emphasizes employment and growth through greater capital formation and expansion of the private sector. Private initiative and the free play of market forces are viewed as powerful engines of growth.

In the U.S., businesses operate with little or no government involvement. There are fewer regulations, distortive subsidies, and other impediments to private initiative, so that entrepreneurs are free to respond to emerging market opportunities in a timely fashion. As a result, the private sector has been at the cutting edge of technological advances. Product-innovations frequently lead to the emergence of whole new industries and transform their originators into multimillionaires. The incentive to innovate is great.

An example of the attitudinal difference toward innovation and enterprise is the American venture capital business. Innovative ideas are backed by financial resources seeking higher returns and often pay off handsomely. Lazer technology, fiber optics, genetic research, and personal computers serve as outstanding examples. The innovative zeal is also observed in financial services and other service industries.

On the other hand, German capital and state subsidies tend to support the advancement of established and tested industries.

But it is also true that the U.S. record on financial stability is less enviable than Germany's. The U.S. experienced a serious inflationary surge in the 1970s, which culminated in double-digit inflation. Germany's inflation reached only half the American level and is still below our level.

Reducing these inflationary excesses of the 1970s proved costly for us in the United States and resulted in the most serious recession since the Great Depression.

What can we learn from the experience of both nations? It is clear that over an extended period of time price stability and growth go hand-in-hand. A certain degree of stability and continuity is essential for economic decision making and growth. The German experience suggests that a commitment to price stability can obviate the need for drastic corrective action, such as was necessary in the early '80s in this country.

But while price stability is conducive to sustained economic growth, excessive pressures to achieve it can inhibit the more dynamic elements of the economy, leading to structural rigidities, low growth and high unemployment.

The U.S.-German experience also tells us that supply-side constraints rob the economy of its dynamism and that government intervention retards growth. Removal of structural rigidities through the repeal of distortive subsidies, taxes and tariffs yields handsome payoffs in terms of economic growth and employment as the German experience of the '50s and '60s shows.

Similarly, the more recent American experience shows that growth-oriented policies that remove unnecessary governmental constraints and lower marginal tax rates bring about a higher degree of resource utilization and efficiency.

In the U.S., growth promotion through private initiative and innovation has done wonders in reducing unemployment and idle capacity. In Germany, substantial unemployment persists, which can be reduced through deregulation and tax reform.

This is also imperative in view of the European integration efforts. While European integration will undoubtedly provide a positive stimulus to growth, those countries that have a flexible industrial structure will be in the best position to take advantage of the new opportunities.

In a nutshell, the experience of Germany and the United States shows that <u>structural flexibility in a framework of price stability</u> will provide the most conducive environment for economic growth. I believe that both nations have now recognized the advantages of such a course.

Both Germany and the United States have done very well in terms of growth and improved living standards during the current expansion. If we imitate each other a bit more and implement the lessons learned, I am confident that we can further extend this record to the benefit of all our citizens.

Thank you very much.