

TRENDS IN THE GLOBAL ECONOMY
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Good afternoon! I'm pleased and honored to have the opportunity to discuss with the leaders of Jamaica's business community the forces shaping change in the world's economy and the directions in which I think that change will lead us. This international gathering is symbolic of the most important of those changes, the dramatic shift toward internationalization of markets that is an irreversible but desirable factor in these times. As we become ever more involved in global business, we become more aware of the necessity to think of ourselves as internationalists—not out of altruism but on the basis of comparative advantage, which works to benefit everyone by having all countries do what they do best. The resulting efficient use of resources means that consumers will have the widest possible choice of goods and services at the lowest price.

Along with these benefits, though, internationalization also demands adjustments in some of our attitudes. The reality of a global market requires us to acknowledge that the economics of production and consumption, once viewed largely as domestic matters, apply across national borders. However, few of us are properly conditioned to making the same kinds of free-market concessions across boundaries as we are within them. Rather, we often try to protect our national economies. Unfortunately, even countries like my own, with considerable experience in the free market, have difficulty coming to terms with all the consequences of working within this new framework. That is why we see pressures to increase protectionism—the antithesis of international market integration—despite abundant evidence that protectionism runs counter to the interests of one's own citizens as well as people in other nations.

I'd like to talk this afternoon about three trends which will have profound effects on the way we do business and thus on the way we live as this century draws to a close. These are (1) the shifts from national economies to a truly multinational economy; (2) the shift in trade patterns that is progressively bringing Transpacific trade to equal prominence with Transatlantic trade; and (3) the shift in the employment base from manufacturing to services. I'll have a few things to say about the damage that countries which attempt to reverse the trend toward internationalization with protectionist barriers could do to their own and the world's economies, and I'll close with some thoughts about what these trends might imply for the direction of Jamaica's economy.

The Shift to a Multinational Economy

Like so many events in the contemporary world, the shift from multiple national economies to a global marketplace is occurring more rapidly than most people had expected. Still, it shouldn't surprise us, because it is the inevitable result of developments set in motion at the end of World War II, the most recent episode when nationalism was allowed to bring chaos into the world community. After the war, the United States, the only advanced economy that had not had its productive capacity ravaged by the fighting, pursued a conscious strategy of encouraging free-market economies as alternatives to the types of government-controlled economic systems that were so intimately linked with the military aggression of the Axis powers. Through the Marshall Plan and other forms of assistance, the U.S. rebuilt former allies and enemies alike into trading partners in the belief that participation in competitive markets would help prevent a return to such external hostilities or tyrannical domination internally.

As time passed, U.S. consumption of foreign-produced goods replaced aid as the locomotive pulling along the free world's economy. However, people in the U.S. were

slow to awaken to the impact foreign products could have on the domestic market, because, with a few exceptions, the quality of these early imports was quite poor. Through much of the 1960s and 1970s, Americans seem to have been focused inward with the Vietnam War and the Arab oil embargo as the main international events which intruded upon their thoughts. Only in the 1980s, through the indelible impressions made by the wild volatility of oil prices and the ballooning of the trade deficit, did the consciousness of the U.S. business community return to the reality that events outside the United States resonate increasingly within our boundaries. Suddenly imported cars were challenging the country's "big three" automakers in both price and quality, electronic products were packed with instructions written in Japanese as well as English, and new shoes and clothing seemed to come almost exclusively from Taiwan, Hong Kong, and Korea.

This imbalance of trade in manufactured goods was accelerated in large measure by the U.S. government's fiscal policy, a policy which pivoted upon a tax cut in 1980 coupled with an increase in defense spending. As federal revenues diminished relative to spending, the U.S. government had to borrow increasingly to make up the difference. It became clear that our domestic pool of savings was insufficient to provide the necessary funds to support both private investment and government financing needs. The shortfall drove up interest rates on investments in the U.S., attracting the attention of foreigners with excess capital to invest. Countries like Japan, West Germany, and the OPEC nations also had hefty trade surpluses. These countries were thus able to become major players in the U.S. bond and equity markets as well as direct investors in U.S. businesses. In the process they bid the dollar to great heights as they scrambled for the dollars to purchase U.S. government securities and other investments.

The resulting high dollar made our products expensive overseas and so reduced sales

while making foreign goods cheaper here—a double blow from which several U.S. industries have yet to recover, despite the equally dramatic slide in the relative value of the dollar since February of 1985. Where U.S. business was hurt abroad as the dollar climbed, the economies of some of our major trading partners are now suffering as the dollar falls. The real winners in the dollar's roller coaster ride were the newly industrialized countries of Taiwan, Korea, Hong Kong, and, in our own hemisphere, Brazil. Those nations gained increased exposure for their products. They have been able to hold on to the market share they built because, until recently, their currencies had not appreciated as much relative to ours as have those of Japan and Germany. In fact, some even peg their currency to the dollar. This has had the effect of accelerating the trend toward their incorporation into the world economy, making them forces that cannot be ignored as we look toward the end of the century.

Another factor that will continue to promote market competition the world over is the production of goods by multinational companies operating inside foreign countries. It is estimated, for example, that in 1985 U.S. companies located in Japan produced and sold more than \$53 billion worth of goods, an amount that exceeded the U.S. trade deficit with Japan of \$46 billion that year. The multinationals are the leading edge of greater integration in the world marketplace because they not only bring competitive foreign products to market, but they also contribute to the economy of the country in which they are located. This contribution is immediate in the form of wages, rents, taxes, and purchases of materials. It also has long term effects through the introduction of alternative methods of management and marketing. The opening of Japanese-owned factories in the U.S. has evoked considerable discussion regarding ways that Japanese management techniques, such as quality control and employee involvement in decision making, can be applied in the U.S. workplace. While all consumers benefit from the competition provided by the multinationals, then, even the industries against which they

compete benefit from this sharing of knowledge.

Along with the growing worldwide integration of production and consumption has come the internationalization of capital markets. The advent of 24-hour-a-day trading in commodity, security, and currency markets symbolizes the global nature of current economic activity at the same time that it makes funds available in a variety of vehicles to advance that activity. The Euroyen and Eurodollar markets, together with other funds that now flow easily across national boundaries, provide potential fuel for economic expansion not only in the developed nations but in the Third World as well, though competition for these funds will be keen in the latter region.

Shift in Trade Patterns

In what I have said so far, the importance of Asian nations in international developments is readily apparent. The shift to prominence in world trade of the Pacific Rim nations constitutes the second major trend that I would like to discuss. Over the past decade, the share of U.S. trade oriented toward Asia has grown from one-fifth to one-third. The shares of Europe, Canada, and Latin America all remained at about the same levels over the decade, Asia's gain coming largely at the expense of the oil-producing countries. Increasing levels of quality, along with the U.S. dollar's appreciation, combined to allow Japan to capture a large share of our foreign purchases. Recently Taiwan, Singapore, Korea, and Hong Kong have also boosted their shares as a result of these factors and their lower costs. We can expect manufacturing to continue to shift toward the East, particularly in light of the fact that there are even cheaper sources of labor--Thailand and China--on the horizon.

Europe's share of U.S. trade remained at a consistent 24 percent over the ten years just ended, and I expect that to continue. The potential danger Europeans face

over the longer term is the self-inflicted one of protectionism. European Economic Community reluctance to participate more fully in restructuring tariffs will, if present tendencies continue, isolate those countries more and more unto themselves, a development that would lead to stagnation.

The outlook for the third major group of nations, the LDCs, will be mixed. Population pressures will continue to beleaguer Mexico and a number of other developing nations. One of the most challenging issues involving the LDCs is the debt many of them owe to foreign banks. Although the size of these external debts makes it extremely difficult for these countries to repay given their present levels of economic growth, they are, at the same time, in need of fresh capital to invest in new factory equipment and materials for production. The creditor nations have a stake in both sides of the dilemma, because on the one hand the balance sheets of some of their largest banks are showing signs of strain, and on the other their industries need the potential markets in the LDCs as an expanding outlet for their products. The progress of internationalization as a force promoting health in the world's economy into the next century hinges in no small measure on how bankers, government leaders, and international organizations like the World Bank and the International Monetary Fund ultimately resolve the debt problem.

Indeed these international agencies and others like GATT (the General Agreement on Tariffs and Trade) will play a major role in the evolving pattern of trade. Mexico has joined GATT, and we have had encouraging signals of interest from two non-market economies, China and the Soviet Union. The upcoming round of GATT talks will shed considerable light on the way international events will evolve in the nineties. A considerable degree of balance could be returned to the international trade scene if GATT were extended to cover service industries like insurance, hospital management, and data processing—potentially some of America's most profitable exports. With

direction from GATT, intellectual properties also could be better protected so that, along with earnings from books and musical compositions, research and development efforts—an extremely valuable and undercompensated export—might be returned to its originators together with the inflow of products they inspire. To realize the benefits of a global marketplace, we must allow the principle of comparative advantage to operate. The United States, I believe, is conceding that less developed countries have a comparative advantage in manufacturing many of the industrial goods long made domestically. By the same token, developing nations must play by the rules of the game and allow the U.S. to reap the benefits of our present comparative advantage in generating ideas for new products and in providing high quality services.

Shift from Manufacturing to Services

The growing urgency of extending recognition of proprietary rights to services in international markets underscores the third of the major trends I mentioned at the outset—the shift of labor from employment in manufacturing to services. This receives a great deal of attention in the United States because our economy has been moving in that direction for some time. The change is one that is important to economies at all stages of development, however. That is because the rapid improvement of manufacturing techniques in the U.S. and other advanced nations, along with the availability of technology and machinery for purchase, means the manufacturing of goods will become more efficient everywhere. Thus not only in the advanced industrialized economies but in developing countries as well, fewer workers will be required to produce the goods needed to supply the demands of consumers and investors. More of the labor force can then be diverted into services ranging from preparing food to entertainment to medical, financial, and legal services.

In the United States, much discussion of this shift in economic emphasis centers

upon fears that that the nation's manufacturing capacity is eroding to the detriment of national interests. In fact, however; U.S. manufacturing has remained at a fairly constant proportion of GDP despite requiring a smaller percentage of the work force. The analogy that helps to visualize this trend is the reduction in U.S. agricultural employment from the beginning of the century, when it stood at about 40 percent of the labor force, compared to today's 3 percent. Agricultural techniques and machinery so increased the efficiency of production that surplus crops were harvested and a surplus of labor could go to work on the assembly lines. The difference between the shift from agriculture to manufacturing and the shift from manufacturing to services now under way is the demands the new order will make on the labor force. Whereas the assembly line jobs that replaced agricultural work were largely unskilled jobs, the service industry will be weighted in favor of information-type employment that requires better educational preparation. In order to ensure an adequate supply of trained workers for the service industry, societies around the world will have to commit more thought and funds to education.

Over the long run, the shift toward services will add to international market efficiency by encouraging different economies to do what they each do best. Consider, if you will, that we as individuals and as entire economies exchange our labor for goods and services. We produce goods and services in order to consume goods and services. Obviously, there is no requirement that we consume only the goods and services we produce domestically; more and more those goods and services are produced elsewhere in the world. It matters little where the things we end up purchasing are initially produced, though, as long as current levels of consumption can be expected to grow and living standards increase. Thus, if the rest of the world is willing to offer more for U.S. engineering services, say, than for its television sets, it would make no sense for American industry to put engineers on the television assembly line. The resulting

decision to sell engineering services and the countless similar decisions made in the context of market discipline pushes toward optimal employment of products and skills existing in an economy at any given time. At the same time, it promotes the diversity that all of us as consumers value. However, these benefits can be obtained only if markets remain free and open. They will be lost if countries attempt to hold on to industries that were important in the past by artificial protectionist measures rather than allowing the free market to set the course of economic development. Let me turn for a moment to the question of protectionism, since it poses the greatest danger to the positive potential I see in international economic development.

Protectionism

Because it limits the ability of a country's economy to do what it does best, protectionism places artificial restrictions on internal economic development along with the artificial barriers presented to import competition. In an open market, consumers benefit from the competing efforts of several companies that produce and market similar products because the prices of each are held to their lowest profitable level. When foreign products are made artificially expensive by tariffs, the test of market discipline is eased for protected producers. Imported goods then cost consumers more, and even domestic prices for the same items often rise because there is less competition driving them down. When the price of foreign goods goes up or when their quantity is limited by quotas, another form of import barrier, we are left with fewer selections and ones that cost more. The cumulative effect of elimination of competition through these and other types of non-tariff barriers (like subsidies and local content requirements) are considerable. One recent study estimates that if all existing tariffs and quotas were removed, the benefits to the U.S. economy would be nearly \$13 billion per year.

Another argument advanced in favor of protectionist policies is that they preserve

jobs for one's own countrymen. Any preservation of jobs promoted in this manner, however, can only be temporary, since propping up an industry that has become inefficient ultimately becomes an unsustainable task. Even more important, protecting jobs in one industry can lead to losses in another. For example, just in my region of the United States—the South—an estimated 14,000 retailing jobs might have been lost had President Reagan not vetoed the 1985 textiles and apparel trade bill. By blunting competition, tariffs cause prices to rise and so hurt retailers. Thus from the viewpoint of the larger economy, protectionism is self-destructive. Aside from costing at least as many—probably more—jobs than it saves, protectionism robs our economic system of one of its great advantages, the continuous process of change that makes industry responsive to the needs of consumers. By keeping capital and labor resources in noncompetitive industries which survive only because they are propped up by trade barriers, we choke off the creation of potential new firms, industries, and jobs.

Worst of all, trade-distorting measures can lead to great costs on the international stage, where protectionism guarantees more protectionism. This arises from both internal and external dynamics. Internally, when any pet industry of a politically powerful group is protected, industries with political clout in other areas begin clamoring for similar preferential treatment. The great disaster of the Smoot-Hawley tariff imposed by the U.S. government in 1933 came about as vested interests were added to the list in just this way until on average tariffs ended up at over 50 percent on an ad valorem basis.

Externally, protectionist measures are almost assured of evoking retaliation. In the recent confrontation between the United States and Canada over lumber we saw very specific examples of this process. Were we to slap a duty on their wood, the Canadians were prepared to tax feed corn accordingly. Again in attempting to help one industry,

another type of producer entirely removed from the original dispute is threatened. The Smoot-Hawley tariff helped tip the world toward just such a spiral of tit-for-tat maneuvers, and the end result was the collapse of world trade and a lengthy depression. Some even tie it to the ultimate outbreak of world war. I believe we have come too far toward internationalization to retrace that unhappy course.

Implications for Jamaica

I've talked about the changes I see taking place in world trade—the shift toward a fully multinational economy, the changing patterns of world trade, and the gradual move toward a service-based economy and I've discussed the threat to realizing the greatest good from these movements posed by protectionism. I'd like now to say a few words about what these changes in the world economic order might mean for the future of Jamaica. I'll refer to Jamaica's participation in the international economy on at least two broad fronts. One is your major merchandise exports, bauxite and alumina as well as sugar, and the other is tourism.

The shift in world trade patterns toward the Pacific, where much primary manufacturing now takes place, makes it likely that the bauxite and alumina industries will continue to face hard times. In the long run, Australia is closer to the growth markets for these raw materials and therefore better positioned to capture the lion's share of sales. I fear that the downturn you have experienced in these industries during this decade will prove all too permanent. Similarly, sugar is beset by difficult commodity market conditions, including chronic worldwide oversupply, conditions that are unfortunately exacerbated by increasingly protectionist quotas in the United States. That is not to say that these industries will cease bringing in foreign exchange—indeed, bauxite and alumina exports improved in the first quarter of 1987. I am suggesting that the best strategy perhaps may lie in developing alternative industries and a more

diversified economy. In terms of manufacturing, the Caribbean Basin Initiative has not generated the flow of foreign direct investment we once hoped it would largely because potential outside investors are concerned that future political developments might endanger their investments. Toward that end, business and government leaders in Jamaica need to arrive at some mechanisms that will guarantee the long-term integrity of foreign-owned firms. Another impediment to investment is the anticipation of difficulty in repatriating profits. A move toward permanently abolishing foreign exchange controls would ease this situation.

Aside from these considerations of your manufacturing base, Jamaicans may also want to think about developing other sectors of the economy, including tourism and related services. This lovely island is blessed with a powerful and renewable natural resource in its ability to attract tourists, particularly from the United States, but also from Japan, Canada, Europe, and other parts of the world as time goes on. With your unique culture, known around the world through the pervasive influence of your music, you have an individual identity superior to any that could be developed by a public relations firm, though, by the way, your "Come back to Jamaica" promotion has attracted a good deal of positive attention in the States. To maximize this natural advantage, you might look at ways to expand the infrastructure and services that accompany tourism. Over time Jamaicans themselves could play a larger role in developing and managing the hotels and restaurants which accommodate the island's guests and in providing the cultural activities that entertain them. These businesses require a relatively low capital investment at the outset and for that reason encourage entrepreneurship in a broad base of the population. For example, a "Mom and Pop" restaurant can serve high quality food and be attractive to customers precisely because it is homey, unpretentious, and an authentic representative of the culture people have journeyed to experience. Recent studies in the United States have shown that small

businesses have been the key source of employment growth. Thus tourism can serve as a catalyst for stimulating economic growth in general.

In my opinion, it would be a mistake for you to forgo these opportunities in the belief that hosting tourists somehow compromises your dignity. Any stigma that might once have been attached to earning income through one of the service industries is surely a thing of the past, since the most advanced economies are, as I just mentioned, evolving into service economies. In my own area of the United States, for instance, many people work hard to promote Atlanta's convention facilities, Florida's amusements and resorts, Tennessee's country music heritage, and New Orleans' cuisine in order to attract even more visitors. Those concerned with economic development have come to recognize that this industry, like others in the service sector, is a tremendous source of jobs and income. Jamaica's comparative advantage in attracting tourists could help you marshal some of the earnings to support your transition to an economy of the twenty-first century. These earnings will be needed for investing not only in modern equipment, but also in human resources. The service- and information-based economy that is already taking hold worldwide will demand well educated workers. Investing more in education is a necessary strategy for any country that wants to be a participant in this new economic order.

In this way, Jamaica can have a bright future in the evolving world economy. I would like to leave you with one word of caution, however, and that is to forgo the protectionist response to the challenge of import competition, regardless how persuasive the arguments in its favor might at first seem. Even the concept of protecting infant industries through an initial period of adjustment carries potentially dangerous consequences and must be applied, if at all, selectively and with great caution. Just as a child will not mature to independent adulthood if it is spoiled by overly dotting parents, an

industry that grows up in an environment where it is not forced to compete will have great difficulty making the adjustment to the free market. If it cannot enter the market on its own and remains a ward of the state, it defeats the initial purpose of promoting overall economic growth. As difficult a master as it often is, the free market is in the final analysis the best provider of the goods and services its participants demand. With new developments in China and the Soviet Union we see that the forces of internationalization are extending the reach of the free market to areas of the world that have had controlled markets through much of this century. This is no time, then, for those of us who have long enjoyed the benefits of liberalized trade to reverse our course and close off growth and efficiency simply to avoid healthy competition.