The U.S.Economy "Back on Top"?

Economic Growth and the Rhetoric of National Power

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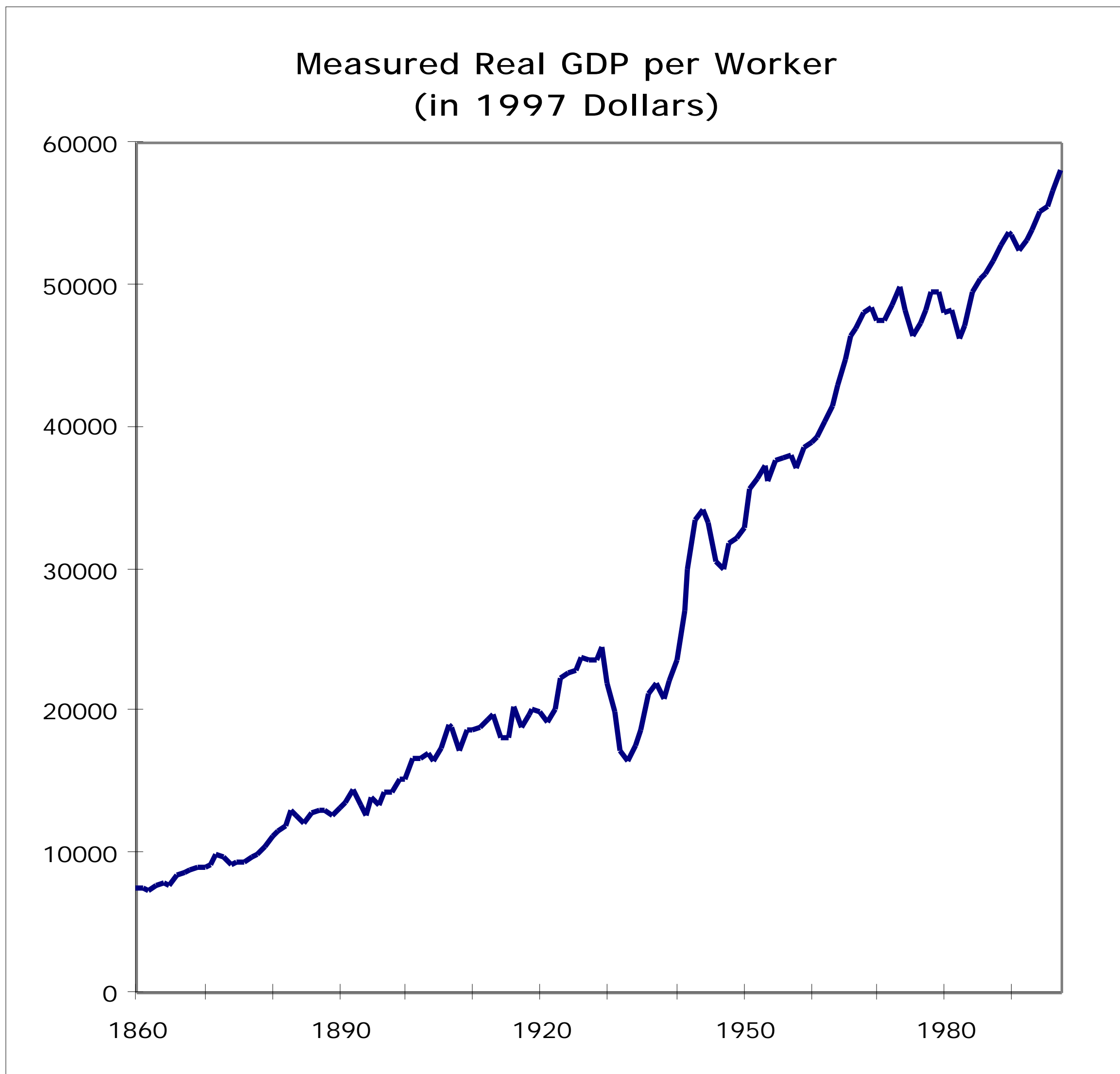
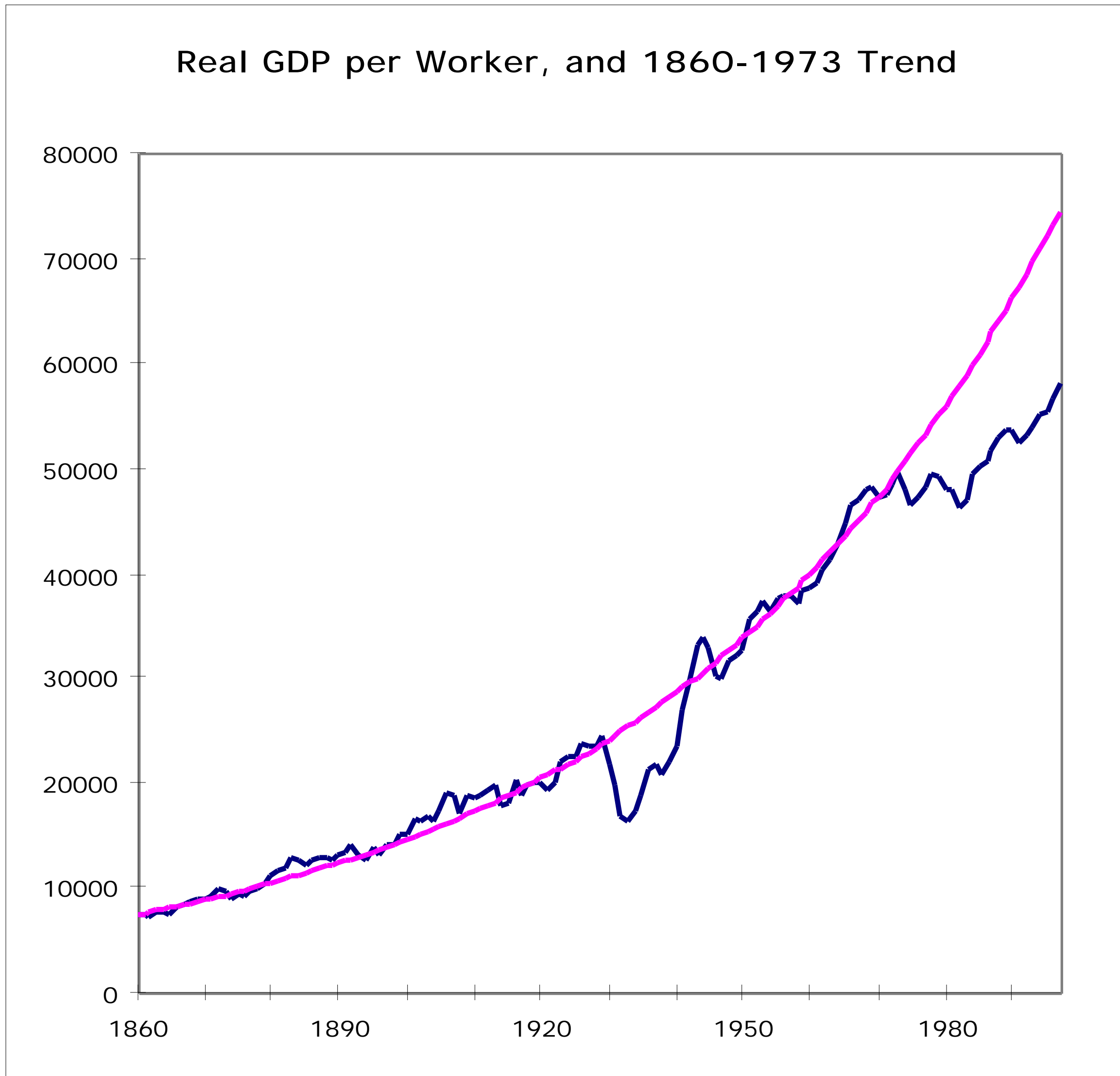


- Measured real GDP per worker has experienced two interruptions in its growth in the twentieth century--the Great Depression, and the period of turmoil of the 1970s.

- Those aside--even including those episodes--the most visible fact about twentieth century growth is its speed: measured output per worker today is some four times what it was at the start of the century. Adjust for the declining work year, and we have a five-fold multiplication of measured material wealth in this century.

- The fastest achieved in any previous century was the --perhaps--doubling of measured real output per worker in the 19th century, and the--perhaps--fifty percent increase in measured real output per worker in the 18th century.

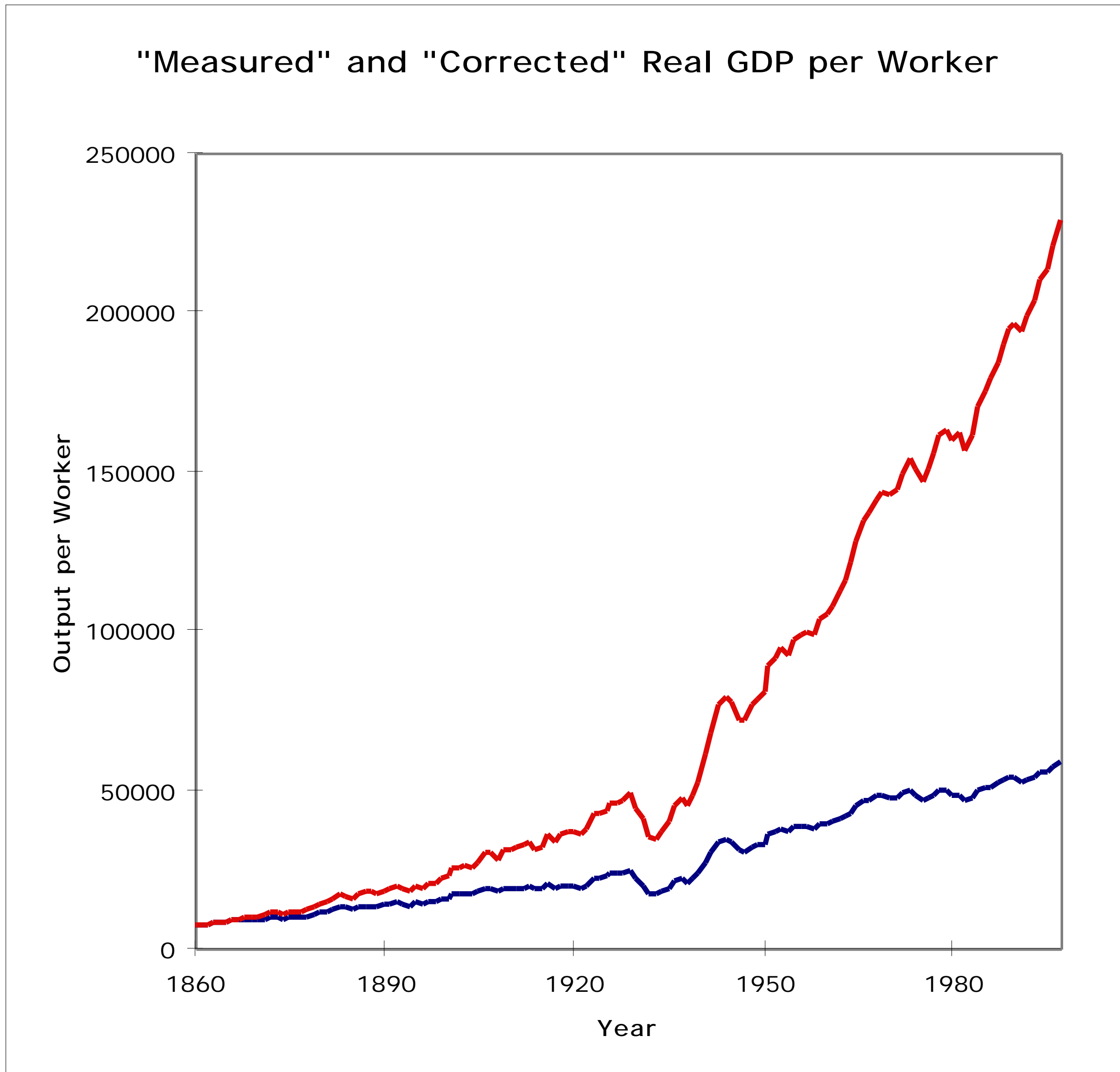
- Before then,a doubling of material living standards was the work of millennia--if there were such doublings. It is not obvious that you had a higher living standard as a Campanian peasant in the 17th century than as a Campanian peasant in the 2nd century B.C.



- If you want to criticize aggregate U.S. economic growth performance over the past generation, the best way to do it is with a graph like the one above: comparing what measured output per worker is now with what it might have been.

- In its essentials, this graph simply notes that the American economy has not continued growing at its 1940-1973 pace--as indeed it has not.

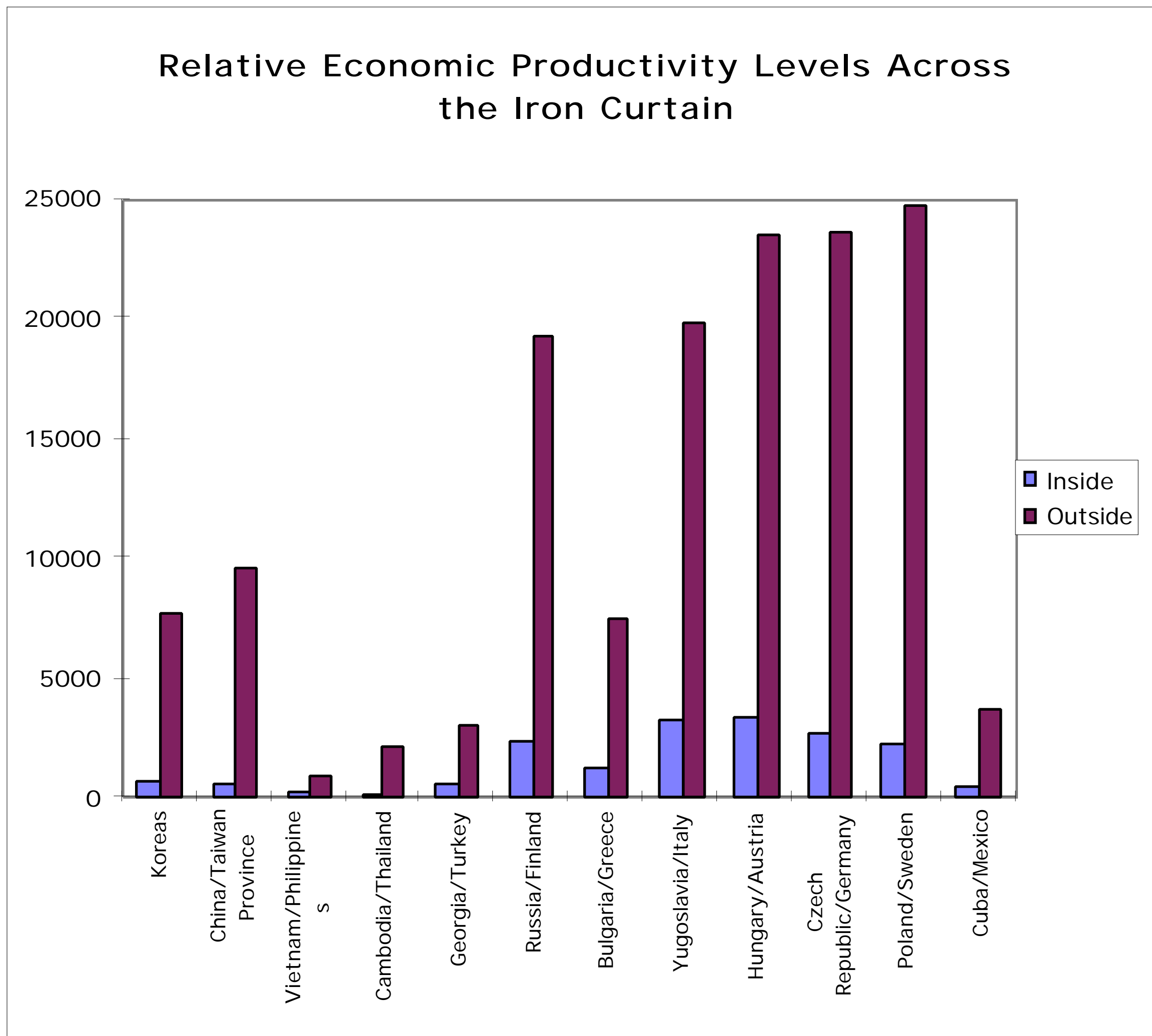
- But remove the 1940-1973 Great Keynesian Boom, and growth today looks much more back on track. 1940-1973 appears more unusual than 1973-1997



- "Correct" as best we can for "measurement error" in calculating real output per worker, and find that real output per worker since 1860 has grown not sevenfold but thirtyfold.

- Is there *anyone* back in 1860 or 1890 with whom you would swap places and regard it as an *improvement* in material well-being?

- The fundamental problem with the standard measures is that when they say that "output per worker in 1860 was equal to $7,400 at 1997 prices," you automatically think of what you could buy today with $7,400. But that is not the right thought experiment. The right thought experiment is: "what could you buy today with $7,400 *if you were restricted to buying those commodities that were produced back in1860?* "

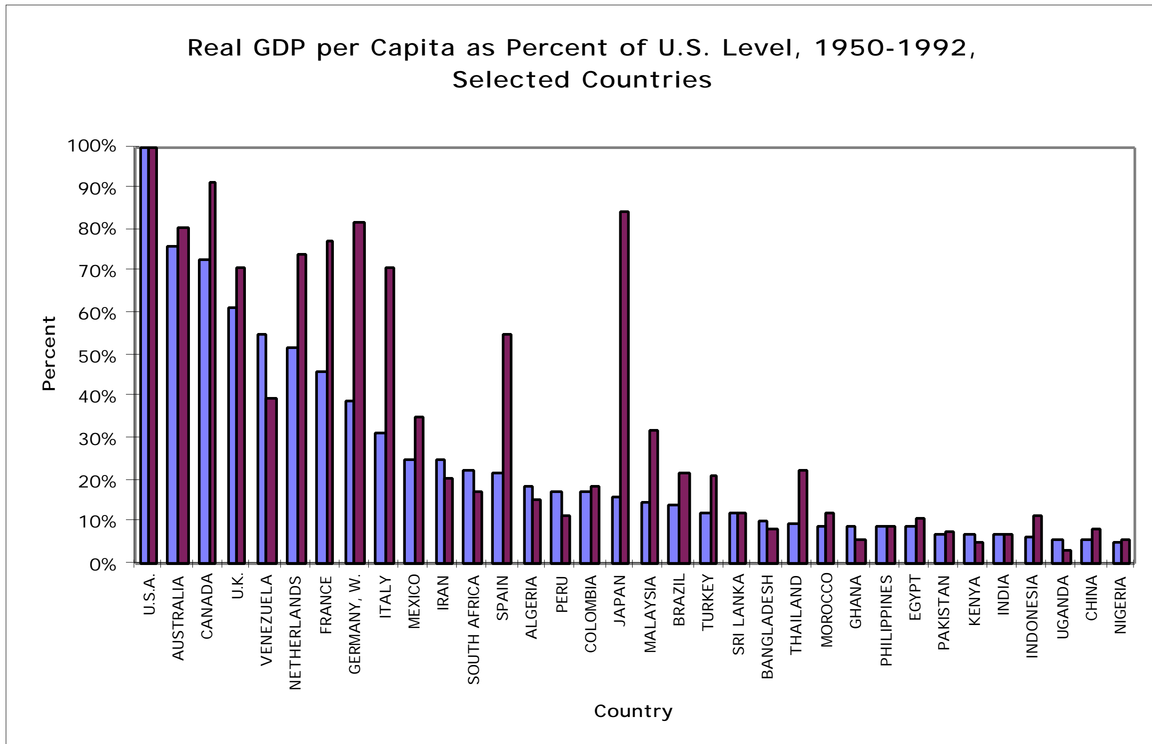


- A first--enormously important--source of relative inequality between nations in our world today is the fact that some spent a generation or two or three behind the "Iron Curtain."

- Wherever you look across the "Iron Curtain," the economies outside are vastly more productive than the economies inside--even though their relative productivity levels were very similar before the Red or the People's Liberation Army showed up.

- Communist regimes were good at some things--building T-34 tanks in large numbers, siting industry in strategic locations so it would still be functioning after *Panzergruppe Hoth* crossed the border, relocating large populations to Siberia, re-enserfing the agricultural population. Communist regimes were not good at long-run economic development.

- 88% of the average material productivity of an economy appears to have been lost as a result of its being placed behind the iron curtain.



- Even leaving the Iron Curtain aside, the world economy today is a more unequal place than it was in 1950--and a vastly more unequal place than it was a century ago.

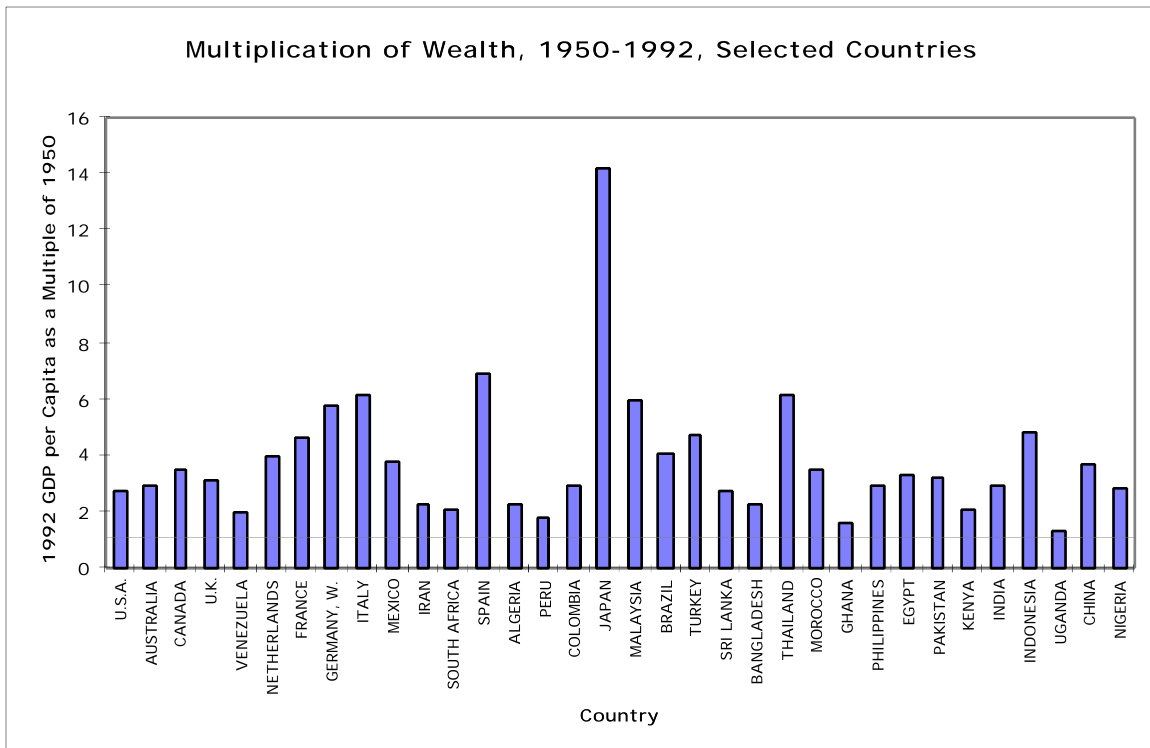
- Since 1950, strong signs of *convergence* among the OECD--that is, the set of Marshall Plan recipients.

- Since 1950, no signs of *industrial succession* (*a la* Holland and England in the late eighteenth century, or Britain and the U.S. and Germany at the start of the twentieth).

- Since 1950, several examples of spectacular *catch-up* : Indonesia, Thailand, Malaysia, Turkey, Japan, Brazil, Spain.

- Since 1950, relative catastrophe and retrogression as well: Venezuela, Argentina and Uruguay (not shown), Peru, Iran, Algeria, Bangladesh, Ghana, Kenya, Uganda.

- Why? What went right in southern Europe after World War II? What has gone wrong in the southern cone of South America, and in Africa? What went right in East Asia?



- We can take a look at development since 1950 and join the "glass is half full" fraction: the "4 billion people now on the escalator to modernity" fraction.

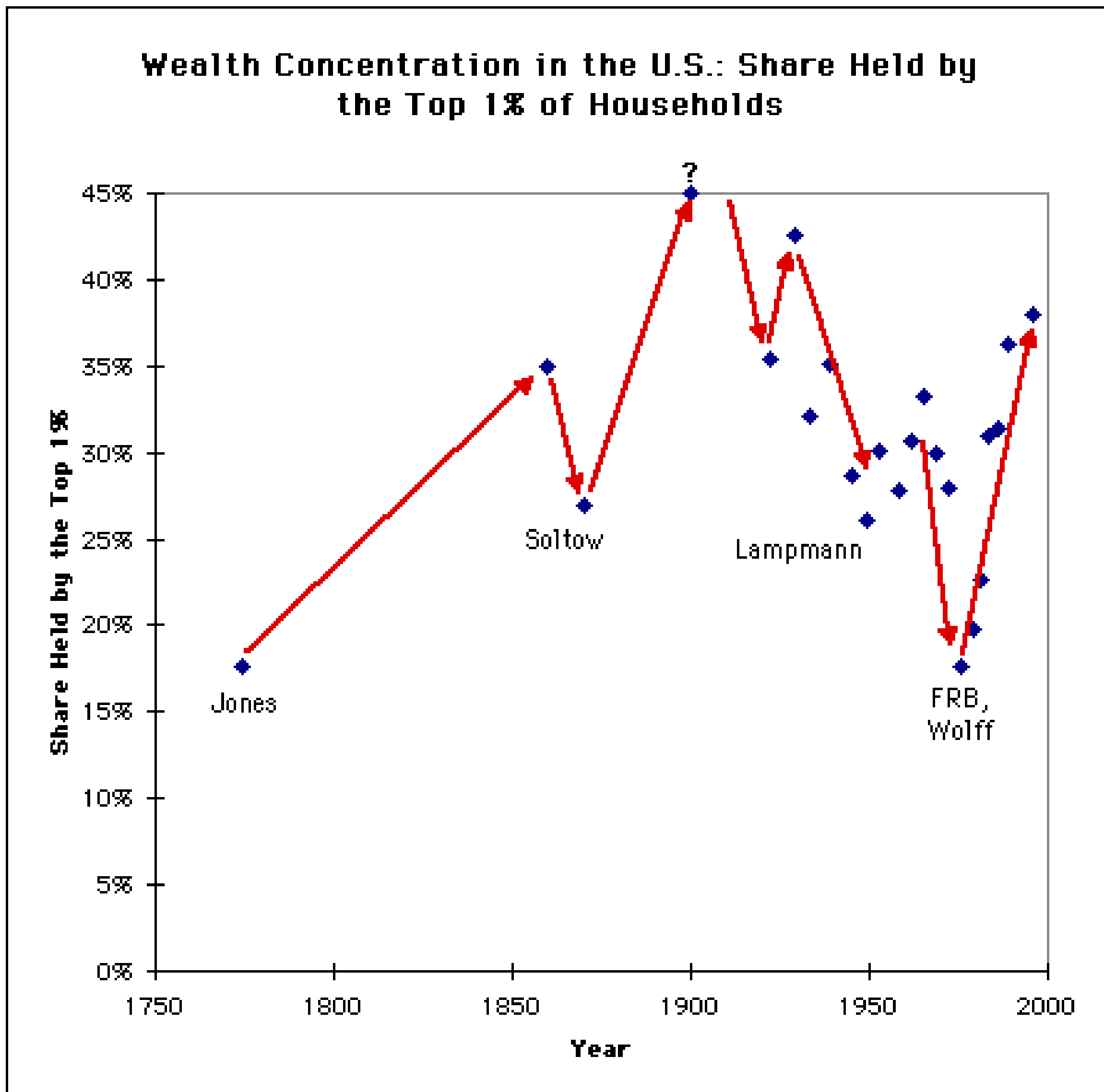
- Even *very bad* regimes are having a hard time keeping standards of living from rising.

- Standards of living of even slow-growing developing economies are rising faster than industrial core standards of living rose in the nineteenth century.

- The extraordinary opportunities for technology transfer mean that whenever a developing economy gets a pro-development government, its growth can take off like a rocket.

- If its GDP per worker grows at only 2.5% per year, in 120 years even Nigeria will have as high a level of living standards and economic productivity as the U.S. does today. From a millennial perspective, the fact that one country started its industrial revolution in 1790, a second in 1890, and a third in 1990 is less important than that they all went through the industrial revolution.

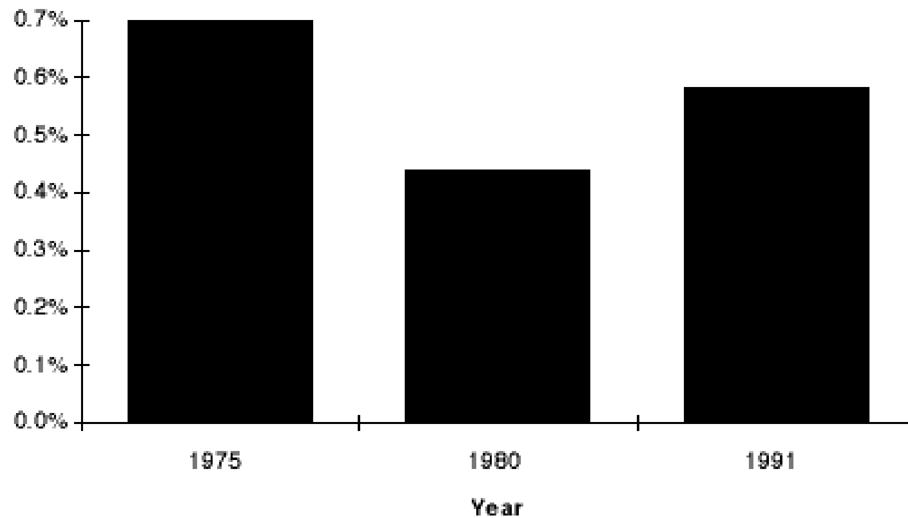
- But will the demographic transition come fast enough to banish the spectre of Malthus from South Asia? Will AIDS be worse for Africa than the Black Plague was for Europe? Has the spectre of Malthus been banished from the world as a whole?



- We used to believe in the "Kuznets curve": income and wealth inequality rises sharply during an industrial revolution, peaks approximately when the industrial share of the labor force peaks, and then (for political *and* economic reasons) falls with the coming of social democracy--mass education, union power, restrictions on immigration, inheritance taxes, progressive income taxes, the works.

- Now it is clear that we are on a Kuznets roller-coaster. Why? Three possibilities:
  - Failure of the educational system to keep up with the skill requirements of modern production. The computer-literate earn 20% more than the non-computer literate.
  - We elected those people: falls in the real value of the minimum wage, large-scale union busting, a reduction in the progressivity of the income tax, and what Robert Kuttner called "the revolt of the haves" had powerful effect, both directly and by changing *mores* concerning what relative pay levels should be.
  - This second is tied up with a third: the U.S. is not a social democracy, it just pretended to be one as long as the memory of the Great Depression remained strong.

Non-Oil Imports from Low-Wage Countries,* as a Share of GDP



*Countries with manufacturing wage levels less than half the U.S.

- Two non-possibilities:
  - International trade: the U.S. imports no higher a share of GDP from low-wage countries today than in 1960. You see, back in 1960 Italy and Japan were low-wage countries.
  - Immigration: according to David Card, immigrants' skill levels are remarkably close to those of the native-born population. Texas and Southern California are dealing with the impact of a large wave of very under-trained and under-educated immigrants. The rest of the country is not--or is not yet.

Walter LaFeber, *The Clash*

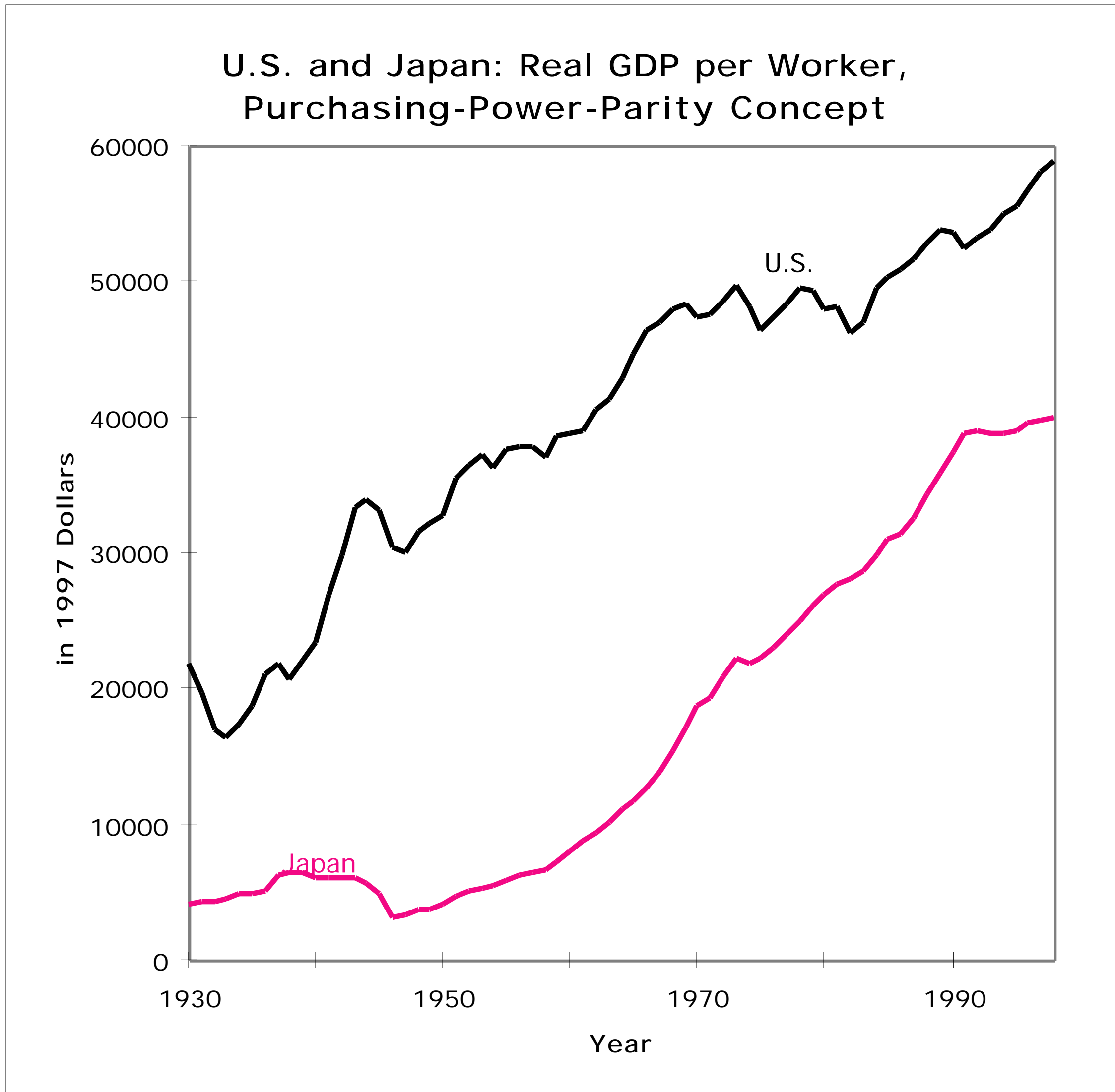
Walter LaFeber's Vision of U.S.-Japan Relations

Focus on the penultimate chapter of LaFeber's book, the chapter "End of an Era" that covers 1973 to 1996. In this chapter seven points are repeatedly driven home with a pile driver:*

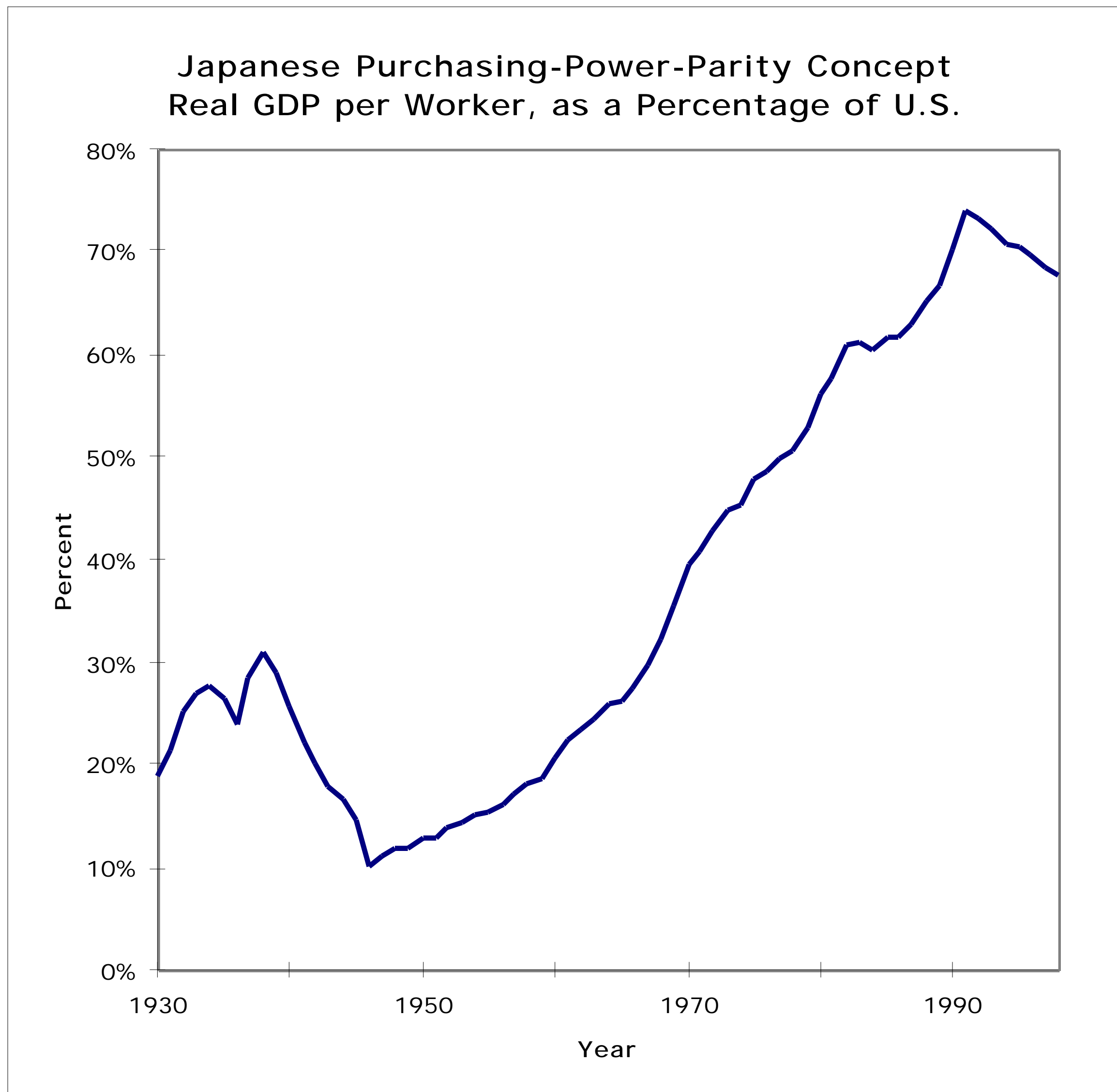
1. Japan plays the U.S. for a sucker by refusing to play by the free-trade rules of the game.
2. The seriousness of the clash between Japan and the U.S. is always increasing.
3. The American government is incompetent, while the Japanese government is very, very competent.
4. The U.S. "loses" foreign market after market to ferocious Japanese competitors.
5. Industry after industry falls to the tide of Japanese imports--which devastate the American economy.
6. America's economic decline is clearly visible in its rising trade deficit.
7. When the Japanese cannot conquer by trade, they conquer by buying up assets.

The conclusion? That "Americans... trust[ed] to the magic of the international marketplace--a marketplace that MITI and the keiretsu had long worked to fix" (p. 379); as "Chalmers Johnson observed: 'The Cold War is over, the Japanese won" (p. 384).

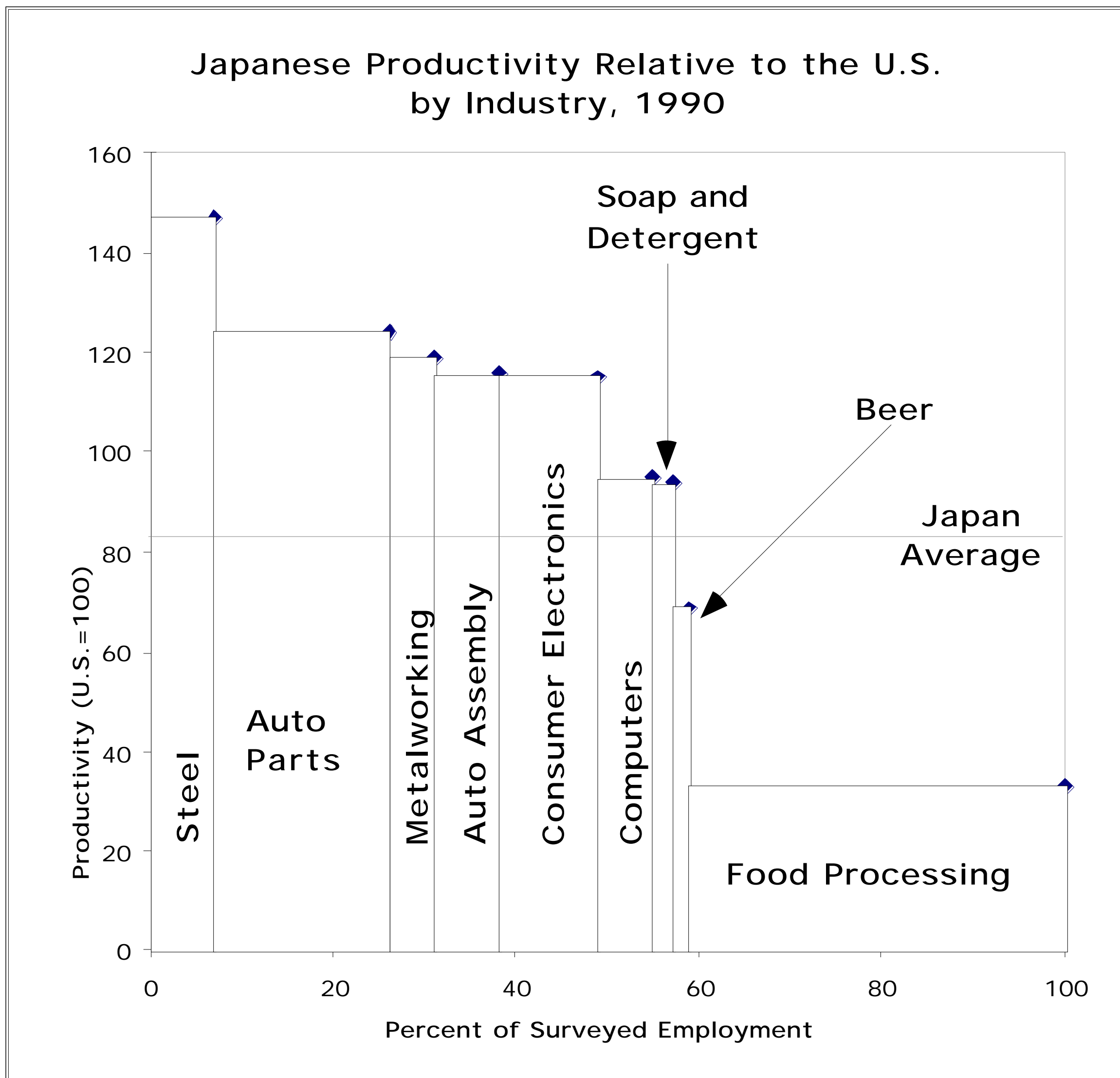
*There is--occasionally, very occasionally, twice in fact--a contrarian voice: "Secretary of State [George] Shultz... avoided a confrontation... if the Japanese 'wanted to pay astronomical prices for goods that are cheaper elsewhere, that is more their problem than ours... if we wanted to see our real problem we should look in the mirror (p. 380)".



- In spite of all Japanese "advantages"--MITI and keiretsu and elite bureaucracy and not playing by the rules and public investment in research and development and its homogeneous population and its excellent secondary education system and all that--its GDP per worker is less than two-thirds that of the United States.
- The Japanese growth miracle of 1945 to 1990 was an amazing achievement, boosting Japanese productivity relative to American sevenfold.
- But it had been preceded by a disaster--World War II--that had cut Japanese productivity relative to American by two-thirds. It took until the very end of the 1960s for the Japanese economy to make up the relative ground that had been lost as a result of World War II.
- The gap in productivity today remains large.



- A diligent reader of LaFeber looking at these figures would rub his or her eyes in disbelief.
- "How can this be?" he or she would ask. Japan has exploited the U.S. by not playing by free-trade rules; by provoking and winning clashes of increasing seriousness; by outmanoeuvering the incompetent American government; and by conquering foreign market after foreign market. U.S. industry after U.S. industry has succumbed to Japanese competition, as shown by the ever-rising U.S. trade deficit. And what Japanese exporters cannot win, Japanese financiers can: Americans now cut timber and catch fish for export to build houses and feed their Japanese bosses.
- So how can the U.S. still have so much more productive an economy?



- Japan's extraordinarily low productivity in branches of economic activity outside of export-oriented manufacuturing is in large part due to its political order
- The Liberal Democratic Party and the elite bureaucrats so-often praised as the public-sector stewards of Japan's economic growth have striven mightily to keep Japanese agriculture, distribution, services, and non-export manufacturing unproductive.
- Prohibitions against the importation of rice boosted Japanese rice prices to seven times world levels.
- Government bureaucrats believe that they have a mandate to protect existing stores against competition-- especially efficient competition from large-scale enterprises that would handle distribution more efficiently.
- If the Ministry of International Trade and Industry has been successfully working to enrich Japan by boosting productivity in the export-oriented manufacturing sector, the rest of the Japanese government has been equally successfully working to make sure the rest of the Japanese economy remains unproductive.

The Value of U.S.-Japan Trade

The smarter Japan-bashers--James Fallows, for example--will admit that Japanese economic policies have been extraordinarily destructive of Japanese economic welfare. But, they go on to say, Japan's economic policy makers do not care about utility or consumer welfare or the national standard of living--it is a producer rather than a consumer economy, aimed at creating economic hegemony rather than enhancing human welfare.

The key point to grasp, they say, Japan's economic policies have harmed us as well. The U.S.-Japanese economic relationship as it has been conducted--by Japan's producer-oriented, consumer-ignoring developmental state and the U.S.'s incompetent government--has been a lose-lose relationship.

What was the value of U.S.-Japan trade in 1996?

U.S. Exports:	**$70 billion**	Alternative value of resources:	**$50 billion**
U.S. Imports	**$115 billion**	Cost if produced at home:	**$150 billion**

Deficit: **$45 billion**

- **$15 billion to fund U.S. exports to other countries (+$5 billion)**
- **$30 billion invested in the U.S. (+$10 billion)**

TOTAL VALUE OF RELATIONSHIP: +$70 billion