Johnson, Howard C. - Articles and Speeches (1966-1967)

The Outlook for International Business

Address by

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It is a sobering experience for a New Yorker to address this conference. Your recent chronicler, Christopher Rand, writing in the "New Yorker" reminds me that in Los Angeles aversion to New York is about as strong as aversion to San Francisco. And, while the cliff-dwellers of Manhattan may well be eating and drinking themselves to death--with nearly 40 per cent of their expenditures going into the purchase of food and into eating and drinking places, you gentlemen have been managing a growth in manufacturing employment five times that of the nation as a whole.

But then as a banker in quest of substantial funds I welcome any opportunity to meet with financial leaders--and I am particularly pleased to meet with bankers of Southern California who, over the past two decades, have increased bank deposits at a rate almost double that of the nation as a whole.

And I am happy to report that a few easterners are even coming to recognize that, with the new Music Center and the intellectual activity built around Caltech and UCLA and the aerospace industry, Angelinos may be well on their way to a successful challenge of both the cultural leadership of New York City and the unique intellectual and electronics complex of Harvard and MIT.

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But now to get down to business, again I learn from Christopher Rand that Los Angeles has become the leading seaport on the west coast. He also makes a statement which was somewhat astonishing to me--that one worker in every four in Los Angeles is now dependent on foreign trade. So it is altogether fitting that this Business Outlook Conference should devote a few minutes to the outlook for international business.

Ladies and gentlemen, we meet at a time of remarkable growth of world business. During the first six months of 1966, world trade increased at the unusually fast rate of 12 per cent on an annual basis. This compares with an increase in 1965 of eight per cent; between 1956 and 1963 it averaged only seven per cent.

Gross national product of Common Market countries combined with the United Kingdom is expected to rise in real terms by 4-5 per cent in 1966. At the same time the continued upsurge in the American economy over the past 12 months, together with the further growth in Canada, has created a new situation in world economic affairs. Virtually all the industrial countries are simultaneously enjoying high levels of employment.

This booming state of world business owes something to the Vietnamese war, which has led to a strong demand for goods and services of many kinds and has created additional incomes which themselves have generated further activity. And the problems of managing the boom have been made infinitely more difficult by the war.

What is the outlook for the principal trading nations? We begin with the United States which, despite the rapid growth in other major economies such as Germany and Japan, still accounts for about one third of world output and for nearly 17 per cent of world exports.

The gross national product of the United States, after allowing for price increases, rose 5½ per cent last year, compared with the recent average growth rate of around 4-4½ per cent. This rapid rate of expansion has continued into 1966 and the third quarter's statistics of American output showed a further increase in activity.

Some evidence is accumulating which points to a slowing of the recent rapid growth rate in the United States; among the factors involved a shortage of capital should be mentioned prominently. But domestic sources are far better equipped than the World Bank to weigh these against the continuing thrust of rising defense spending and outlays for business plant and equipment.

In Canada the economy has been enjoying an unusually long period of expansion. Over the past five years the gross national product of Canada has been rising at an annual rate of about six per cent. But, as in the United States, Canada has reached the point where its resources, especially of manpower, are becoming increasingly tight and where more emphasis must be placed for the time being on price stability than on further growth.

The position of the principal economies outside of North America is varied. The recent tribulations of the United Kingdom are well known to you. The British Government has been forced to take stern measures. These measures have already brought about some slackening of the British economy. The British Motor Corporation, makers of Austin and Morris cars, has recently dismissed 12,000 workers as well as reducing working hours of another 40,000 because of a sharp increase in its stock of vehicles and in the stocks held by dealers. Cutbacks have also been announced recently by British manufacturers in other fields--domestic appliance, textile, steel, chemical and plastics. In the circumstances, any growth in the British economy next year seems likely at best to be modest.

Other leading trading nations in Europe, Germany, Sweden, Belgium and Holland, have also taken action in recent months to check inflationary pressures in their economies. The most significant developments have been in Germany, which has been one of the pacemakers of the expansion in the European Common Market during the past few years. As in most other industrial countries, unemployment in Germany is low and prices and wages have tended to rise too quickly. To stabilize the situation, the German Government has placed restrictions on spending by the public authorities and has provided the central bank with powers to limit commercial bank lending.

There are signs now that the boom in Germany may already have passed its peak. Internal demand has recently declined and capital expenditure by industry has lost some of its strength. According to a report published last month by a group of German economists, the growth of the German economy has fallen this year from five per cent to about three per cent. For 1967, these economists forecast an increase of only two per cent. This, however, runs counter to the view held by other authorities, who believe that higher exports and public spending will carry the economy up quite substantially in 1967. At the moment, no clear, firm judgment on Germany seems possible.

In every country I have mentioned so far, with the possible exception of Germany, the prospect for next year is for a slower rate of growth than in 1966. This group of countries accounts for over 50 per cent of world exports and for nearly that proportion of world imports. Thus, from our analysis of the outlook for this major block of countries, world trade seems likely to be less buoyant during the next 12 months.

There are three countries, however, all of growing importance in world trade, which help to brighten the outlook. I refer to Japan, France and Italy. These three countries have experienced their inflationary troubles earlier than the countries I have just discussed and have already emerged from a period of retrenchment. Their economies then started going ahead at a fast pace, providing growing markets for other countries in the process. Indeed, imports of Japan, France and Italy more than doubled in the past eight years and now account for about one sixth of the world total. After a slow 1965 imports of these three countries increased in the first half of this year in annual terms by around $4 billion. This was about one third of the total increase in world imports during the period.

Japan, of course, has been one of the economic stars of the past few years. Output has been rising at an annual rate of about 10 per cent, and after the slowdown in 1965 it is expected to return to about this figure in the near future. In France the gross national product should advance about five per cent this year, and is expected to accelerate next year to nearer six per cent. Expansion in Italy has been slower to revive, but there, too, it is now getting well under way. There is ample slack in the economy still to be taken up. This situation of course is now complicated by recent flood disasters, the full impact of which is not accurately known.

I turn now to the worldwide shortage of capital, as this is one of the outstanding features of the world economic situation.

In the United States, as you know well, interest rates have risen sharply from the relatively low levels ruling at the end of 1964. The yield on U.S. Treasury bills has been at a height only touched briefly during the crisis in 1929; that on medium-term government bonds has been higher than at any time since shortly after World War 1.

Rates in other countries have gone higher still. In the United Kingdom yields on government securities rose at one stage over seven per cent and even top-class companies have had to pay over eight per cent for long-term finance; second-class companies have had to pay more than nine per cent. In Germany, money has been even dearer than this, with yields on government securities over eight per cent and the price of money to industrial borrowers sometimes in double figures.

This sharp rise in interest rates, though a worldwide phenomenum, cannot be said to be entirely due to any one single factor. Nonetheless, there is a handful of major causes which can be pinpointed. In the United States business has made big demands for capital to carry stocks, finance expenditures on new plant and equipment, and to sustain production at the high levels to which it has risen, as a result largely of the Viet-Nam war.

Abroad, too, interest rates have been forced up by a combination of strong demand from industry and the public sector, and by government monetary restrictions. In the United Kingdom, for example, a ceiling has been fixed by the Bank of England above which lending by the commercial banks must not be allowed to rise. This has created a squeeze on credit, making it necessary for a number of industrial companies to pay an exceptionally high price for the funds they need. Then again in Europe the shortage of capital has been intensified by the U.S. program to reduce the deficit in its balance of payments and by the reaction of the private banking system to this program.

This worldwide shortage of money has understandably caused concern. The Managing Director of the International Monetary Fund, M.Pierre-Paul Schweitzer, felt it necessary at the recent annual meeting of the Fund and World Bank in Washington to warn governments that further squeezes on liquidity, and further rises in interest rates, could have an adverse impact on particular categories of financial institutions and borrowers, with consequent repercussions on confidence and on economic activity.

One reason for hoping that the peak of pressure on interest rates lies behind us is that there now seems to be a growing realization in a number of countries that the recent reliance on monetary weapons to check inflation has been excessive. It is recognized that greater use of fiscal measures such as tax increases and cuts in government spending are needed in many countries to deal with inflationary pressures.

The next question is whether the recent downward movement in interest rates will be carried far; the general feeling at the moment is that it will not. As the World Bank pointed out in its annual review this year, the pressure on interest rates is likely to persist as long as public sector expenditures in the industrial countries remain high, as long as private investment and consumption demand are strong, and as long as capital flows between industrial countries are subject to government restraints.

Demand for funds in the United States remains strong. It is hard to see the shortage of capital easing to any great extent here in the near future. Overseas, it is possible that the easing may come more quickly. In the United Kingdom in particular some slackening is already evident, though there, too, interest rates seem unlikely to revert to earlier levels for some while yet.

This worldwide shortage of capital has undoubtedly been a factor in the recent fall in prices of industrial securities on world stock exchanges. I hardly need remind you of the recent performance of Wall Street. From the new peak reached last February, New York Stock Exchange prices dropped back this summer by around 25 per cent and, though better lately, are still about 20 per cent down. The pattern has been similar abroad. In London, stock markets have been down to their lowest level for several years. Prices in Paris have also retreated and appear to have been reacting sharply for the slightest reason. All the major stock markets, indeed, are now well below their all-time highs. Over the past year the Belgian market has fallen by more than 20 per cent, the German market by about 18 per cent, the Dutch market by 16 per cent and the Canadian and Swedish markets by about 14 per cent. Only two markets have moved decisively against the trend--they are the Italian stock market, which has risen during the past 12 months by about 28 per cent, and the Japanese market, which has risen by about 14 per cent.

I mention these figures because they show, with the two major exceptions I have mentioned, a strikingly uniform picture. The widespread uncertainty about the future which they appear to indicate, whether justified or not, could itself have an impact on the economic situation through its effect on consumer spending and, more important, through its effect on business attitudes toward expenditure on new plant and equipment.

To sum up--the course of the Viet-Nam war is of major significance in the outlook for world trade in 1967. The shortage of capital can be expected to have a dampening effect on activity of major industrial countries during the coming year. The faster growth in prospect in Japan, France and possibly Italy will help offset the slower expansion which seems likely in most other major industrial countries. In 1967 growth in world trade should continue, not at this year's exceptionally fast pace of 11-12 per cent, but nonetheless at a pace which should at least equal the 1957/63 average of seven per cent.

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Now let us take a somewhat longer look--first to the East and then to the West.

In 1960 the Organization for Economic Cooperation and Development--OECD--set for its members the target of raising their combined economic output by 50 per cent during the decade of the 1960's. The OECD has now reported on the progress made in the first five years of this period. The gross national product of the area, even excluding Japan, which was not a member of OECD when the target was fixed, has been increasing on average by 4 3/4 per cent a year, well in excess of the 4.1 per cent needed to reach the target figure. OECD now believes that there is every chance that OECD countries will achieve their target for the decade.

This five-year outlook for European nations is a very favorable one indeed. Nevertheless, when we look at the world economy from the World Bank headquarters in Washington, we are struck by the more rapid rate of growth that is appearing as characteristic of many of the economies in the Pacific, compared to the Atlantic community. You know about your own more rapid growth compared to the East. Across the Pacific, Japan's 10 per cent growth rate is of course over twice as fast as Western Europe.

As if responding to the dynamism of Japanese expansion, the other Pacific economies are catching this virus of rapid growth. Taiwan and Hong Kong for some years now have been growing at 7-10 per cent per year. Korea has likewise begun to join in this with rates of growth of 7-8 per cent; last year exports jumped by 60 per cent! Malaysia and Singapore, now that the Indonesian confrontation is over, also are getting into the swing.

Australia has been growing for years at a satisfactory Atlantic rate. Now that the economy has been oriented more toward Japan--through mineral exports in part, but also wool and manufactures--Australia has begun to accelerate towards a Pacific growth rate. New Zealand, with greater sentimental ties to the United Kingdom, is only now beginning to make a serious effort to take advantage of the Pacific opportunities.

The Philippines, hopefully, under the new administration, has begun to accelerate its very recent slower rate of growth.

Thailand, in part for special reasons, has also been showing the Pacific rate of growth of 7-8 per cent per year.

Indonesia and Burma have been cases apart as a result of mismanagement of their economies. In the long run, Indonesia may become an asset to the Pacific region instead of a drag.

The Vietnamese war is also a factor in all of this. On the one hand, it must be considered a positive economic factor for the Pacific countries in providing some of them with quite easy markets and foreign exchange earnings. On the other hand, it is an economic threat for exactly the same reasons--by diverting energies from the harder work of building up permanent peacetime markets.

The point which emerges from this analysis is that as one looks five years ahead, the Pacific basin, with the tremendous pull of your booming California on one side, and booming Japan on the other, should be replete with opportunities for American business.

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Ladies and gentlemen, these opportunities owe their existence in no small part to the substantial official capital transfers that industrial countries have made to Pacific rim countries. And development of business will be furthered by additional capital transfers in the years to come.

Since 1961, the level of official net capital flows from the main industrial countries to the developing countries has remained static at about $6 billion a year. As a proportion of the rising incomes of the industrial countries, these net official flows have declined from an estimated eight tenths of one per cent to six tenths of one per cent. To be sure, export of private capital has increased, but most of it is directed to only a few countries, and discouragingly little of it goes to the poorer ones. The problem is complicated by the fact that more than half the inflow of development finance is now being offset by the return flow in the form of amortization, interest and dividends.

Paradoxically, during this period when the relative volume of aid has been dwindling, the capabilities of the developing countries to absorb aid have been growing. World Bank studies conclude that the developing countries--outside the Sino-Soviet areas--each year could effectively use, on the average, some $3-4 billion more of development finance than they are now receiving. This judgment is based on estimates country-by-country of the capacity of the developing countries to save and to export, to follow acceptable economic policies, and to plan and carry out high-priority development.

The capacity of the industrialized countries to support an effective assistance effort has also been rising. Assuming that effective financial assistance would cost an added $3-4 billion a year, the industrialized countries can certainly afford it. Their national income has been increasing, in the aggregate, at the rate of $40-50 billion a year. If only one per cent of this five-year increase were devoted to additional development support in 1967, we would be well on the way to a satisfactory level of assistance. Thank you.

INFORMATION DEPARTMENT

The attached news story appeared on page 57 of the May 9, 1967 issue of:

THE NEW YORK TIMES
THE WALL STREET JOURNAL (NEW YORK)
THE JOURNAL OF COMMERCE (NEW YORK)
THE WASHINGTON POST (D.C.)
THE EVENING STAR (WASHINGTON, D.C.)
TIME (NEW YORK)
NEWSWEEK (NEW YORK)
THE TIMES (LONDON)
THE FINANCIAL TIMES (LONDON)
the Providence Journal - Providence -

# World Bank's Role Growing

## R.I. Area Bankers Hear the Director Of New York Office

By JOSEPH L. GOODRICH
Journal-Bulletin Financial Writer

The World Bank will play an ever increasing role in coordinating aid going to underdeveloped countries from the United States and other countries, a senior member of that bank's staff predicted last night.

Howard C. Johnson, director of the New York office of the World Bank, told 135 Rhode Island area bankers at the Rhode Island Country Club in Barrington that more countries are looking toward the bank for this coordination because of its know-how in the field of economic development.

Mr. Johnston spoke at a forum and seminar program of the Providence Chapter of the American Institute of Banking. He said that one of the biggest moves that will be made by the World Bank within the next 20 years will be to broaden its field of overall coordination of foreign aid programs.

"Safe Bridge"

The World Bank, formally known as the International Bank for Reconstruction and Development, was described by Mr. Johnson as "a safe bridge over which public and private funds flow into underdeveloped countries."

He said the bank raises from 400 to 500 million dollars in public and private funds each year for loans to promote economic development in these countries.

Increasingly, Mr. Johnson said, the United States and other Western nations are looking to the World Bank to coordinate their foreign aid because the bank, through its technical know-how and investigatory procedures, is equipped to establish justification and priorities for foreign aid projects, thereby assuring the most effective use of aid funds.

Funds "Worth More"

He also noted that the United States is "making an effort" to channel more of its foreign aid money directly through the bank because "a dollar spent through the World Bank is worth more than a dollar spent unilaterally."

This is because the World Bank, under its "project loan" program, insists that any equipment or services needed for an economic development project for which a loan is made be purchased through international competitive bidding, Mr. Johnson said.

William H. Heisler 3rd, president of Citizens Savings Bank and Citizens Trust Co., was chairman of the meeting.