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Are the 1980s Like the 1930s?

Observers of the history of international lending bring a sense of *déjà vu* to the "debt crisis" of the 1980s. Recent debt-servicing difficulties in Latin America, Eastern Europe, and elsewhere represent only the latest in a series of similar episodes stretching back over centuries, report NBER Research Associates **Barry Eichengreen** and **Richard Portes** in **Debt and Default in the 1930s: Causes and Consequences** (*NBER Working Paper No. 1772*). However, institutional arrangements that govern international lending have changed so fundamentally that the interwar experience may contain few meaningful lessons for the 1980s, they conclude.

Historically, the problems encountered by sovereign borrowers frequently have culminated in default; the defaults of the 1930s are merely the most dramatic and generalized instances of a recurrent phenomenon. Quite often, defaulting debtors were able to reenter the international capital market only to default again; creditors were then criticized for reckless lending, ascribed to myopia or excessive competition.

In the 1930s as in the 1980s, illiquidity was not confined to any one country or region. Moreover, in neither period could the problems experienced by external debtors be attributed exclusively to domestic economic and political developments. Rather, they were and are linked to disturbances in the world economy including real interest rate shocks, commodity price fluctuations, and exceptionally severe recessions in industrialized regions. These parallels lead many observers to fear a replay of the collapse

of international capital markets witnessed in the 1930s.

But much has changed since the 1930s. The switch from bond to bank finance, by changing the provisions of loan contracts and reducing the number of creditors party to negotiations, may make rescheduling of debt an alternative to outright default. In addition, the International Monetary Fund (IMF) now serves as an external lender of last resort to illiquid borrowers. At the same time, the IMF provides useful signals to the capital market, conferring information on domestic adjustment programs. The establishment of central banks as domestic lenders of last resort, the spread of deposit insurance, and the implementation of macroeconomic stabilization policies also significantly diminish the likelihood of a downturn in the business cycle on the scale of the Great Depression.

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Through a careful analysis of the interwar period, Eichengreen and Portes conclude that developing countries did have alternatives to default even during the Great Depression. They question whether noneconomic factors were decisive, as some have claimed. Instead, simple economic variables go a

long way toward explaining the incidence and extent of default in the 1930s. They find that the proportion of a country's debt in default during 1934–38 was positively related to its debt/GDP ratio, the extent of deterioration of its terms of trade from 1929 onward, and the increase in its government budget deficit during 1929–31.

Finally, Eichengreen and Portes provide a long-run perspective on default and on the remedies available to creditors. They present new estimates of the rate of return on foreign loans floated in the 1920s, in different years, to different countries, and to different classes of borrowers. For example, average realized rates of return on government-backed loans were 3.25 percent for dollar issues and 5.41 percent for sterling issues. The rate of return on default-free loans was close to 6 percent for both dollar and sterling issues, but default hit dollar bondholders much harder than those holding sterling bonds. Despite the preoccupation with sovereign default, Eichengreen and Portes conclude, investors who made loans directly to national governments and held the bonds to maturity ultimately received respectable rates of return. DF

Productivity in Japan and the United States

Costs were 34 percent higher in the U.S. auto industry than in the Japanese auto industry in 1980. Most of this difference was caused by a low rate of capacity utilization in this country, according to a recent study by NBER Research Associate **Melvyn Fuss** and **Leonard Waverman**. Therefore, now that the U.S. auto industry has scrapped much of its excess capacity, the Japanese advantage is considerably smaller.

In **The Extent and Sources of Cost and Efficiency Differences between U.S. and Japanese Automobile Producers** (*NBER Working Paper No. 1849*), Fuss and Waverman estimate that the Japanese cost advantage would have been only 12 percent in 1980 if American producers had been operating at Japanese levels of capacity utilization. Although the cost of labor was higher in the United States, this was somewhat offset by lower costs for capital and materials.

Fuss and Waverman conclude, "In 1980 the primary place where North American producers could not compete with the Japanese was in the design of automobiles with appropriate quality and size characteristics, rather than in relative production costs." Now that American auto producers have closed a number of plants and shifted production toward

smaller cars, they are much more competitive with the Japanese in terms of cost. The recent appreciation of the yen should further erode any cost advantage the Japanese may have.

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In a related study, NBER Research Associates **M. Ishaq Nadiri** and **Ingmar Prucha** report on productivity growth in the U.S. and Japanese electrical machinery industries. Between 1974 and 1979, output in those industries grew by 4.9 percent annually in the United States and by 6.4 percent annually in Japan. During the same period, employment here grew by 1.4 percent annually and fell by 2.5 percent in Japan. As a result, the annual growth in labor productivity was 3.5 percent in the United States and 8.9 percent in Japan.

In **Comparison and Analysis of Productivity Growth and R and D Investment in the Electrical Machinery Industries of the United States and Japan** (*NBER Working Paper No. 1850*), Nadiri and Prucha estimate that the rise in productivity in both countries was primarily caused by increasing returns to scale and by technical progress. They also report that the U.S. industries spent a higher percentage of revenue on R and D than the Japanese industries, but that the Japanese invested a higher percentage of their output in capital.

Would Higher Taxes on Beer Cut Youth Drinking?

Higher taxes on beer would reduce both the number of youths who drink and the amount that they drink, according to NBER Research Associates **Douglas Coate** and **Michael Grossman**. This might also have a significant effect on traffic fatalities.

In **Effects of Alcoholic Beverage Prices and Legal Drinking Ages on Youth Alcohol Use** (*NBER Working Paper No. 1852*), Coate and Grossman also find that raising the minimum drinking age to 21 would decrease youth drinking.

According to a national survey of the drinking habits of youths 16–21 conducted in the late 1970s, over 11 percent of youths drink beer four to seven

times per week; they are termed frequent drinkers. An additional 27 percent drink beer one to three times per week (fairly frequent drinkers), while 43 percent never drink beer. Fewer than 1 percent drink wine or hard liquor four to seven times per week; about 65 percent of the youths never drink these beverages.

“Higher taxes on beer would reduce both the number of youths who drink and the amount that they drink.”

In their study, Coate and Grossman estimate how three possible tax increases would affect youth drinking. The first option would adjust the federal excise tax on beer for the amount of inflation since the tax was last changed in 1951. Such a tax increase would raise beer prices by 12 percent and lower the number of frequent and fairly frequent young drinkers by about 4 percent. The number of youths who do not drink beer would rise by 5 percent.

The second option would tax the alcohol in beer as heavily as the alcohol in hard liquor. This would raise the federal excise tax on a six-pack of beer from 16 cents to 52 cents. The number of frequent and fairly frequent young beer drinkers would fall by about 7 percent, and the number of youths who never drink beer would rise by 8 percent.

The third option, combining these two taxes, would raise beer prices by 57 percent, reduce frequent and fairly frequent drinking by 21 percent, and increase abstinence by 25 percent.

Coate and Grossman estimate that raising the drinking age to 21 in all states would reduce the number of frequent drinkers by 27 percent. The number of fairly frequent drinkers would drop by 7 percent, and the number of abstainers would increase by 8 percent.

income of a household headed by someone aged 35 to 44. By contrast, the 1984 average income for a babyboom household (headed by someone aged 25 to 34) was 75 percent of that of the 35–44 household.

In **Changes in the Age Distribution of Income in the United States** (*NBER Working Paper No. 1766*), the three economists report that the number of households headed by someone aged 25 to 34 doubled between 1968 and 1984. Their share of total income rose 20 percent, but their income per household fell 12 percent relative to the next older group (35–44). Their share of property income also increased substantially for a large part of the period but began to decline around 1981 (the year that some babyboomers began moving into the next age group).

“Since 1968, the incomes of the elderly have risen sharply relative to the incomes of other age groups.”

During the same period, the authors report, “the share of total income received by households headed by those 65 and over increased over 30 percent.” Relative to the 35–44 group, that was a 25 percent increase in income per household. At the same time, for this group and those aged 55–64, relative earnings fell while relative income rose. The share of total property income among those 65 and over also rose, by about 12 percent. However, the authors note that some of that increase represents a change in the number of households. Furthermore, they caution that property income may be underreported in the Current Population Survey, the source of their data. Boskin, Kotlikoff, and Knetter attribute some of this pattern among the older groups to the growing contribution (both absolute and relative) of Social Security to their incomes and to the declining labor force participation that other economists have noted.

Elderly Gained, Young Lost Income since 1960s

Since 1968, the incomes of the elderly have risen sharply relative to the incomes of other age groups. At the same time, the relative incomes of those aged 25 to 34 (the babyboom generation as of 1984) have been falling, according to a recent study by NBER Research Associates **Michael Boskin** and **Laurence Kotlikoff**, and **Michael Knetter**. Despite this fact, the average income in an elderly household (age 65 and older) in 1984 was only 54 percent of the average

Union Organizing

Police unions have become increasingly common in recent years. Indeed, over 60 percent of municipal police departments were unionized by the end of the 1970s. According to NBER researcher **Casey Ichniowski**, the process of police unionization is crucially connected to the state laws that govern collective bargaining.

In **Public Sector Union Growth and Bargaining Laws** (*NBER Working Paper No. 1809*), Ichniowski

studies 1000 municipal police departments and finds that the ones not covered by collective bargaining laws rarely have police unions. Departments *allowed* to bargain under their state laws are more likely to have unions, while those departments covered by laws *requiring* employers to bargain have the highest rate of unionization.

“Increases in the union wage premium have reduced the chance of unions winning representation elections.”

Interestingly, the extremely low rate of unionization among police departments not covered by bargaining laws does not necessarily indicate a lack of interest in unionization. In **Public Sector Recognition Strikes: Illegal and Ill-Fated** (*NBER Working Paper No. 1808*), Ichniowski reports that nonunion police departments in states without bargaining laws, or with laws that merely allow bargaining, are more likely to strike for recognition than nonunion

departments in states requiring employers to bargain. However, departments that do engage in such strikes are no more likely to obtain recognition than other nonunion departments.

In another NBER study on unionism, Research Associate **Richard Freeman** reports that increases in the union wage premium have reduced the chance of unions winning representation elections. That is because the greater the union premium, the more management resistance there is to unionization and the more unfair labor practices are undertaken by management. The effect of this increase in management resistance outweighs the direct effect of potential higher wages on worker voting. Freeman estimates that as much as one-quarter of the recent decline in votes to unionize may be the result of the increase in the union wage premium during the 1970s.

His results are reported in **The Effect of the Union Wage Differential on Management Opposition and Union Organizing Success** (*NBER Working Paper No. 1748*). Freeman's research is based on data on NLRB elections, unfair labor practices, and union wage differentials by industry from 1950 to 1980.



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