

A ¥en for more data

THE US government's intervention to buoy up the value of Japan's currency on June 17 testified to the global proportions of the crisis that has its roots in the 1980s. But debate about strategies for preventing the recurrence of another boom/bust is bedevilled by the paucity of data. The OECD's Secretary General, Donald Johnston, warns: "Political leaders in all democratic societies have an obligation to encourage informed debate on these questions which will influence our lives in so many ways".¹

But the OECD is not able to propose new strategies for structural change to remove whatever is the cause of the recurring recessions, which in Japan is verging on a 1930s style deflation. The OECD calls for "continued vigilance and improved surveillance of the world's economy", and joins in the political chant for "transparency in the international system".

Western governments berated the Asian "tigers" for causing the crisis which is undermining the European economy and could even feed into the US. But official analyses of what caused the Asian collapse contain nothing to encourage the view that additional data would have prevented the crisis in Thailand and South Korea.

Experts, including US Federal Reserve Chairman Alan Greenspan, have skated close to references to asset prices as an element in the destabilisation process. But they lack a theoretical framework that explains why economic prosperity cyclically terminates in collapse. For example, in its annual report issued in June, the Bank for International Settlements stated:

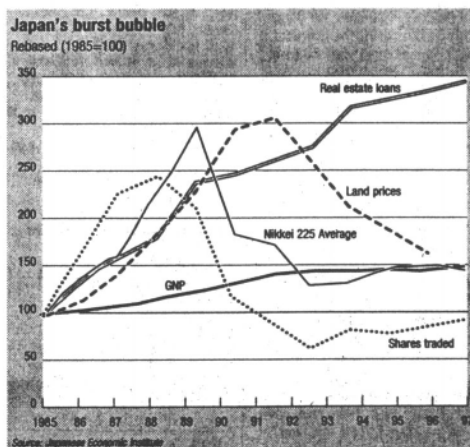
"Economic circumstances can change quite quickly and all economic projections and judgements should be approached with a proper sense of humility.

"Even the broad success of policy makers in reducing consumer price inflation may have attendant dangers if this inadvertently encourages the development of asset price bubbles, while at the same time reducing the policy scope to resist them."

A theoretical black hole underpins such analysis. Armed with an economic theory which comprehensively embraces all the

relevant forces which drive the economy, it is possible to see circumstances changing from a long way in advance. There was no need to be caught unawares by the Asian crisis. It could have been predicted years in advance.

The BIS's word that gives the game away is "inadvertently". Asset price bubbles such as the one causing protracted pain in Japan today are not accidents. Economic success feeds into asset prices, but the economic consequences vary according to whether the flow of funds is directed at investment in the shares of companies or in the land market. Land booms ultimately strangle the entrepreneurial economy, whereas finance in the hands of companies is invested to expand production.



As we see from the graph, share prices which become unrealistic quickly adjust themselves to the underlying realities. But in the land market, dealers and banks hang on in the hope of realising the expectations that were nurtured in the growth phase of the cycle. And the tax system nurtures these unrealistic expectations - although the Japanese experience of the 1990s, with banks reluctant to write off their land related debts, has proved exceptional.

Media commentators spread the illusion that capital flows could be controlled to prevent another boom/bust. The IMF continues to agonise about how to balance liberalisation of the money markets with stability at the level of the street - but unable to offer any analytical statements to separate their insights from the voodoo

economics of the Reagan years.

Which means the Asian crisis will be replicated in the next emerging market to be favoured by the institutional investors. In 1995 the total assets of insurance and investment companies and pension funds in the OECD area amounted to more than \$24.4 trillion (an astonishing 106.7% of GDP). These funds slush around the world and no amount of "transparency" will prevent them from searching out the highest returns available.

The next boom is likely to be in the resource rich regions of Eastern Europe, where the resource rents will be capitalised into prices that will be too tempting to ignore. Towards the end of the cycle, as asset prices roam beyond their true economic value, "hot" short-term loans will flood in to satisfy the speculative greed. There is nothing in the current thinking of organisations like the IMF and BIS to stop the calamity. In fact, the statements from people like the Chairman of the BIS board of directors, Alfons Verplaetse, are forlorn. He warns that monetary policy should closely monitor development of asset prices, which "can cause lasting damage to the banking system and to the broader economy".² But an improvement in the quality of data by itself will help no-one.

The European Union is agonising over the poor quality of statistics which are said to be insufficient to support the single European currency when it is launched next year. But Japan is the living evidence that data by itself counts for little. That country - unlike those in North America and Europe - has an exemplary statistical service. Its land market data is second to none. And yet, although governments could see the price bubble frothing away in the 1980s, the fiscal tools for defusing the imminent volcanic eruption did not exist. Nor do they exist today, because economists have still not focused on the distinctive characteristics of the land market. Until they do, the yen for transparency and more data serves as a smoke screen for the political inaction that will condemn many more people to poverty in the 21st century.

¹ *The OECD Observer* (212), June/July, 1998, p.4.

² *Financial Times* (London), June 9, 1998.