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TO THE CANADIAN CLUB AND THE EMPIRE CLUB

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Let me first say how honoured I am to be your guest today.

If I am to use this occasion to address some remarks to the subject of "the Interdependence of Nations and the Place of Canada", I should perhaps begin by briefly presenting the Organisation for Economic Co-operation and Development.

Almost exactly twelve years ago, on 30th September, 1961, this Organisation, the OECD, came into being as the direct successor of its parent body, which had a confusingly similar set of initials. This was the Organisation for European Economic Co-operation, OEEC, which the European countries had founded in 1948 to allocate Marshall Plan aid. They launched in this way, the process of a joint endeavour to restore their economies in the aftermath of the war. Canada and the United States were associate members of this European organisation. The generous and constructive Canadian contribution to the success of this venture will not be forgotten. Here, for the record, I would also like to pay tribute to the benefit which the Organisation derived from the quality and ability of the first Canadian Permanent Representatives, notably Ambassadors Sydney Pierce, Arnold Heeney and Jules Léger, and also of Mr. Peter Towe, whose return last year as Ambassador has been so widely welcomed. As further evidence of the positive interest of the

Canadian Government during the Fifties, mention should be made of the work of Ambassador Wilgress, whose Report on "Co-operation in Scientific and Technical Research" led the way to the systematic study of Science Policy in our Member countries and the first Ministerial Conference ever to be held on that subject in 1963.

In 1961, Canada and the United States became full members of the OECD. Japan joined in 1964, Finland in 1969, Australia in 1971 and New Zealand in the summer of this year.

What is it, we are often asked, that our 24 countries have in common? In the (not very elegant) parlance of the United Nations, the world is divided into three:

- countries with developed market economies,
- countries with centrally-planned economies, and
- the developing countries.

As a matter of convention, then, we - the OECD - are generally thought to be approximately the first group, the developed market economies..

But getting away from this static jargon, our Organisation's members have the following characteristics:

- they are certainly highly developed and industrialised, almost all of them;
- they are highly liberalised as regards trade and capital movements and integrated as regards their monetary systems, as compared to their relations with the developing or Sino-soviet countries;

and from this stems the basic ineluctable fact that they have to co-operate together on the whole range

of economic policy issues, and OECD is the main place they do it (i) on a day-to-day basis and (ii) in an integrated manner across the whole range of economic policy issues;

- some tend to say they are a "richman's club";

I would prefer to distinguish a group of countries which supply 90 per cent of the world's development assistance, and which have been prepared to work constructively together towards a coherent and sympathetic approach to the economic problems of the developing countries.

- they are "market" economies, so says the jargon.

This fact that we have market economies is perhaps the most important thing we have in common - but it is also the most easily misunderstood. We have market economies because we have learnt that, other things being equal, the price mechanism is the most flexible and democratic means for achieving an efficient allocation of resources to satisfy individual material needs. But we have also learnt that the market economy requires enlightened and sophisticated management, and that action by the public authorities is needed to regulate and complement market forces in order to ensure high levels of employment, an equitable distribution of income, the protection and conservation of the environment and, more generally,

a steady improvement in the quality of life.

Now we all know that to intervene in the market mechanism to further these wider objectives while reaping the maximum advantage from the efficiency of the price mechanism is far from easy. Public intervention needs to be carefully designed to achieve the desired objectives, and that vigilance is essential to ensure that action in favour of particular interests is not unduly detrimental to the general interest, either at the national or at the international level. Because this is a common problem for the "market economies" it lies at the very centre of the work of OECD. Indeed, I would say that 99 per cent of our work concerns the exchange of experience and the elaboration of lines of action on how best to reconcile the efficiency of the market mechanism with economic and social objectives. In many cases it is mainly a question of learning from each other about the best way of tackling domestic problems. But to an ever-increasing extent national policies in different countries interact with each other through trade, capital movements, migration and also "demonstration effects". This is, I believe, the basic reason why the 24 Member countries of OECD, including your own, have found the Organisation useful to them.

Against this background, the two general themes I would like to stress today concern:

First, the major changes that are at present under way in our economic systems, which, collectively, stand to be recognised as a turning - point in the economic history of the post-war period.

These changes are seen in:

- the international monetary reform under negotiation,
- the new round of trade liberalisation negotiations opened in Tokyo in September,
- the questioning of old concepts of growth and development, and the rise of the environmental factor,
- and the so-called energy crisis,
- the rise of Japan as a major economic power,
- the enlargement of the European Community,
- the major diplomatic initiatives opening up bilateral relations between our OECD countries, Russia and China,
- and the proposals for reassessment of relations between the United States, Europe and Japan.

During this period of transition, it is natural that the past traditional fabric of international economic co-operation is being questioned. There are some who are tempted to argue that our changing world implies that the very

concept of international co-operation is made obsolete. From our vantage point at the OECD, and this is my Second theme, we are particularly well placed to observe and assess the changing international economic order. We see the required response as anything but a return to unilateralism, or even bilateralism, and I will be developing some examples in a moment. More generally, the task is to recognise how the structural changes at present at work imply the need for:

- new solutions to old problems that now appear in a guise different from before, for example, international monetary and inflation problems;
- solutions to new problems, or at least problems that now pose themselves with increasing force, for example, in the areas of income distribution (between and within nations), energy and the environment, to take three of them.

In virtually all of these problems, we see clearly the links between today's immediate problems and longer-run goals, the inter-relations between the problem areas, and the need for internationally coherent solutions as opposed to a return to unilaterism, which would aggravate the collective problem.

May I now dwell in a little more depth on the two areas of immediate and urgent concern to all OECD Member countries, the reform of the international monetary system and the problem of inflation.

As the reform of the international monetary system is being laboriously - and, I am afraid, necessarily so - worked out, we are witnessing an experiment in the widespread floating of exchange rates. At an early stage in our present experience, there was much, almost euphoric, welcoming of the freedom of floating. Now, with the advantage of almost ^{two} ~~three~~ years' experience, some more balanced perspective is emerging. Certainly, we remain freed of the excessive rigidities of the Bretton Woods regime, which collapsed because the old adjustment process was inadequate, and because of failure to agree upon a new system. On the other hand, we have begun to perceive that the problems of generalised floating are much broader than those perhaps seen from earlier Canadian experiences of unilateral floating in a generally fixed exchange-rate system. Our "broader problem" must surely focus on doubts as to whether "the free market" may not, for example, exaggerate exchange-rate changes in some circumstances, or whether there is not a new and different set of inflationary dangers inherent in a floating system. (I will come back to this in the context of commodity prices in a while.)

The only conclusion, then, that I would like to draw today as regards the international monetary system, is that those who thought our new system should and could consist of a resort to free and unconstrained generalised floating - displacing the need for careful and continuous international co-operation - are being seen to be increasingly unrealistic. We, at the OECD, are intimately involved in the

monitoring of the existing de facto arrangements, and in assessment of the implications for the reformed system under negotiation.

To say some words now on the problem of inflation, you may be thinking that I will wish to stress the links between the international monetary disorders and the obduracy - even aggravation - of the problem. Links there are, but

these must be kept in perspective. In many European countries the opinion is frequently held that imported inflation is the principal and irresistible cause of domestic inflation. Over the last twelve months one has also increasingly heard the argument - particularly in Europe and Japan - that accelerated inflation is mainly due to the commodity price boom, that is to "world forces beyond our control". But this tends to overlook the fact that, netting out imports and exports the OECD area is about 80 per cent self sufficient for its consumption of crude primary materials taken together, in other words that 80 per cent of the rise in incomes resulting from higher commodity prices is to be found somewhere else in the country concerned or in another OECD country. Of course the commodity price boom is important, and I will return to this later. But let us not all delude ourselves, each sitting at home in our respective countries, that "someone else" has caused the inflation problem. One advantage of the kind of international economic analysis that is done at the OECD is that, when adding the OECD area all up together, it becomes clear that the "imported inflation" game has to stop somewhere.

Most OECD inflation is, in fact made-at-home in the OECD taken as a whole. To give one example, we estimate that at the present time - with consumer prices rising at close to 10 per cent in the OECD area as a whole - only about one-half of 1 per cent can be attributed to the improvement of the developing countries'

terms of trade that has come with the commodity price boom.

More basically, inflation has become deeply built into all our OECD economies. This much is evident from the extremely short and limited progress that was made in reducing the rate of price increase during the business slow-downs or recessions of the early 'seventies. The present business upswing may have made the rate of inflation worse again - in part through the commodity price boom. However, the signs are becoming increasingly clear that we have moved into a world in which the inflation cycle consists no longer of symmetrical ups and downs, but more of an upward ratchet mechanism, with the rate of inflation moving from peak to plateau to new peaks.

And the "world" here is in fact more the "OECD world".

The days are passed when developed countries could provide object-lessons in stability to the developing countries. The average rates of price increase in Africa, Asia and even in many individual Latin American countries in 1972 were below the rates now being experienced in the OECD area.

There are at least two reasons for regarding recent rates of inflation with alarm. First, when the annual rate of inflation approaches 10 per cent, the real losses of those least able to protect their incomes risk becoming sufficiently substantial to give rise to major social strains. Moreover, the higher rate of inflation, the greater the risk that it will lead to undesirable distortions of economic decisions and the allocation of resources. The second, and perhaps

the more disturbing cause for alarm, is that the higher the rate of inflation, the less certainty there is that a steady - or not so steady - acceleration of the price rise can be prevented. When prices rise at their current speed, the strategies of business and labour in the formation of prices and money-wages anticipate with resolution the price rises of the future. Nobody is prepared to be left out of the attempt to ensure their incomes against the price rise assumed for next year. Regrettably, there is sufficient precedent to legitimise this assumption.

It is illusory to imagine that everyone's income can be indefinitely assured by indexation arrangements against a 10 per cent or 15 per cent inflation rate, and with no tendency by particular interests to try to jump the queue. This would require throughout the economy of our Member countries - and virtually throughout the world - an indexation of wages, price, profits, professional fees, investment income, pensions and allowances which no government, in or outside the OECD area, is equipped to manage. This is why I say that recent inflation rates, if contained for long, could bring us to the point of no return - to the point at which the only likely change in the rate of inflation would be upwards.

Let me say, I am afraid, that we claim to have discovered no simple panacea to the problem of inflation; I do believe, on the other hand, that there is now increasingly widespread recognition of the need for the kind of "multi-

policy" attack on inflation that we advocated in one of our principal publications on the subject about three years ago in 1970. By "multi-policy approach" we meant that the problem of inflation was too intractable to be capable of solution by demand management policies alone - and indeed by price and wage controls alone. Some of the extra policy instruments that may usefully be brought into the stabilisation package have in fact been well illustrated by Canada, for example through your large-scale manpower policies to try and reduce regional disparities in labour market pressures, and the trade liberalisation measures introduced in your last Budget. One further new dimension that has been coming to the fore has been the inter-relationship between rising tax burdens and inflation - over and beyond the traditional tenets of fiscal policy.

But the major new feature of today's inflation is undoubtedly the contribution of the commodity price boom. Government representatives are, in fact, meeting at the OECD in Paris this week, to make an up-to-the-minute assessment of the problem, and to prepare recommendations for an important meeting of our Economic Policy Committee in two weeks' time. Canada, as a major producer of primary materials, is experiencing its fair share of the problem, to say the least. It is my conviction that we need to reflect very seriously upon the underlying causes of this commodity price boom: to us at the OECD, it does not appear to be a simple, isolated accident of the business cycle. Many commentators have pointed to the unreformed international monetary system as a factor aggravating speculative demand. There is probably something in this. What has struck us also, however, has been some unexpected inter-actions of recent exchange-rate changes, the commodity price boom and the general course of inflation. Normally, one would have expected

the revaluing countries to have absorbed a large part of the recent commodity price rises with their revaluations, while the price-rising stimulus would have been very much greater for devaluing, importing countries. In fact, we find that something of the reverse is happening with the revaluing countries losing much of the stabilisation benefits that might have been expected with their domestic inflation continuing at a fast or even accelerating pace; while in the devaluing countries, perhaps mainly because they have resorted to price and wage controls, there has been some success in absorbing, or at least holding back, part of the commodity price boom, or its effects on the wage-price spiral.

Time does not permit me to go into these complex inter-relations. The point I would like to bring out, however, is that in our present world of:

- (i) universal inflation,
 - (ii) a changing international monetary system,
 - (iii) a changing set of relations between primary producers and consumers, and
 - (iv) an increasingly synchronised world business cycle, itself showing a worrying tendency towards excessively severe peaks and troughs;
- these various factors are:
- (i) deeply inter-related, such that
 - (ii) any country individually is, on its own, powerless in the face of a seemingly disordered international system, and

- (iii) efficient international co-operation in economic affairs remains indispensable to help assure concerted and mutually reinforcing national policies.

The links between these priority problems of the moment and several so-called long-term problems are impressive. Take the growth debate, for example. How, we may ask, would a severely reduced growth rate fit with the need to:

- make available the financial resources to transfer to developing countries,
- make available the resources required to clean up the environment,

- make available the resources to reduce income inequalities without reducing real living standards for many.

From the OECD vantage point, the question whether we should drastically reduce the rate of economic growth really seems to be missing the point. What we must do is to make imaginative use of public policy so as to ensure that in the growth process increasing weight is given to emerging demands for quality rather than quantity and to the constraints arising from the finite supply of non-renewable natural resources and the increasing density of population. If we do this it is possible - perhaps probable - that the growth rate of GNP as conventionally measured will slow down. But while statisticians may worry about this, world-welfare in the wider sense will still be growing, and I doubt whether the ordinary citizen will worry very much what the figures show.

Questions of long-run physical resource supplies and within this the energy problem, are further examples of topical issues which link together the internationally shared problems of long term growth strategy and a number of other important issues of national and international concern. The OECD's study of the long term energy problem is indeed dealing with the inter-relationships of the future development of demand and supply with inter alia the environment policies, the policies of development co-operation, international monetary relations and policies in the field of science and technology. The OECD is active in all these areas and the place of Canada is clearly of major

international importance in a number of them. The objective of our long-term energy assessment is to bring together and to synthesise all these relevant aspects of energy policy and, through this process, to define the long-term policy options for our Member countries.

Another of our activities of particular interest to Canada is our work on international investment and multinational companies. These issues are related to the balance of payments, inflation, employment, trade, taxation, national development policies and, of course, the relations with developing countries. And, indeed, OECD's work on development co-operation increasingly reflects the need to integrate into these policies not only our financial and technical assistance but also our trade, investment, agricultural, industrial policies and, even, our policies for science and technology - the success of the development policies of the poorer countries is to a large extent dependent on the economic policies of the developed countries } I may in this connection, come back for a moment, to the long-term energy problem.

It is clear that substantial increases in the price of oil will aggravate the inflationary situation in the OECD area; they will also imply a deterioration of the terms of trade with the oil producing countries with corresponding consequences for the balance of payments. For the OECD countries this poses in varying degrees difficult, but not unmanageable problems. For the developing countries, however, the situation is entirely different; they, simply, cannot afford to spend so much more for import of oil without seriously jeopardizing their development process. Clearly there is a need for an international approach to this problem in the common interest of the developing, the developed and the oil producing countries.

The particular vocation of OECD among the several international economic organizations is to help keep the various pieces of the jig-saw puzzle of international economic affairs together. As I have just hinted, this is a constantly changing jig-saw puzzle producing continuing surprises. It is our challenge at the OECD to help the international community keep day-to-day control of its complex economic system. It is also our task to help our Member Governments maintain a constantly updated and coherent link between the reality of today's priority problems and the long-term structural developments that are being negotiated or evolved at the same time.

It is, however, equally important to be vigilant to preserve what has been achieved. One of the most significant factors in the history of post-war economic development has been the role of multilateral co-operation. There can be no doubt that the constant efforts and progress towards the opening of our economic frontiers, the removal of the obstacles to international economic co-operation, has been one of the most important driving forces to achieve the unparalleled prosperity that we have enjoyed during this period. While this is generally recognised, it is still no guarantee that when countries are faced with economic difficulties, they may not tend to see their problem in isolation and to seek national solutions to problems which are fundamentally international, or to seek bilateral solutions to problems which are of a wider international concern. Here the OECD has an important role to fulfil. By placing the issues in their true international context and perspective, it can act as the "economic conscience" of its Member countries. Among our Western countries we have been successful in creating and maintaining a "One World" economic concept. This "One World Concept", this concept of multilateral

co-operation between all countries, large and small, can be strengthened but not replaced by a network of bilateral relations. The historic achievement of the OEEC - our predecessor organisation - has been to transform European bilateralism into multilateralism. Equally, the OECD of today has the vocation to strengthen the multilateral co-operation between all Member countries and to resist any retrograde tendency towards new "macro-bilateralism" between its major economic units which seems to be advocated from time to time.

We are living through a period when the ground rules governing so many of the important sectors in international economic and social relations are rightly being revised but, in this process, we should keep constantly in mind the objective of strengthening, not weakening, the "One World" concept. The place of Canada will, I am sure, continue to be in the forefront of the discussions within the OECD and in the other international organisations where an improved economic future, based on the interdependence of nations - and the interdependence of the developed and developing world - is being forged.