dependence on the U.S.S.R. In order to fragment its political/military
empire. This simplistic nostrum ignores the government dependencies
created within certain sectors of the U.S. economy—in this case, banks,
farmers, and agricultural traders.

If business-government relations are to be improved by a return to
laissez-faire, neutrality toward all businesses and industries rather
than selective support of some must become a criterion of policy deci-
sions. The market must be allowed to perform its functions, even though
some effects may be painful. By guarding banks against risk, government
erodes a crucial role of banks—that of economic "barometer". Moreover,
the separate identity of banks and the government becomes clouded, and
government becomes implicated in any mistakes the banks might make. In
addition, if government is to keep its "hands off" the economy, this
policy must apply internationally as well. The government cannot mix
economic aims and political ends without compromising its domestic
credibility and perhaps without opening itself to unexpected foreign
policy results.

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The Political Crisis of the Enterprise System. R. Ellis. New York:
Business and Public Policy. J. T. Dunlop, Editor. Cambridge, Mass:

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Briefings

Volume II, No. 7
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The Dean Rusk Center was established in 1977 to foster interdisciplinary research, service and education concerning institutions and processes basic to efficient intercourse among nations. U.S. fiscal and monetary policy has separate emphasis, due to its increasing impact upon international commerce. U.S. trade and investment in a world environment remains the primary focus of its study and policy recommendations sponsored by state and federal entities. The Center also recognizes that internal dynamics of nations remain the major determinant of international relations and that domestic concerns about the quality of life, stability and efficiency will continue to vie for dominance in determining a nation's posture in world affairs. Thus, much of the Center's data collection and analysis dwells on domestic events of nations and diverse disciplinary explanations of their presence and evolution.

Admittedly, the interactions of fiscal and monetary policy, international arrangements and domestic events cannot fully be analyzed in a specific geographic or subject context. Nevertheless, many of the Center's policy development activities concentrate on the North American region and related subjects of agriculture, national development, business-government relations and public governance. These bi-weekly briefings reflect the convergence of the Center's diverse activities and interests.

Facts and details of events addressed in Briefings are gathered through a scanning of major daily newspapers and weekly periodicals, which are cited throughout each article. Sources of related policy and disciplinary material appear in a listing following each article. The purpose is to link facts with policy implications and academic points of view in order to present an integrated and in-depth approach to current issues. Views expressed are not necessarily those of the Rusk Center.

I. FISCAL AND MONETARY POLICY

ENVIRONMENTAL ISSUES AND THE BUDGET - While the rapid decline in oil prices is welcome news to industry, its effect on the federal budget is cause for more sanguine feelings among Reagan administration officials. There is widespread concern that lower oil prices will reduce revenues from the windfall profits tax and other oil industry taxes, offsetting revenue gains from an economic recovery. Because tax cuts and generous investment allowances have, as yet, not caused a boom in savings and investment, the administration is engaged in a search for new revenues as well as further means to cut the budget. The president's economic policy advisory board, at its quarterly meeting on March 24, favored an increase in excise taxes on alcohol and tobacco and energy levies on natural gas and possibly on gasoline or imported crude oil. Transportation Secretary Drew Lewis has been lobbying hard for a five-cent increase in the federal gas tax. The existing tax has not been raised since 1959, and conservation measures and rising construction costs have placed the highway trust fund in jeopardy (Bus. Wk., 4-22-82, p. 29 & pp. 88f; Economist, 4-13-82, p. 20).

The recession, with its attendant erosion of the tax base, has given the Reagan administration less room to maneuver, straining the legislative coalition and making the president's task much more difficult politically. Environmental groups are particularly concerned. In his proposed fiscal 1983 budget, President Reagan has eliminated almost all the traces of his predecessor's preference for coal, conservation, and solar energy. New emphasis is being placed on nuclear energy, which would be the principal focus of a new agency, the Energy Research and Development Administration (ERDA), to be placed in the Commerce Department. Funding has been cut to the Synfuels Finance Corporation, and administration of the Strategic Petroleum Reserve is to be moved to the Interior Department (Economist, 2-19-82, pp. 14f; 4-13-82, p. 63; Congressional Quarterly, 2-13-81, p. 261).

President Reagan's 1983 environmental budget is down 16% from 1982, with Environmental Protection Agency (EPA) operating funds down 29% from
fiscal 1981 spending levels. Environmentalists argue this will cut EPA spending power by almost 40% from pre-Reagan days, after adjustment for inflation. The president wants to raise more than $8 billion in new receipts in fiscal 1983 from an accelerated offshore oil and gas leasing program and $17 billion over the period 1983 to 1987 by selling off "unnecessary" federal land at market prices. A five-year plan for increasing this leasing is soon to be announced by the Interior Department. In 1981 the Department offered 7.5 million acres for offshore leasing, the most made available in the 22-year history of the program (Bus. Wk., 3-22-82, p. 26; Congressional Qtrly. Wkly. Report, 2-15-82, p. 267).}

The new environmental budget proposes the elimination of federal grants to states for planning coastal development and for mitigating the impact of offshore energy development. It further aims to increase user charges at national parks. The administration also plans to propose legislation expanding the number of services for which user fees are charged. This will affect the administration's water development and irrigation programs. An estimated 15 federal dams, predominantly in the West, need structural improvements to make them safe. Estimated costs of repairs are six times the amount already authorized for this purpose, and the administration wants western farmers who benefit from the irrigation schemes to pay for a portion of the repairs (Congressional Qtrly. Wkly. Report, 2-6-82, p. 205; 2-15-82, p. 268).

Much of the present administration's efforts to reduce the size of the budget deficit are in keeping with its philosophical desire to tighten the burden of regulation on business and shift control of environmental matters to the states. What concerns environmentalists and others is the preoccupation with short-run panaceas and the lack of foresight with respect to their longer-run implications. For example, while the new clean air bill (HR2552) under discussion has basic administration and industry support, a strong body of legislators believe its passage could mean that much of the environmental achievements made in the past decade would be lost. They especially find unacceptable the provision that would delay from 1982 to 1993 the deadline for various clean air standards. While environmental groups recognize the need to reduce the budget deficit, they object to the administration's concentration upon "soft" budget items whose benefits accrue over longer periods and are less amenable to economic quantification. Their ability to mobilize public support for these issues is dependent upon the length and severity of the current recession. If unemployment remains high, organized labor will likely swing toward supporting further reductions in environmental regulatory restrictions for the sake of job creation.


II. INTERNATIONAL ARRANGEMENTS

A. POLITICAL/MILITARY - MEXICO'S CENTRAL AMERICAN PEACE INITIATIVE

On February 21, 1982, Mexican President Lopez Portillo unveiled a three-part plan to bring peace to Central America. The plan called for an end to the fighting in El Salvador and inclusion of the leftist opposition in the March 28 elections, a non-aggression pact between Nicaragua and its Central American neighbors as well as the United States, and a resumption of talks between Cuban and American officials. Mexico is to act as mediator, with both President Portillo and Foreign Minister Casanovas conducting "shuttle" diplomacy among the powers involved. Although at first the official U.S. reaction appeared cool, by mid-March Secretary of State Haig's two meetings with the Mexican Foreign Minister indicated a heightened interest in Mexico's proposals. Nicaragua, too, seemed receptive to the plan despite its allegation that the U.S. was responsible for the bombing of several bridges near the Honduran border (N.Y. Times, 3-12-82, p. A14; Wall St. J., 3-12-82, p. 25).
There is debate regarding the reasons for recent interest in the peace proposals, most of which have been presented previously. Some observers speculate that the Reagan administration may feel pressured to seek a diplomatic solution because of increased congressional opposition to U.S. military involvement in El Salvador and damaged White House credibility concerning its allegations of Soviet military influence (Wall St. J., 3-12-82, p. 26).

Nicaragua's interest in the peace initiative may be rooted in the socio-economic costs of its military build-up. Like many Central American countries, its economy is suffering deteriorating terms of trade as a result of rising oil prices and a weak market for commodity exports. This problem is exacerbated by its political and military instability, which has deprived it of much foreign credit. In addition, it is short of technical and professional workers: militarization siphons off scarce human resources needed for development. Mexico's peace plan includes provisions for U.S. economic assistance in exchange for a Nicaraguan agreement to scale down its military (Latin America Regional Reports: Mexico and Central America, 3-19-82, p. 74).

Mexico's role in the peace initiative represents the most fundamental change. The peace proposal is the most recent expression of a policy of regional leadership that began at least 10 months ago. During that period Mexico and Venezuela agreed to sell oil cheaply to seven Caribbean nations. In addition, Mexico has given various forms of economic assistance to Nicaragua, and it has established a trade preference system allowing many Central American products to be brought into Mexico for only 25% of normal import duties (N.Y. Times, 3-21-82, p. E3). Even the present peace initiative is only the latest in a series of diplomatic moves by Mexico to bring political stability to Central America. Last November, for example, Mexico arranged for talks between Hugi and Cuban Vice-President Rodriguez.

Some analysts suggest that domestic political concerns underlie Mexico's assumption to regional leadership. Revolutionary movements in this region may spill over into Mexico, especially given its current economic problems, such as underemployment and inflation. Last year it deported 3,000 Guatemalan refugees, not only because the southern region to which they fled already had serious unemployment and other economic problems, but also because the government feared that these refugee camps might become breeding grounds for guerrilla opposition movements within Mexico. Mexico has never given Guatemalan leftists the kind of public support it has expressed for the Sandinistas in Nicaragua and the guerrilla left in El Salvador. Recently it has reduced its support for these (Chn. Sci. Mon., 2-5-82, p. 7; N.Y. Times, 3-21-82, p. E3).

Other analysts place more emphasis on U.S.-Mexican relations in explaining Mexico's new role. Further deterioration of the area's stability could precipitate U.S. military intervention, which would not further Mexico's objective of attaining greater independence from its northern neighbor (Chn. Sci. Mon., 3-9-82, p. 3). Conversely, it may be precisely because Mexico has achieved considerable self-confidence as a result of its oil wealth and rapid economic growth that it no longer needs to use foreign policy as a symbolic expression of its putative independence from the U.S. (N.Y. Times, 3-21-82, p. E3).

Whatever the motivations underlying the coincidence of interest in a negotiated resolution of Central American instability, the implications for policymakers are clear. The regional approach Mexico has chosen complements recent American foreign policy measures, such as President Reagan's Caribbean aid plan, in which Venezuela, Colombia, Mexico, and Canada have joined as co-leaders (N.Y. Times, 3-15-82, p. A14). Because of its long and close ties with leftist regimes and opposition movements, as well as with the United States, Mexico is in a good position to mediate within such a regional context.

However, significant differences remain between Mexican and American understandings of Central American problems and solutions. For example, the United States has been encouraging El Salvador's military junta to carry out land reforms, whereas Mexico has ceased land redistribution despite its symbolic value in maintaining control of its own
left. Land reforms in El Salvador have been sharply criticized not only for the hasty manner in which they were carried out, but also for their macro-economic inefficiencies and resultant general impoverization. Mexico stresses Nicaragua's sense of isolation and insecurity. Surrounding countries harbor Somaya exiles, whom Nicaragua believes the U.S. is secretly funding. Nicaragua claims some coastal territory held by Colombia. The U.S. has tended to regard expressions of such concerns as rhetorical (Chr. Sci. Mon., 3-16-82, p. 1+; N.Y. Times, 3-12-82, p. A11; Latin America Regional Reports: Mexico and Central America, 3-19-82, p. 7+).

The most fundamental differences pertain to the cause of Central American instability. Mexico blames internal problems, such as poverty and authoritarian rule. The United States regards Soviet arms supplies as the critical factor and considers Central American problems as virtual pawns in the East-West conflict (Chr. Sci. Mon., 3-9-82, p. 3; 3-16-82, p. 1+; Wall St. J., 3-15-82, p. 2). If the United States pursues a global solution, it may give the Soviet Union a more direct voice in regional discussions than it would have under Mexico's plan. Furthermore, such action would undermine Mexico's efforts to create a middle course between the United States and communism in Central America and the Caribbean and thereby to wean Cuba away from Soviet dependence (Chr. Sci. Mon., 3-16-82, p. 28; Wall St. J., 3-16-82, p. 2).


B. SOCIAL/CULTURAL - ISLAMIC BANKING

Though many believe that the principles of Islamic religion are inherently incompatible with economic development and adaptation to the demands of the modern world, Muslim governments are busy modeling development plans in accord with traditional Islamic constraints on economic activity. State-owned banks and "hawala" (Islamic banks) have been instituted, with ambitious goals both for their depositors and clients and for the Islamic community as a whole. One such bank is the House of Islamic Funds, whose shareholders include Bahrain, Egypt, Guinea, Kuwait, Malaysia, Pakistan, Qatar, Sudan, and the United Arab Emirates. Its goal is to work with $1 billion dollars in capital and to compete successfully with established Western banks. Other Islamic banks are located in Kuwait, Sudan, and Egypt. The largest concern, however, is the Islamic Development Bank (IDB), founded in 1923, whose assets were worth $1,480 billion in FY 1981 (Currency, 11-81, p. 59; FMEQ Special Report, 11-81, pp. 20+; Far Eastern Economic Review, 11-81, pp. 86+; Wall St. Journal, 11-81, p. 31). The Islamic world is characterized by ideological tensions between developed and developing countries and within the Islamic community itself. Rivalry with large Islamic populations is interested in using Islamic banking methods to develop financial system. The other hand, such financial ties may also serve the larger goal of forming a vital cross-national Islamic identity with worldwide inter-cultural consequences.

Islamic banking methods provide an immediate point of contrast between the West and the Islamic world. Whereas Western banks obtain an investment return on loans by charging interest on the principal, Islamic banks must forego this method because religious law forbids the charging of interest, or usury on loans; interest is thought to be instrumental in what Muslims consider immoral disparities in wealth distribution in many societies. Instead, Islamic banks receive a return on their investment by sharing in the equity of the investing firm. This system of joint ventures provides the basis for financing
Industrial and agricultural projects, commodity trading, trading companies, and small businesses.

The chief political rationale for the proliferation of Islamic banks seems to be rooted in the struggle within the Islamic community over what form pan-Islam should take. Politically conservative and moderate regimes with dominant or exclusively Muslim populations seek to legitimize their rule by identifying themselves with established religious hierarchies; such is the case with Saudi Arabia, Egypt, Pakistan, South Yemen, and the United Arab Emirates. They are faced with a revival of traditional, populist Islamic sentiment that constitutes a revolutionary challenge to the conservative status quo. Prominent instances of revolutionary sentiment are the Ayatollah Khomeini regime in Iran; the occupation of the Grand Mosque in Mecca in November-December 1979 by Shi'ite revolutionaries; and the assassination of Anwar al-Sadat in October 1981, for which the Muslim Brotherhood holds itself responsible. Affected regimes are responding by employing their massive oil-derived revenues in the interests of political stability not only within their borders but in the Muslim world in general. For example, Saudi Arabia has subsidized the oil-import-caused deficit that Pakistan is experiencing; and the IOB has been financing Pakistani trading projects, thus doing what it can to support the Zia-ul-Haq regime, which professes to rule on Islamic principles but which has been accused of exploiting Islam for political purposes (World Development 8/7(81):568-75, July/Aug. 1983). The alternative to his rule is a fundamentalist regime in which Saudi Arabia thinks will be susceptible to Soviet revolutionary appeals and will gravitate towards the Khomeini regime. The IOB also disburses funds to another strategically significant country, Turkey, even though it is a secular state. Another notable financial policy of Islamic banks is to provide non-competitive loans to small entrepreneurs, perhaps in hopes of creating a small business class that would have reason to prefer the status quo rather than a revolutionary environment (Economist, 11-91, p. 28).

What binds all Muslims together, however, is a common commitment to worship in an egalitarian religion. Whereas western societies are characterized by a clear separation of church and state and often treat religion as an individual and private matter, Islam conceives of religious belief, ethics, and politics as an organic whole guided by a strong but benevolent God. The shari'a, or body of law and tradition, regulates the economy to prevent the emergence of cutthroat competition and exploitation of the disadvantaged. Nevertheless, as Islamic ethics are fundamentally moderate, significant latitude exists for entrepreneurship to flourish, expressly for the ultimate good of the community. The ban on interest, the obligation to pay a religious tax (zaka'i), and the duty to offer charity to deprived relatives and indigents has not reduced business incentives, though they have perpetuated the Islamic tradition. Aside from pragmatic motivations, Islamic oil-producing states are using their enormous revenues to reinforce Islamic values among Muslims by creating a sense of identity based on Islam's ability to foster economic development and bring the benefits of affluence to Muslims without the "disadvantages" that have stricken the West—materialism, secularism, and, above all, a colonial mentality.

Though the emergence of a pan-Islamic consciousness would be a significant development, its implications for the future international environment cannot be assessed. Its cross-national scope could be an achievement in itself, or it might pose difficulties insofar as some of the states it would encompass have populations that are not all Muslim, such as Malaysia, Nigeria, and the Soviet Union. A larger conflict, of course, is over what form Islam should take. Revolutionary, fundamentalist Islam possesses potential and actual mass appeal in all states with large Muslim populations and hence could have a destabilizing effect that conservative regimes strive to undermine in the long term by developing a middle class. The Khomeini regime probably cannot be reproduced in other countries because the mujahid classes are not large enough to govern without participating in coalitions; but conservative regimes, deeply concerned for their survival, are using their oil-derived revenues to promote domestic stability. Whatever the outcome of this intra-religious conflict, a common effort on the part of both sides is to avoid the worst effects of the onslaught of modernization by
employing religious principles that are nearly 1,300 years old to ameliorate the conditions of nearly a billion people.


III. DOMESTIC ISSUES

A. HUMAN DYNAMICS - CHINA'S BUREAUCRATIC STREAMLINING

Since the death of Mao Zedong in 1976, China has undertaken a path toward modernization and economic development that has already begun to have profound effects on the political ideology unifying the party leadership and on the society as a whole. Now a bureaucratic reorganization, long anticipated, has been set in motion by Deputy Prime Minister Deng Xiaoping. The goal of this restructuring is to reduce the size of the central government by a third and its number of departments by half; to lower the very high average age of bureaucrats; to raise the proportion of college-educated officials holding responsible positions; and to increase the number of women in the system. Eventually, this process is to be repeated at other governmental levels and within the communist party itself (Economist, 3-13-82, p. 50; 2-20-82, p. 57). In announcing the government's intent in December before the National People's Congress, Prime Minister Zhao Ziyang asserted the need to "insure effective leadership" by altering "such intolerable phenomena as ... multi-echelon departments ... crammed with superfluous staffs, numerous deputies and nominal chiefs and bogged down in endless debates and shifts of responsibility, causing very low work efficiency" (N.Y. Times, 12-2-81, p. A7). Also stressed was the intent to seek out and remove corrupt officials. Not emphasized but certain to occur is an attempt to eliminate bureaucrats who obtained their positions during the Cultural Revolution of 1966-69, remain committed to its precepts, and now present serious obstacles to the introduction of changes deemed vital to modernization (N.Y. Times, 1-20-82, p. A11; 12-2-81, p. A7).

In contrast to past major reorganizations, this one tries to deal positively with those removed from their jobs. Official publications have labeled the decision to retire as honorable, even patriotic; and in some cases, the government is permitting those stepping down to retain the income and perks, such as housing and cars, attached to their sinecures. Bureaucrats have often been encouraged by their families to retain posts until an advanced age because retirement would mean the loss for the entire group of the status symbols of a nominally classless society (N.Y. Times, 1-20-82, p. A11; 11-29-81, p. E3). For able adults forced out of jobs, the reorganization plan calls for retraining. While the necessary structures are not in place to provide education and training on a massive scale to inculcate such skills as modern management techniques, the Chinese have begun to seek aid in establishing programs of this type (N.Y. Times, 12-2-81, p. A7; J. Commerce, 2-3-82, p. 1A). The attack on the problems of the bureaucracy is not occurring in isolation. The basic decisions to modernize and to improve the living standards of the Chinese have led Deng and his associates to look critically at the obstacles impeding development of the economy. Among the glaring deficiencies are sectoral imbalances and low productivity, the latter caused in part by the former. Great inefficiencies have also been introduced into the system as a result of central planning, because upper echelon decisions become ossified as they move through the bureaucratic structure and cannot be adjusted at the implementation stage even when they are patently inappropriate. Moreover, individual managers have little motivation to do so (World Today 36(11):445-51, Nov. 1980; Interconomics 15(4):181-85, July/Aug. 1980; 16(1):43-47, Jan./Feb. 1981).
The question of motivation is not a new one. Under Mao certain members of the party leadership, chief among them Liu Shaoqi, advocated the use of material incentives to stimulate industry and agriculture. But the approach was anathema to Mao; and Liu, for a time considered the heir apparent, was disgraced and imprisoned and his family brutalized for his ideological deviations. Now through Deng's leadership, Liu's concepts are gradually being reintroduced into party ideology, while the formerly unassailable thoughts of Chairman Mao are thrown into question (N.Y. Times, 1-11-82, p. A7).

To combat the dual inefficiencies introduced by central planning and by the lack of sufficient incentives to encourage rational decision-making at the enterprise level, a number of reforms have been instituted on a limited basis. In industry, selected firms are being permitted to retain profits on production over quota. Part of the profits are paid out as bonuses to workers and management; the remainder can be reinvested to enhance the productive capability of the firm. These enterprises are for the first time being given the authority to obtain their own supplies and to handle such marketing functions as price setting for above-quota production. In agriculture, similar capitalist intrusions are being permitted to individual farmers and cooperatives (Current History 79(458):24-28; Intereconomics 16(1):43-47; Fortune, 12-28-81, pp. 90-99).

Interestingly, the changes occurring now, so antithetical to policies and programs of Mao, nevertheless emanate from a fundamental belief which he laid down regarding China's position on the world scene—that the Soviet Union, expansionist by nature, was the power most threatening to China and that China must therefore look to the West (to Japan and the U.S.) for its security (World Today 36(11):445-51, Nov. 1980). In the intervening years, China has grappled with the reality that the safety of the nation could not be guaranteed alone either by alliances or the sheer numbers of its masses, but must be supported by economic and technological development that would bring China abreast of the world's major industrialized nations. With the Soviet Union identified as the ultimate enemy, China was perhaps more susceptible to the economic models and practices of the West when it opened its doors to the world. Moreover, as China moved away from the doctrine of self-reliance, realizing that modernization can progress far more quickly with an infusion of foreign technology and investment, it sought those inputs from the West. China's need to obtain hard currency to pay for industrial capital goods and its attempts to do business with the West have provided a strong rationale for making attractive economic overtures to Western firms; the special economic zones now being promoted are one example. Developing relationships have also highlighted obstacles to foreign investment and cooperative ventures—e.g., a stiffening inefficient bureaucracy that cannot expedite needed permits or coordinate the provision of adequate transportation so that special economic zones can be used (Economist, 1-9-82, pp. 45-6).

At present, no one can predict how far Deng will be able to carry through on his bureaucratic organization, nor can one guess to what extent these market concepts will be allowed to intrude into a planned economy. The introduction of change in both these areas is rife with difficulties. Deng has apparently had to halt modernization plans more than once in order to consolidate his own power and gain the necessary political consensus to move forward (Problems of Communism 30(5):62-65, Sept.-Oct. 1981). Whether he can win popular commitment to his program may also prove problematic, while the liberalization of the system to permit petty-capitalist activities is proving popular among participating individuals, many Chinese, especially the young, have become cynical about the ideological gymnastics that have occurred over the past 30 years (N.Y. Times, 1-11-82, p. A7; Problems of Communism 30(6):65-68, Nov.-Dec. 1981). Moves toward free enterprise activities in manufacturing and industry will also be hampered because of a lack of managerial experience in key business functions and because of distortions introduced by a still rigid economic system.

Despite these difficulties, however, the climate for further change along present lines seems auspicious. An important consensus seems to have emerged in the Chinese leadership about the value of stability to economic development. Such sudden and traumatic upheavals of the Great
Leap Forward of 1956-57 are to be avoided, as are harsh reprisals against people out of political favor (Problems of Communism 30(5):62-65, Sept./Oct. 1981). Equally important, the process by which development is to occur is being rationalized very much along western lines. For example, prices at which above-quota goods are sold are to form the basis for an adjustment of the Chinese pricing structure; and in general, the results of this limited experiment with free market mechanisms are being carefully watched and analyzed as a means to improve future economic decisions. Emphasis on the importance of decentralized planning, managerial skills, and bureaucratic efficiency is also illustrative (Interconometrics 16(1):43-47, Jan./Feb. 1981). This process will likely accelerate as Chinese trained in the U.S. or in U.S.-designed programs gain positions of responsibility in China (Briefings 1-29-82, pp. 13). The U.S. government can best enhance the process now underway by maintaining steady, friendly relations with China and ensuring that channels of exchange-economic, educational, and cultural—remain open.


B. RESOURCES - ELECTRONIC MAIL

On January 4, 1982, the U.S. Postal Service introduced its electronic computer-originated mail service, E-COM. The system, which had been in planning and development stages since 1978, consists of 25 post offices throughout the country equipped to receive electronically transmitted messages. These messages are then printed, put in envelopes, and delivered through normal mail channels within two days of origination at a cost of $0.26 for a two-page document. This application of communications technology was designed to be most efficient for firms sending mass mailings; and by December 1981, 80 organizations, including such diverse examples as Eastern Airlines, the NFL, Union Oil, and Temple University, had signed up to participate in E-COM (Wall St. J., 1-4-82, p. 24; N.Y. Times, 1-10-82, p. F2; 12-29-81, p. D1).

E-COM debuted amid a flurry of legal and regulatory controversy. A Washington, D.C., appeals court denied a Justice Department request for a restraining order to block final implementation. Though this effort was based on the procedural failure of the Postal Service to obtain Postal Rate Commission approval for a permanent system, the underlying issue was concern that the publicly supported Postal Service would compete unfairly with common carriers such as the Bell System and GTE's TELENET or with service providers such as Exxon and IBM. The relatively low price of $0.26 per two-page document has fueled fears that the Postal Service would subsidize the new electronic mail operations with federal money or revenues from other services. This has become a sensitive point as a result of the recent settlement of anti-trust actions against AT&T, which provided the phone company with the opportunity to offer computer communications capabilities directly to the desks of executives via already in-place telephone lines (N.Y. Times, 1-10-82, p. F2; 1-2-82, p. 27; Economist, 1-16-82, pp. 134).

For its part, the Postal Service views E-COM as a requisite for survival. According to the National Research Council, 80% of first-class mail is generated by business or government, 30% of which can be adapted to the electronic medium. Accordingly, nearly one-fourth of first-class mail, the Postal Service's prime money maker, could be diverted to private, electronic couriers. Estimates project that over 11 billion messages will be sent via electronic mail in 1995 as compared to 930 million in 1980; this growth will concentrate in intra-company communications (N.Y. Times, 1-10-82, p. F2; 1-5-82, p. D5; Chris. Sci-Mon., 1-19-82, p. 11).
The real regulatory and efficiency questions, however, relate to the future, and not to the present, E-COM system. As described above, E-COM is a second-generation electronic delivery system in that information transmitted is printed before delivery to the addressee. In third-generation systems messages are generated, transmitted, and delivered all in electronic form, thus increasing the speed of communication, enhancing the utility of the information for the end user, and reducing the cost. Most of these systems utilize large mainframe computers and communications networks, but many companies have turned to using small, relatively inexpensive personal computers which can communicate with each other as well as with larger computers via ordinary telephone lines at a much lower cost than that of the major providers. For example, a commodity trading advisory company, Hamilton and Wasson, uses an Apple personal computer to transmit daily charts and text about the commodity markets directly to customers who used to receive the same information by mail (Wall St. J., 12-11-81, p. 29; N.Y. Times, 1-10-82, p. F2). With sales of desktop computers to the business and professional sector estimated to increase from 80,000 units in 1979 to 507,000 units in 1984 (an annual growth rate of 41.9%), machine-to-machine electronic communication will displace the more costly and slower second-generation electronic delivery of the Postal Service E-COM, as well as competitors such as Western Union's Telex or Hawaii's Telex and Teletype (Appliance Manufacturer, 2-81, p. 53).

In addition to the rapidly expanding business and professional market for word processors and micro-computers, the burgeoning home market will also affect the future of electronic mail. Approximately 20% of American households are expected to utilize personal computers by 1989 (Canadian Datatrends, 12-80, p. 26). Already, the home user has ready access to some 200-500 computer "bulletin boards" which service information and message-exchange needs. By using a micro-computer, communications software, and either a modem or acoustic coupler (minimum costs of about $750), messages may be scanned or posted. As the business community and individuals become more knowledgeable and sophisticated in the communications applications of inexpensive personal computers, we can anticipate greater use of direct electronic interchange of information at the expense of both public and private sector electronic mail systems, whether generation two or three (National Bus., 2-82, pp. 644; N.Y. Times, 2-21-82, p. F4).

Regulatory decisions and choices made by electronic mail users about whether to employ system suppliers such as the Postal Service or direct micro-computer communication links will have more than domestic consequences. As more of the world community enters the environment of the "post-industrial society," the nation in the best position to dominate the revolution in communications technology will likely have great influence over the future of international commercial and political intercourse (Economist, 1-16-82, pp. 13-14).


IV. NORTH AMERICA

DOMESTIC EFFECTS OF THE MEXICAN PESO DEVALUATION - On February 18, 1982, the Central Bank of Mexico allowed the peso to float. It rapidly fell 40% against the U.S. dollar. Depletion of the Bank's reserves for supporting the peso was the immediate cause of the decision to allow the floating. Underlying this catalyst were three interrelated economic problems: a growing trade deficit, capital flight, and inflation.

Last year Mexico's current accounts deficit doubled because of a combination of decreasing income from tourism and exports and increasing foreign debt. World recession dampened tourism and export sales. Lower
all prices resulted in a $6 billion shortfall in expected revenues from exports. Declining oil revenues were especially serious because of the predominant role oil and gas exports have come to play in Mexico's economy: in 1981 they accounted for 75% of merchandise exports, compared with 44% in 1979. In anticipation of a rumored devaluation, wealthy Mexicans have been converting pesos to dollars or to U.S. investment property and consumer goods. Ninety percent of new deposits in Mexican banks were in U.S. dollars, despite the fact that interest rates on peso accounts were 23 percentage points higher. Ten percent of Texas bank deposits were made by Mexicans. Over the last 10 years Mexicans have invested $6 billion (U.S.) in Texas real estate. High inflation rates underlie these other trends. In spite of government efforts to control inflation, largely by restricting oil production levels, prices in 1981 were climbing at a rate of 30%. Two factors were responsible for this problem: bottlenecks created by sudden oil wealth and rapid growth, and government deficits which have risen from 6% of GNP in 1980 to 14.2% in 1981. Much of this deficit has been financed through international borrowing. As a result, Mexico has built up a foreign debt second only to Brazil's among less developed countries (J. Commerce, 2-1-82, p. 1A; Wall St. J., 3-19-82, p. 14; 2-23-82, p. 30).

Certain effects of the devaluation are predictable. Some businesses are likely to have difficulties repaying debts because the peso shortage has encouraged many firms--U.S. subsidiaries, in particular--to borrow dollars. Economic growth is likely to slow to 4.5-5.0%, compared with the 6.5-7% predicted earlier by the government. Because minimum wage laws do not cover the majority of workers, real wages are likely to be reduced overall despite the government's recent announcement of a 10-30% wage increase. Unemployment will probably rise as a result of deferred business and government investment and increased bankruptcies. Border residents, many of whom buy consumer goods from U.S. merchants and borrow money from U.S. banks, are especially affected by the decline in the value of the peso. Voter apathy may rise and popular support for the government fall because of the dissatisfaction of the political left and organized labor, who were not consulted prior to the devaluation decision and who were angered by the government's failure to raise wages immediately and to impose price and foreign exchange controls (Wall St. J., 2-23-82, p. 3B; 2-2-82, p. 6; N.Y. Times, 2-22-82, p. 28; 2-20-82, p. 15).

There is debate over the longer-term implications of the devaluation. Some find cause for optimism in the smoothness with which the government handled the devaluation and the calmness of public reaction. In comparison with the 1976 devaluation, when panic was widespread and a nearly 45% price increase sent the economy into a recession from which it did not recover until oil production began in 1978. Then the Mexican economy was less developed, business-government relations were strained, and political instability and social unrest were fresh in the collective memory. The absence of these factors, according to some observers, presages a fairly rapid economic recovery (N.Y. Times, 2-22-82, p. 28; Wall St. J., 3-19-82, p. 11).

Other analysts regard the underlying situation as worse than that of 1976, when inflation was running at 15%. A few economists fear the advent of hyperinflation, and even the government predicts that inflation might reach 50-60%. At such rates, farm price supports, designed to revive Mexico's declining agricultural sector, will become virtually unaffordable. Agricultural prices have traditionally declined following devaluations in Mexico, and, unlike 1976, when world agricultural markets were expanding, such lower prices are not likely to spur exports. The net result will be further stagnation of Mexico's agricultural sector. On the other hand, government policies to mitigate the domestic effects of the peso devaluation may fan the flames of inflation. The government's 10-30% devaluation-related wage hike follows January's 34% raise. Because Mexico's swollen bureaucracy falls under minimum wage provisions, the latest increase will make it difficult for the government to carry out its promised 3% budget reduction. Similarly, the government's promises to increase incentives for exports, to assist injured businesses by allowing a 42% write-off of losses incurred as a result of devaluation, and to aid border residents, make many observers doubt it will follow through with its announced budget cut (Wall St. J.,
Ironically, this budget reduction, although generally regarded as necessary, would further retard economic growth and could lead to social unrest. Mexico's poor, for example, may perceive that their relative share of national income has been reduced since the discovery of oil, a fact heretofore concealed by growing incomes in all strata. If, however, the government does not reduce the budget, it will damage its credibility, already tarnished by its failure to control inflation and transform Mexico's oil riches into a more equitable income distribution.

Abroad, reduced faith in the Mexican government and economy could raise the rate Mexico must pay to borrow in the international market from 4.5 to 5.0 percentage points above the London Interbank rate, an increase in debt servicing that would exacerbate Mexico's balance of payments problem (Wall St. J., 3-19-82, p. 14; 3-26-82, p. 30).

If the recent devaluation proves to have worse repercussions than that of 1976, the critical differentiating factor will probably be inflation. Unlike Brazil, Argentina, and Chile with their relatively closed economies, Mexico is unable to tolerate high inflationary rates. Mexico's long border with the United States renders it an open economy. As long as wide differences exist between inflation rates in Mexico and those in the U.S., capital will continue to leave Mexico and imported goods will remain cheaper than those manufactured in Mexico. Devaluation is a method of treating symptoms, not causes. If Mexican leaders do not fashion policies that address the causes of inflation, not only will another devaluation soon be necessary, but some of Mexico's basic goals, such as diversification of its economy away from dependence on oil, will be postponed indefinitely (Qtrly. Review of Econ. and Bus. 21(2): 115-30, Summer 1981).


V. EDITORIAL

FREE TRADE EXCEPTIONS - While the predominant thrust of western international economic policies since the Second World War has been to promote and foster free trade, it is clear that the mercantilist trade philosophies of the 18th century die hard. The problem is a perennial one facing government administrators and policymakers. While sound theoretic economic reasons exist for instituting certain international trade actions that increase the aggregate welfare, few theoretic guidelines are available to follow in the distribution of these gains. Of more delicate import is the fact that policy actions to foster free trade often involve losing sectors within a country which could theoretically be compensated by the "gainers," but which in practice seldom are. Allowing cheaper textile imports into the United States may benefit the majority of the consuming public, but explaining this to unemployed textile workers has never been a politician's or policymaker's forte.

Governmental trade negotiations, both at multilateral and bilateral levels, have always posed tricky governance problems. The overall benefits of free trade are rarely at issue, general consensus having long been reached and recorded in the preamble of the General Agreement on Trade and Tariffs (GATT). Agreement on necessary exceptions to free trade, however, is difficult to achieve. Domestic policy objectives together with the wishes of vocal and powerful political action groups may often be in conflict with and take precedence over international arrangements and agreements. The political survival of a government may
often hang in the balance, as is illustrated by the difficulties the Belgium government has experienced over the plight of its steel industry.

While competition will operate successfully when a consistent set of rules applicable to everyone is in force, strong incentives to violate these rules are always present. Whether or not violations are a real threat to that competition depends in some degree on whether they are a form of economic chauvinism or a short-term expedient designed to defuse a temporary political problem. For example, the European Economic Community's Common Agriculture Policy (CAP) has two main themes. First is the recognition that much of the local agriculture is on acreage too small to compete with larger-scale producers abroad, so that time and protection are needed to rationalize the domestic production system. The second theme is a national security one, whereby the Community is anxious to maintain a measure of food self-sufficiency. Both objectives have legitimacy, certainly given domestic political realities, but the first is a short-to-medium-term policy goal. As often occurs with temporary policy objectives, however, the insulate domestic producers from the harsh reality of competition that little incentive exists to bring about the desired rationalization.

Japan's non-tariff barriers and the less developed countries' "infant industry" arguments contain similar domestic political rationales that are often difficult to displace once they have been introduced. This is especially true in developing countries where tariffs or government subsidies have long protected inefficient local producers. These protected sectors may constitute a powerful political coalition of unionized workers and local business people that inhibits gradual removal of the protection, as envisaged when it was first introduced.

Competitive advantage is not impervious to the dynamic influences of a changing international economic order. Industries that were once unassailable become inefficient producers and political liabilities as comparative advantage bascions its largesse on other regions of the world. In consequence, we can expect continual pressures for protection or subsidy as governments wrestle with tensions among their constituencies. Wise negotiators learn to recognize and assess the magnitude of these domestic problems because they do represent areas where a government has less room for maneuver. If governments are granted relief during trade negotiations in areas of prime concern to them from a domestic political stability perspective, they will be more willing to accede to other issues.

Success in the negotiation and implementation of international economic agreements rests upon a mutual appreciation of each involved party's political environment and domestic problems. Only on this basis can a sound evaluation be made of the validity of requests for exceptions or of the weight of protectionist pressures. Negotiators must focus not only upon the "losing" sectors within their own country but also on those within other countries. How strong are the losers politically? How important are they to the overall economy, and what is the magnitude of such macro-economic factors as unemployment and economic growth? All too often, each country brings to the negotiating table extensive awareness of its own specific grievances but little understanding of the legitimacy of another country's concerns. At best this may cause considerable delay; at worst, positions may harden to the point that protectionism becomes an uncomfortable reality.


