AHN JUNG-KYU

Edmund S. Phelps, right, recipient of the 2006 Nobel Memorial Prize in Economic Sciences, has a conversation with SaKong Il, an adviser to the JoongAng Ilbo, on Feb. 21 at Phelps' office in Columbia University.

The fate of free markets in age of Trump

Nobel laureate finds the president's early intervention troubling

BY SONG KYUNG-JIN

Edmund S. Phelps, recipient of the 2006 Nobel Memorial Prize in Economic Sciences, called the Trump administration's market intervention in the United States excessive during a recent conversation with SaKong Il, an adviser to the JoongAng Ilbo. The Columbia University professor said the president's actions could jeopardize the integrity of American capitalism and the free market.

Phelps discussed the current state of the U.S. economy with SaKong on Feb. 21 at his office in Columbia University in New York. Here are edited excerpts from the interview.

SaKong: How do you explain the so-called Trump phenomenon? What socioeconomic or political factors do you think made people choose a nonconformist like Trump as president?

Phelps: I am not sure if we have gotten to the bottom of that. I feel that one reason Democrats lost is they seemed to pay no attention to the white working class in the Appalachian mountains — in those states like upper New York, Pennsylvania, West Virginia, Kentucky, and also over to Iowa and as far as Ohio. So the Democrats lost badly. Those people feel neglected. They are expected to be self-reliant while everybody else is at the public trough receiving all sorts of subsidies and contracts and everything.

And I think their attitude is a little bit unfair because after all, they do have all the welfare benefits that other people in the country have. I think their problem is they've lost meaningful jobs, meaningful work. They used to have factory jobs which had a degree of autonomy, that required a little bit of judgment, and then you can feel important doing these jobs. And they lost those jobs.

But it has to be said that Democrats were also a victim to the indifference of a lot of people to the left. Many people on the left felt that the Democrats were not addressing the issues of the left. I don't know whether I can claim to be left to some degree, but I do think that the Democrats did not do much for the working people, low-paid people. The blacks in the United States did not turn out to vote. They did not go to vote. That indicates that they felt that the Obama presidency did not pay enough attention to inequality, which is a different sort of issue than the Appalachians.

SaKong: How do you see the 1-month-old Trump administration? You have been widely quoted as saying that this country has not seen such policies since the fascist policies in the early 1930s.

Phelps: What struck me about Donald J. Trump is that he seems to want to be a puppeteer that's controlling the economy right down to the individual firm or even the individual plant. This is incredible. That would be extremely destructive for the performance of a capitalist economy. A capitalist economy can't perform well unless it's able to exercise its strengths, which are spontaneous leaping to take advantage of new opportunities, imagining and creating new possibilities. All of that would be very much hurt if success requires a good fortune of support by the government.

SaKong: You have been highlighting the downsides of corporatism. I am sure you are concerned about acts of interventionist corporatism by Mr. Trump, for instance pressuring Carrier, Ford, et cetera, not to relocate to Mexico while aiding Google and other companies.

Phelps: Corporatism is inherently very interventionist. It really started with the Christians in the 1890s. They said that we all have to help one another, and in particular, the companies have to help their workers provide medical care and all sorts of benefits. And then Mussolini came with a much broader concept of corporatism in which every industry sort of watched and had to behave according to what's good for the society as a whole. Some industry was expected to produce more and some other industry was expected to produce less. Needless to say, Mussolini's corporatism did not perform well as all.

SaKong: Direct intervention in the name of protecting jobs will in fact likely reduce jobs and make the economy less efficient. You said one cannot overemphasize the importance of encouraging entrepreneurship and start-ups. Direct government intervention inspired by corporatism hurts the spirit of the market economy.

Let's turn to another subject. Trump blamed trade for reducing jobs and causing unemployment. In any case, the primary goal of Trump's policies is to close the trade gap. But concentrating on the trade deficit may lead the economy into a vicious cycle with more protectionism and more unemployment.

Phelps: Correct. We know that nations as a whole benefits from trade. That's for sure. I think one can also argue that employment is also helped by trade, generally speaking. But as we have not done very well on addressing the losers from trade, there has been a lot of pretense that a rising tide lifts all boats.

SaKong: I fully agree. I suppose economists and policy makers have always been emphasizing the overall net macroeconomic benefit without paying enough attention to the downsides, particularly the distributional aspect of trade and the losers, both in terms of workers and industries.

Now let's talk about the relationship between innovation and jobs in the context of the so-called fourth industrial revolution.

Phelps: Some think that robots leading to automation will on the whole destroy jobs and reduce employment, so that we just have to get used to a new way of life in which we maybe only go outdoors and work and sell them. Some even joked that they need a night watchman and a dog to watch the night watchman. I don't believe this. Throughout history on the whole, innovations have made labor of all sorts more productive, made capital more productive and made land more productive — ultimately, a society in which the workers are phenomenally productive thanks to innovations. And society ended up with higher wages, not lower wages. But I have to work more on that. But I am sure appropriate education and labor reforms will help produce more jobs.

SaKong: Going back to Trumponomics, you said President Trump must stress competition more than deregulation. Could you elaborate on that?

Phelps: I think the answer is competition. We can get competition so that the companies are running scared and they have to innovate in order to save themselves. If we can get back to that, that we will be OK. At least, I think that's a big part of it. But there's not much support for that. People want so much security, and the politicians want to give them stability.

SaKong: I know you have been advising Li Keqiang and other Chinese leaders. You've written elsewhere that even already dynamic economies can get into severe doldrums, and on the other hand, torpid economies can rise perhaps in a delayed time span. That brought me to China. You were quite optimistic about China last time. Is that still your view?

> 'A capitalist economy can't perform well unless it's able to exercise its strengths.'

Phelps: Yes, I was optimistic. However, I confess I don't have any persuasive answer now. I do think that China is paying the price for some unfavorable institutions and organization of the economy. On the other hand, they continue to create new firms, and young people continue to be in those new firms, and it looks like the forces of innovation in China are very real and powerful. But it seems they have not been strong enough to overcome the institutional mishaps and institutional weaknesses of the economy, even after these past six or eight years of testing times. We will have to wait and see what the future will bring.

SaKong: So it sounds like the future of the Chinese economy depends on institutional reforms and restructuring along with continued innovations, and it is too early to make any decisive conclusion at this point. What is your longer-term view of the U.S. economy, which has always been more dynamic than any other advanced economies?

Phelps: I'm among those who find serious faults with the American economy, but I think one reason why the U.S. economy pulled completely out of the global slump created by the global financial crisis was entrepreneurship and innovation. This is a country that is still innovating, and it is a country where there are some energetic entrepreneurs constantly on the lookout for new opportunities. Both of these things — entrepreneurship and innovation — were present and are present in the U.S. economy. And that's primarily what I think pulled the economy back up.

Entrepreneurs and innovators walking down Main Street would see — I love this metaphor — storefronts that are closed and say, "Oh, I gave up on my idea before because I didn't think I could find the workers, find the floor space and find the customers because all these firms were there. But when some of them aren't there anymore, there are vacant stores. Maybe I can seize this opportunity to try my new idea." I think it's happening. I think it's happened to a degree.

SaKong: I recall your earlier point that too much intervention and government control undermined growth.

Phelps: If we could fix all that, maybe the growth rate of total factor productivity will go from 1 percent back to 2 percent. That's tremendous. That means doubling your productivity every 36 years instead of every 72 years. It's huge. It mounts up to something enormous.

SaKong: That is exactly the power of compound interest. Since economic growth is the game of compound interest, even a small difference in growth rates will turn into a huge gap quite soon. The two Koreas, South and North, dramatically illustrate this point.

Song Kyung-jin is president of the Institute for Global Economics.

Phelps broke ground linking unemployment, inflation

BY SHIM JAE-WOO, JIN EUN-SOO

Edmund S. Phelps is a towering figure in economics and continues to be active in the field. When the JoongAng Ilbo met with him in his office on Feb. 21, the 83-year-old Columbia University professor couldn't spare even a few minutes afterward because he had to leave for Mexico right away for a business trip.

In 2006, the Nobel Memorial Prize in economics committee recognized Phelps for his research in the 1960s that found a correlation between unemployment and inflation.

Before Phelps' study, a theory called the Phillips curve, which claimed that unemployment and inflation moved in the opposition direction, dominated the academic scene. The curve, which was based on past cases, implied that people had to endure high inflation in order to lower the unemployment rate and vice versa.

Entering the 1970s though, the theory didn't seem to hold anymore as stagflation, with both inflation and unemployment rising, persisted.

Finding the Phillips curve was no longer applicable, Phelps defined a "natural rate of unemployment" that existed regardless of government policy. The fact that monetary policy could not affect soaring unemployment led many countries to instead focus on price stabilization.

After receiving the Nobel Memorial Prize, Phelps served as an economic adviser to Chinese Prime Minister Li Keqiang, and for his contributions, he received the National Friendship Award from the Chinese government in 2014.

Phelps was born in Evanston, Illinois, and received his Ph.D. in economics from Yale University in 1955, studying under Nobel Memorial Prize laureates James Tobin and Thomas Schelling among others. After five years as a professor at the University of Pennsylvania, he joined the Columbia faculty in 1982.

Some of his notable books include "Rewarding Work: How to Restore Participation and Self-Support to Free Enterprise" (1997), "Structural Slumps: The Modern Equilibrium Theory of Employment, Interest and Assets" (1994), and "Inflation Policy and Unemployment Theory" (1972).

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