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Great Britain: New Inflationary Impulses

One year after the beginning of the tougher incomes policy no slackening of the inflationary development can be foreseen in Great Britain. Last but not least strong external inflationary impulses made it unavoidable for the Government to somewhat loosen the wage and price controls for Phase III of the incomes policy. Already now the new framework is in danger, however, to be broken by labour disputes within the country's power industry. In addition there are the effects of the oil crisis.

Declining Expansion of Consumption

Total national production, which had decreased during the second quarter after the forward shift of demand due to the introduction of the added-value tax, has risen again, though at a slower rate than it did until spring. In the matter of demand especially the stimulating forces originating from private consumption have weakened. Adjusted for price and seasonal variation it showed a recovery, but its level did not surpass the average position of the first half

year. Against this in investment activities the expansive factors should have clearly reasserted themselves after distortions in the course of the first half of the year.

Increasing External Imbalance

As to foreign trade the expansion of exports in the third quarter was significantly left behind by that of imports. Since during the last three months until September import prices had been rising much faster than export prices (12.9 p.c. vis-à-vis 3.7 p.c.) the foreign trade deficit increased substantially. Altogether, between January and October it corresponded to £ 1.8 bn for the whole of the year, i.e. it was twice as high as in 1972. With the exorbitant rise of import prices the continuous devaluation of the pound sterling played an important part; so did the strong upward trend of prices in international trade to which finally — especially in the case of crude oil — an extraordinary impulse was given.

Under these circumstances industrial raw material prices rose

until October by 42.0 p.c. within a year's time. During the same period producer's prices for semi-finished and finished goods increased by 10.6 p.c. Not much lower was the rise of private cost of living, last but not least caused by the strong upward movement of food prices. While since the middle of the year the tendency of prices to rise grew stronger again, the upward movement of wages slowed down, primarily because no important wage agreements had to be concluded at the time.

1974: Further Slackening Growth

In the course of the year British economic policy has with the progressional devaluation of the pound got into a dilemma. The Government thus adopted a restrictive monetary policy in order to dampen the pressure on the pound by changing the margin between domestic and foreign interest rates. The limitation of growth in the volume of credit will, however, further restrain the expansion of demand. Consequently, even if the shortage of energy is not taken into consideration, it seems uncertain whether the demand-stimulating forces, which are still resulting from private investments and exports, will guarantee the maintenance of

Index Numbers of World Market Prices of Foodstuffs and Industrial Raw Materials

Index and commodity group	1972	1973					
	November	February	May	August	November	Nov. 16	Nov. 30
HWHA-Index * (1952-1956 = 100)	122.7	142.8	163.7	190.7	208.9	207.4	221.5
Foodstuffs	119.8	141.5	158.9	189.6	193.9	195.9	193.8
Raw materials other than foodstuffs ...	124.0	143.4	166.1	191.2	216.3	212.9	234.9
Fuels	130.4	137.9	153.3	155.0	182.7	177.8	215.7
Raw materials for consumer goods ..	123.9	153.9	171.8	209.1	194.4	193.0	199.1
Raw materials for capital goods	117.7	141.9	175.1	215.6	264.0	261.6	278.3
Reuter's Index (18. 9. 1931 = 100)	675.7	827.1	905.4	1175.1	1217.7	1216.6	1292.7
Moody's Index (31. 12. 1931 = 100)	447.5	499.9	529.4	678.9	671.8	678.2	—

* Index compiled by the Hamburg Institute for International Economics. On dollar-basis.

the achieved degree of utilisation. Thus a rough bisection of the growth rate of Gross Domestic Product in real terms of 5.5 p.c. reached in 1973 may be expected for 1974.

The shortage of energy resulting from the labour disputes as well as the uncertainty about crude oil developments forced the Government in mid-November to announce an energy emergency

programme. It becomes already obvious that a continuance of the international crisis of oil supplies will also affect Great Britain's expansion of production. After all nearly half of its energy supply is based on crude oil. Already now the sudden enhancing of its price means a worsening of the balance of trade and a new impulse for the tendency of prices to rise.

corporations about a revision of the price agreement in Teheran, the upward trend of market prices caused the OPEC-countries to raise the posted price (which is the basis of levies and taxes) by 70 p.c. in October 1973. Hitherto the oil corporations passed on only moderately the cost price increase via higher prices of oil products. But panic buyings of mineral oil and its derivatives effected a price explosion on the free markets.

Raw Material Markets

Supply Crisis in Mineral Oil Markets

The oil boycott of the Arabian oil exporting countries happened at a time, which had already been marked by an increasing world-wide shortage in mineral oil; the reason was the enormously increasing import demand of the USA. At the beginning of October this shortage had grown worse because of the war in the Near East; large quantities of mineral oil could not be transported out of the eastern mediterranean ports. Directly affected by the oil boycott are mainly Western Europe and Japan. The West European countries receive more than 70 p.c. of their oil requirements — in view of their own small production — from Arabian states. Due to its large own oil output, the independence of the USA of

the supply with Arabian mineral oil is greater. In the first half of 1973 Arabian oil's share in total US-supply was only 5 p.c., while the Arabian countries' rapidly growing share in the oil imports of the USA reached in the meantime nearly 25 p.c. But due to its insufficient output of natural gas and its insufficient refinery capacities the USA's import demand for mineral oil derivatives is rapidly increasing. So far in view of the worldwide scarcity in oil derivatives the USA is also affected indirectly by the oil boycott.

Due to the expected oil shortage relatively high price increases preceded the latest abrupt rise in prices of mineral oil and its derivatives. After the unsuccessful negotiations with mineral oil

At present an end of the Arabian states' boycott is not in sight. If export limitations will be maintained for a short period only, the reserves in the consuming countries will be sufficient — together with the policy of retrenchment — to avoid aggravating detriments to their economic development, although in the long run the energy supply will be influenced by the oil shortage. In any case price rises will last. If the boycott will go on for a longer time, steep declines in production and employment will surely not be avoidable. A large-scale transition to other resources of energy and forcing the output of mineral oil outside the Arabian world needs much time and large funds for financing purposes.

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