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WORLD BUSINESS TRENDS

World Economy in Stagflation

At the turn of the year, the industrialised countries' economic development is characterised by an extensive cyclical downswing that started in the US and Japan already in 1973. By now the expansive forces have more and more slackened also in the West European economies. Unemployment is rising almost everywhere. At the same time the extraordinarily strong upward movement of prices generally continues and in most cases there are no signs yet for a reduction of the deficits in the balances of current transactions which have been caused, or raised to an exorbitant magnitude, by the explosion of oil

prices. Thus at the end of the year 1974 the authorities concerned with economic policies are in many countries faced with the fact that they have more or less missed all their main aims simultaneously.

1975: Small Growth Rates, Continuing Inflation

In this situation of conflicting aims, the orientation towards restrictive economic policies, which had for some time been clearly dominating, has already been given up by a number of industrial countries. Provided that this re-orientation of economic policy continues, the

downward tendencies of production and employment, which currently prevail in the industrial countries, may be expected to come to an end in the course of the next year. Thus demand and output will at last begin to rise again which, however, as a rule, will hardly mean a new upswing in the proper sense of an increasing utilisation of productive capacities. After the total stagnation during 1974, the industrial countries' average growth rate of GNP for 1974 will probably amount to no more than roughly 1 p.c.; GNP deflators are expected to rise again at a rate of almost 12 p.c.

West Europe: Economic Policy Already Expansive

In West Europe — particularly in the Federal Republic of Germany, Denmark, Great Britain, the Netherlands, and Austria — significant fiscal stimuli have already been agreed on. Measur-

Gross National Products of the OECD-Countries

(Comparison with a year earlier in p.c.)

Country / Region	At constant prices			At current prices			Price Index of GNP		
	1960-73 ^a	1974 ^b	1975 ^c	1960-73 ^a	1974 ^b	1975 ^c	1960-73 ^a	1974 ^b	1975 ^c
USA	4.2	-1.5	-0.5	7.4	8.0	10.0	3.1	10.0	11.0
Canada	5.4	4.0	2.0	9.1	17.0	13.0	3.5	13.0	11.0
Japan	10.4	-3.5	3.0	18.4	20.0	18.0	5.4	24.0	15.0
West Europe ¹	4.7	2.5	2.0	9.9	13.0	13.5	4.9	10.0	11.5
Austria	5.0	5.0	3.5	9.7	15.0	14.0	4.5	9.0	10.0
Belgium	5.0	4.0	3.0	9.3	13.0	14.0	4.1	10.0	11.0
Denmark	4.7	1.5	1.5	11.5	15.0	17.0	6.5	13.0	15.0
Fed. Republic	4.6	0.5	2.0	8.9	7.0	9.0	4.1	6.5	7.0
Finland	5.1	3.5	2.5	11.6	19.0	18.0	6.2	15.0	15.0
France	5.7	4.5	3.5	10.8	16.0	17.0	4.8	11.0	13.0
Great Britain	2.8	-0.5	1.5	8.1	12.0	17.0	5.2	12.0	15.0
Italy	5.1	4.0	0.0	10.6	20.0	15.0	5.2	15.0	15.0
Netherlands	5.2	3.0	3.0	11.2	12.0	13.0	5.7	9.0	10.0
Norway	4.9	4.5	5.0	10.0	14.0	15.0	4.9	9.0	9.0
Spain	7.3	5.0	4.0	14.3	16.0	15.0	6.5	10.0	11.0
Sweden	3.8	4.0	3.0	8.9	13.0	13.0	4.9	9.0	10.0
Switzerland	4.4	1.0	0.0	9.8	9.0	7.0	5.2	8.0	7.0
OECD-countries total ¹	5.2	0.0	1.0	9.5	11.5	12.5	4.1	12.0	11.5
OECD-countries total ²	5.0	2.5	2.0	10.0	13.5	14.0	4.8	11.0	11.5

¹ Weighted by GNPs and exchange rates of 1972; OECD without Australia. ² Weighted by shares in German exports in 1972.
^a Average annual change. ^b Estimates rounded off to 0.5 p.c. ^c Forecast. Sources: OECD, EEC, national data, own estimates.

ed in real terms, GNP might in 1975 still grow by 2–2.5 p.c. altogether, which is again only half of the long-term average. In view of the slow expansion of production, rises of productivity will in many cases be only modest so that a checking of internal cost increases is rendered difficult. In these circumstances it must be doubted that the expected stabilisation or even reduction of prices of imported raw products — where prices of raw materials, fuels and food-stuffs may well show diverging developments — will be sufficient to weaken the upward trend of the general price level. Nor are there any signs for a significant overall improvement of the imbalances in foreign trade and payments.

USA: High Unemployment, Heavy Price Increases

The US Government will, in view of the rapid increase of the unemployment ratio which amounts to 6.5 p.c. of the labour force, not be able to put its anti-inflationary policy into execution. But even if it takes a new tack, GNP in real terms will — if only because of the usual time lags — increase not before the later part of the coming year. It does not seem very likely that the upward trend of prices which, until now, has lost

nothing of its strength, can be significantly weakened during the year 1975.

Japan: Deficit in the Balance of Current Transactions Reduced

In Japan harsh restrictions led to a drastic reduction in the deficit of the balance of current transactions since the middle of 1974. The producer prices, in contrast to the consumer prices, have also risen, though still slowly. So much the more — in view of the steep decline in the utilisation of capacities and a prospective decline in employment — there will be increasing pressures on the Government to take expansion promoting measures. The present stagnation — after a sharp decline in production early in 1974 — in 1975 should be replaced by a gradually accelerating growth of GNP in real terms.

Monetary Policy as "Crisis Management"

A decisive condition for the outlined business trend forecast is the further avoiding of external liquidity crises of important countries in spite of continuously high "oil deficits". This, to begin with, will probably only be achievable with the aid of interstate support actions — also if exchange rates are floating on principle. In this context

there is the dilemma, on the one hand, not to delay for too long the necessary dislocation in the streams of transactions, which impairs the wealth of the deficit countries, and, on the other hand, to prevent the flight into a shortsighted national protectionism. It is just rising unemployment that increases this danger.

Inflation as the Central Problem

From a standpoint beyond the immediate future the solution of the inflation problem seems to be even more important. This problem has been merely intensified, but not created by the oil price explosion. The high price increases handicapped the governments in an early cyclical counter-steering, and now the intensified struggle for income distribution threatens to impede considerably the employment effects of expansive measures. Thus the renunciation of an inflation mentality will obviously become the prerequisite to a lasting improvement of the economic situation and with that of employment.

Compiled by the Department on Business Cycles and Statistics of the Hamburg Institute for International Economics.

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