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The Crisis of Economic Policy

The economic situation in the western industrialized countries has been exacerbated further in the first months of this year. Some evidence of initial successes in fighting inflation and overcoming trade imbalances is at hand, but almost all countries have still a long way to go before stabilization. Simultaneously the contractive forces have gained greater ascendancy over production and employment than at any time since the war. The gross national product of the western industrialized countries has been declining adjusted for price since last autumn, and unemployment has risen in all major countries to a point indicative of underemployment of the economy. More and more often one hears the question asked whether the world economy is on the brink of a slump as in the early thirties.

Seeing that the aim of full employment holds a dominant position in economic policy, it is not surprising that in this situation the governments have despite persisting stabilization problems turned increasingly from a policy of demand restraint to one of encouraging expansion. The Federal Republic of Germany — where stabilization has been most successful — and the USA have gone farthest in this respect, but Great Britain, France and even Italy — all countries which had to brake sharply because of big price rises and their extremely high balance of payments deficits — have followed a similar course

though to different degrees. Since they have coped relatively well with the recycling of the petrodollars and the oil deficits promise to abate more quickly than expected, the external economic troubles now apparently take second place to employment problems. It is only too easy to overlook the fact that the reduction of the oil deficits is only partly due to the surprisingly swift increase in the absorptive capacity of the oil exporting countries. The crucial factor was the weakening of the demand for mineral oil products in consequence of the recession in the industrialized countries. The more successful the policy of demand stimulation proves to be, the stronger will be the position of the oil exporting countries.

In a still markedly inflationary climate it is imperative that the effectiveness of stimulatory measures should receive careful consideration. Optically impressive though they may be, they must be deflated to show how far they go in actually stimulating production rather than fanning inflation. The recent slowdown of the uptrend of prices in most countries has reinforced hopes that the prices and wages are not yet entirely unresponsive to cyclical changes; the substantial underemployment of available resources will certainly tend to damp down activity throughout this year. There is thus good reason to believe that the expansionary measures will — at least in the later part of this

year — stimulate production in the industrialized countries and, after some delay, help to expand employment.

It is not to be expected however that the fierce allocation struggle in the form of the price-wage spiral will subside as much as in the analogous phases of previous economic cycles. On the contrary, it will probably revive comparatively early. This would put a return to the high employment levels to which the industrialized countries have long been accustomed in jeopardy, either because resurgent inflationary expectations would prevent real demand from rising sufficiently or because more and more governments would resort to short-term stop-go policies which impede the full deployment of economic forces. In the medium term the fight against inflation is the prerequisite and not an alternative to assured employment.

Seeing that even the tumble from the ascending employment path of the fifties and sixties has apparently failed to induce the social groups to go back to the "rules of the game" observed during those years, one may well ask whether the prevailing economic order can still work efficiently under manifestly changed social conditions. The world-wide recession will thus provide fresh evidence for the fundamental discussion of the aims and instruments of economic policy in the western industrialized countries.

Günter Großer