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# ECONOMIC TRENDS

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## Prices Advancing More Slowly in Industrial Countries

While in most industrial countries the hopes for a progressive acceleration of the slack growth have been dashed by the development of production and employment since the spring of 1977, notable successes have been achieved in curbing inflation. On the consumer level the price rise in the industrial countries of Western Europe still averaged 10% in June 1977 (compared with the same month a year earlier) — by June 1978 it was down to 6½%. In Japan the rate receded from 8½ to 3½%. In the USA on the other hand it speeded up to 7½%. Several countries, including Japan, the Netherlands, Belgium and Austria, have followed Switzerland and the Federal Republic of Germany in bringing the price rise down to the rates recorded in the sixties. The other industrial countries have almost all at least left two-digit inflation behind.

That the prices in Western Europe and Japan have risen more slowly does not mean generally that the advance of current prices slowed further in the first half of 1978. The continuing letup compared with the preceding year was largely due to a basis effect which in several countries was felt especially strongly during recent months because fiscal stabilization efforts had led to a bunching of upward revisions of public utility charges and indirect taxes in the first half of 1977. This was one reason why the prices of oil products and electricity and in some countries also the charges for services (e.g. transport) have been rising rather more slowly. The slowdown was less marked for durable and other consumer goods (not incl. fuels) and for residential rents. It was most pronounced for food, drinks and tobacco; the relapse of the coffee and cocoa prices was here

of great help. For these as well as various other products general factors have for several years already been outstripped as short-term price determinants by supply variations due to crop fluctuations. The marked slowing of the price rise for foodstuffs was thus a "fortunate incident" as far as the price stabilization efforts are concerned.

### **Uptrend of Wages Weakened Further**

Inflationary expectations were evidently tempered as the uptrend of prices weakened. This was important for wages as the preservation of real wage levels is generally a minimum aim in wage negotiations. In a number of countries wages therefore again advanced less strongly this year — in some much less strongly. The differences between individual countries remained, however, in keeping with the inflation rate differentials. The wages of industrial workers in Switzerland, Austria, the Netherlands, the Federal Republic of Germany and Japan were at the last count 3–6% higher than 12 months earlier; in Sweden, France, Denmark, Great Britain and Italy they were still rising at the two-digit rates. The biggest increase was again noted in Italy (a good 17% in

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## ECONOMIC TRENDS

### Consumer Prices

(Change over preceding year in %)

Country	June		
	1976	1977	1978
Switzerland	1.1	1.8	1.1
Federal Republic	4.5	4.0	2.4
Austria	7.5	5.8	3.2
Netherlands	9.4	7.2	3.4
Japan	9.1	8.5	3.5
Belgium	9.4	7.8	3.7
USA	5.9	6.9	7.4
Great Britain	13.8	17.7	7.4
France	9.2	10.2	9.0
Italy	16.3	18.6	12.2

based HWWA Index of World Market Prices industrial raw materials were at mid-1978 on average only 2% dearer than 12 months earlier. This means that the large majority of industrial countries were actually importing raw materials more cheaply in terms of their own currencies as these had gained ground against the dollar.

### Exchange Rate Movements Underscore Inflation Differentials

the year to April); even so the rate has been about halved in one year. The slowing of wage rises must for the most part be seen in the context of the still very high unemployment. The "response" of the negotiating parties was probably hastened or strengthened by the efforts of many governments for an incomes policy. In Great Britain the incomes policy conceded a more substantial uplift to wage- and salary-earners as they could not be expected to accept further real income losses; while the guidelines were exceeded by a substantial margin, there would certainly have been even

more "making up for arrears" had there been no incomes policy.

### Raw Material Prices under Pressure

The slower uptrend of wages was not fully reflected by the unit wage costs because the rise of productivity slowed at the same time. On the other hand, in most industrial countries lower interest rates helped to keep costs down between mid-1977 and mid-1978, and the favourable price trend for imported raw materials was a stabilizing influence of some weight. According to the dollar-

The different price trends in the USA on the one hand and most other industrial countries on the other, seen against the background of a fundamental current account deficit in the USA, were one factor which kept the dollar under strong pressure this year. Expectations about future international inflation differentials had in this respect more effect than the actual changes. The consequent real up- and downward movements of exchange rates reinforced the anticipated trends because they conduced to importation of stability into revaluing countries and of inflation

### Determinants of the Price Trend

(change over preceding year in %)

	Money Supply M <sub>1</sub>		Interest <sup>1</sup> (level in %)		Effective Exchange rate		Average Import Values		Wages <sup>2</sup>	
	1977 June	1978 latest value	1977 June	1978 June	1977 June	1978 June	1977 2nd quarter	1978 last three months	1977 June	1978 latest value
Belgium	6.8	9.5 <sup>a</sup>	8.9	8.2	7.6	2.6	2.8	0.3 <sup>b</sup>	9.5 (t)	6.1 (t) <sup>a</sup>
Federal Republic	5.7	13.5 <sup>c</sup>	6.6	5.6	8.5	6.9	3.6	- 5.9	7.7 (t)	5.6 (t) <sup>d</sup>
Denmark	6.9	8.6 <sup>c</sup>	16.1	15.9 <sup>c</sup>	0.1	2.7	10.4	2.6 <sup>a</sup>	10.1 (v)	13.8 (v) <sup>a</sup>
Finland	11.5	6.8 <sup>b</sup>	10.8	9.7	- 5.4	- 8.6	17.9	16.4 <sup>a</sup>	8.7 (v)	.
France	5.9	11.9 <sup>a</sup>	9.9	10.8 <sup>c</sup>	- 6.4	1.4	15.9	3.1 <sup>c</sup>	12.4 (t) <sup>e</sup>	12.0 (t) <sup>b</sup>
Great Britain	11.6	23.4 <sup>c</sup>	13.3	12.8	- 3.6	2.8	18.9	2.9	8.8 (m)	14.4 (m) <sup>c</sup>
Italy	20.1	23.6 <sup>b</sup>	14.8	13.6	- 6.2	- 3.9	11.0	7.0	29.4 (t)	17.4 (t) <sup>b</sup>
Netherlands	16.7	9.5 <sup>b</sup>	7.5	7.0	7.2	3.3	4.7	.	4.9 (t)	5.8 (t) <sup>c</sup>
Norway	13.8	9.5 <sup>c</sup>	7.3	8.5	5.5	1.1	8.5	.	10.8 (v) <sup>g</sup>	9.6 (v) <sup>f</sup>
Austria	5.4	3.9 <sup>c</sup>	8.7	8.3 <sup>c</sup>	7.5	3.2	5.9	- 0.4 <sup>b</sup>	9.6 (t)	3.4 (t) <sup>c</sup>
Sweden	6.2	15.5 <sup>d</sup>	9.7	10.2	- 0.4	- 8.7	12.1 <sup>h</sup>	9.9 <sup>c h</sup>	2.8 (v)	11.0 (v) <sup>c</sup>
Switzerland	3.7	18.3 <sup>c</sup>	4.5	3.4	- 2.2	24.5	10.6	- 12.6 <sup>c</sup>	1.2 (m) <sup>g</sup>	3.0 (m) <sup>f</sup>
USA	6.8	8.1 <sup>d</sup>	7.0	8.5	1.0	- 3.9	8.5	7.2 <sup>c</sup>	8.5 (v)	8.2 (v) <sup>d</sup>
Japan	6.2	11.9 <sup>c</sup>	7.3	6.0 <sup>c</sup>	10.2	26.2	- 1.7	- 17.4 <sup>c</sup>	11.9 (m)	6.3 (m) <sup>c</sup>

<sup>1</sup> Government bonds. - <sup>2</sup> Mostly manufacturing industry. - <sup>a</sup> March. - <sup>b</sup> April. - <sup>c</sup> May. - <sup>d</sup> June. - <sup>e</sup> July. - <sup>f</sup> 1st quarter. - <sup>g</sup> 2nd quarter. - <sup>h</sup> Import prices. - (m): Monthly earnings. - (t): Standard hourly wages according to collective agreement. - (v): Hourly earnings. - Source: OECD, IMF and national data.

into devaluing countries. Even in the USA with its very low ratios of imports to national product and consumer goods imports to private consumption many domestic producers have been given considerable scope for price increases by the weakening of foreign competition due to the decline of the dollar rate. The connection between the development of exchange rates and that of import prices in national currency is quite clear: In Japan, Switzerland and the Federal Republic of Germany — i.e. in the countries with strongly rising exchange rates — import prices were in the first half of 1978 on average considerably lower than a year earlier while the USA, Sweden and Italy — i.e. the countries with falling exchange rates — recorded substantial import price rises.

**Monetary Policy Back on the Expansion Track**

Even if analysts do not agree on what importance they should attach to the various determinants of inflation, the marked slowdown of the price upswing in the last 12 months has certainly some connection with the precedent monetary restrictions in most industrial countries. The latest acceleration of the money supply expansion — in many countries since the middle of

last year — is a warning sign pointing to future price movements. That the monetary expansion has gathered momentum does not by any means indicate that the economic authorities are now less intent on stability; in many instances it was due to external factors, namely to efforts to keep exchange rates in Western Europe and Japan from rising to undesirable heights. Whatever the motives however, there is now more scope on the money side for price increases. What use will be made of it depends on quite a number of other factors.

**Inflation Rates Will Not Subside for the Time Being**

The food prices will again play a specific role in the near future. Their destabilizing effect in the USA, and likewise their stabilizing effect in other industrial countries, will probably subside, assuming that crops will be more or less normal. As for the general cost factors, the imported raw materials will probably do less to moderate price rises. As oppressive inventories are reduced and suppliers operate more cautiously, the situation in some important markets will change in favour of the commodity producers although the raw material requirements in the industrial countries

will increase only slowly as the rise of production is still rather restrained; the mineral oil prices will probably be raised at the beginning of 1979. Exchange rate movements will again be of importance for the individual countries. Great importance will, as always, attach to the development of wages, beside the external cost impulses. That the inflationary expectations will subside and that they will exercise a moderating effect on wage contracts is not very likely against the background of a more expansionary monetary policy and a "normalization" of food prices. It is almost impossible to predict what successes will attend the efforts for an incomes policy, and this applies again with special force to Great Britain, Italy and France. In the USA the strong upsurge of prices may, on balance, be expected to slow down but Western Europe and Japan cannot count on further stabilization successes in the near future. In many industrial countries the inflation rates reached their lowest point probably in the last few months.

*Compiled by the Department on Business Cycles and Statistics of HWWA-Institut für Wirtschaftsforschung-Hamburg.*

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

Index and commodity group	1977		1978				
	August	November	February	May	August	Sept. 8	Sept. 22
<b>HWWA-Index * (1952–1956 = 100) .....</b>	<b>309.0</b>	<b>310.0</b>	<b>317.0</b>	<b>314.9</b>	<b>315.6</b>	<b>320.5</b>	<b>325.3</b>
Fuels .....	248.2	255.7	263.5	254.9	231.9	244.7	249.5
Raw materials for consumer goods ..	338.3	336.2	342.8	343.8	356.0	357.1	361.8
Fuels .....	548.8	552.2	562.7	556.7	561.6	562.3	582.9
Raw materials for consumer goods ..	187.9	176.7	181.4	186.5	196.4	195.6	196.2
Raw materials for capital goods .....	228.6	227.4	231.3	236.5	257.6	260.3	272.1
<b>Reuter's Index (18. 9. 1931 = 100) .....</b>	<b>1491.3</b>	<b>1477.4</b>	<b>1395.1</b>	<b>1473.3</b>	<b>1441.5</b>	<b>1482.2</b>	<b>1476.9</b>
<b>Moody's Index (31. 12. 1931 = 100) .....</b>	<b>833.5</b>	<b>839.7</b>	<b>901.4</b>	<b>916.1</b>	<b>927.8</b>	<b>937.9</b>	<b>948.8</b>

\* Index compiled by HWWA-Institut für Wirtschaftsforschung-Hamburg. On Dollar-basis.