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USA: Recession Merely Deferred

In analyses of the cyclical events in the USA against the background of the so far unfulfilled recessionary expectations it is often overlooked that the US economy has already been in a state of stagflation for a full year. While prices have surged ahead much faster, industrial production has remained unchanged; the real gross national product was in the fourth quarter of 1979 only 1 % up on the year before. The capacity utilization rate was lower; in manufacturing industry, for instance, it declined – seasonally adjusted – by two percentage points between the first and fourth quarter. The situation in the labour market remained surprisingly favourable, for the number of persons in employment increased up to the end of the year; in the fourth quarter it was 2 % higher than a year earlier. The decline in productivity indicated thereby was however a material factor in speeding the upsurge of costs, as was the big price rise for imported oil. The pace of inflation has speeded up further: in January the consumer prices were 14 % higher than twelve months earlier.

That the real gross national product still rose slightly in the

fourth quarter of 1979 was chiefly due to the continuing fairly fast expansion of private consumption which is all the more remarkable as the disposable real incomes of private households probably declined slightly at the time. The trend of the savings ratio thus plays a key role in an analysis of last year's cyclical trend. Its increase early in 1979 could at first be interpreted as a typical precautionary response to deteriorating economic prospects. The reduced automobile purchases later were connected with temporary gasoline supply difficulties. But the sharp fall of the savings ratio in the second half of 1979 came as a surprise; many consumers were evidently reluctant to adjust consumption already in the short term to declining disposable real incomes but curtailed their savings instead. At the moment it is hardly yet possible to decide what role increased inflationary expectations played in this connection.

The corporate investment activity probably reached its climax in the third quarter of last year. Inquiries suggest that capital expenditure is still rising strongly but adjusted for price changes the

third-quarter level was evidently no longer fully maintained in the fourth quarter. Measured by the order receipts of the US equipment producers the demand for capital goods was, seasonally adjusted, in the second half of 1979 markedly lower than in the first half, but the decline has not gathered force during recent months. It was probably chiefly because of the still relatively favourable profit trend that falling capacity utilization rates and deteriorating cyclical expectations have not had a more depressive influence on investment decisions. Inventory planning on the other hand has been a curb on production since the middle of 1979 already; the inventories have been reduced considerably.

Although foreign trade carries much less weight in the USA than it does in the other industrialized western countries, it clearly supported the cyclical trend last year, for the export volume increased rapidly in the second half and advanced by an estimated 15 % in the year 1979 as a whole. It probably benefited in special measure from the cyclical expansion of demand in the other industrialized countries but certainly also from the improvement of imports into the oil exporting countries. Besides, US products had become much more competitive in 1977 and 1978. While imports virtually stagnated throughout the year, the vigorous export surge was sufficient to absorb the burden imposed on the balance of trade by the acute worsening of the terms of trade. The current account was last year only slightly, if at all, in deficit.

The consumer prices rose in the 1979 average by a good 11 % and the producer prices for finished products by only little less. The labour unit costs of the private sector increased almost as much. This is surprising as the average gross hourly earnings advanced "only" by a good 8 %. The discrepancy is explained by the overproportional increase of the indirect wage components (e. g. employers' social security contributions) on the one hand and the decline of productivity throughout the year on the other; in the fourth quarter productivity per working hour was 2 % lower than a year earlier. Many explanations have been proposed for the levelling-off of productivity (which had been observed already previously), including the inadequacy of investments in preceding years, the structural shift towards service sectors with low productivity and the falling-off of skills as more people enter gainful employment. One of the major explanations may be however that with the existing possibilities for passing on rising costs and given the moderate wage policy it was possible for firms to earn satisfactory profits without significant rationalization efforts.

Only since October has the monetary policy been following a consistent stabilization course. The restrictive influences resulting therefrom are only gradually becoming effective. Nevertheless recessive tendencies may be expected to show already in the short term. Crucial is in this respect that consumers are less and less likely to increase their purchases. Owing to worsening business and employment prospects precautionary saving will probably gain again in importance. As real incomes decline private consumption will therefore fall off substantially. At the same time a lasting decline of residential building may be expected. Even though there are no signs yet of a corresponding trend in the investments in fixed assets by industry, the investment plans give at any rate no indication of a further real increase in the course of this year. The prospects for the public demand for goods and services are, to go by the budget plans, not significantly more favourable.

Cyclical inventory adjustments will certainly support the recessionary tendencies. So far however even the downturn phase has brought no excessive inventory

accumulations as this process started in the second half of 1979 already, so that future contractionary impulses from this side are likely to be kept in relatively narrow limits in regard to their intensity as well as their duration. There are thus still good prospects that the indicated recession – even if it proves the distinguishing feature of the demand and production trend over most of this year – will not be severe. The decline of the real gross national product may thus be limited to about 1 % in the 1980 average. Seeing that the inflationary expectations are still sustained by extraneous impulses, the price surge will probably subside only gradually; the consumer prices will on an annual average again rise more sharply than in the preceding year. The scope for economic measures will therefore still be narrowly circumscribed by stability considerations. This is one of the major reasons why the recession is unlikely to be superseded soon by a cyclical recovery.

*Compiled by the Department
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of HWWA-Institut für
Wirtschaftsforschung-Hamburg.*

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

Index and commodity group	1979				1980		
	February	May	August	November	February	Feb. 29	March 14
HWWA-Index* (1952-1956=100) . . .	341.8	367.5	408.0	438.7	512.6	514.7	502.9
Foodstuffs	244.2	255.2	288.6	309.0	327.4	325.2	305.9
Raw materials other than foodstuffs . .	388.8	421.6	465.6	501.3	602.0	606.0	597.9
Fuels	585.4	653.8	751.8	831.2	1036.3	1048.8	1053.4
Raw materials for consumer goods . .	213.8	229.6	240.2	244.3	273.9	274.3	267.1
Raw materials for capital goods	309.9	318.4	330.8	344.0	387.9	385.9	364.3
Reuter's Index (18. 9. 1931 = 100) . . .	1532.1	1569.9	1563.2	1692.7	1808.9	1785.7	1719.7
Moody's Index (31. 12. 1931 = 100) . .	1038.1	1061.7	1073.8	1152.7	1433.0	1410.8	1244.4

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