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USA: First Signs of Economic Revival

Following definite successes in checking inflation and the backing-down from tight monetary policies last summer the first indications of a turning-point in the demand and production trend in the USA have led to a sharp improvement in the overall economic climate. This has been supported in particular by the increase in new orders and in industrial production at the start of the year. This development would appear to reflect a marked change in stockpiling behaviour. In addition, there was another substantial increase in the number of building projects started. This is all the more surprising since the fall in interest rates already came to a standstill last autumn at a relatively high level.

During the final months of 1982 the influence of considerable stock reductions had allowed recessionary forces to regain the upper hand. GNP fell in real terms and its annual average was 1.8 % down on the figure for 1981. Final demand as a whole, however, increased substantially, although exports fell strongly. Particularly private consumption revealed a considerable increase at the end of last year. The development of incomes was checked via the drop in employment and the levelling-off of wage increases. The result was an only marginal increase in disposable real income despite successes in keeping down prices. It would, however, seem that reduced interest rates together with improved discount terms and favourable credit packages for car-buying have stimulated the propensity to consume. On the other hand, the propensity to invest remained weak until the end of 1982 in the face of repeatedly disappointed sales expectations, subdued company profits and high real interest rates. Investments in industrial fixed assets consistently fell during the whole year.

Price and Wage Increases Levelling off

The upward movement in prices slowed down considerably during the course of 1982. Whereas at the end of 1981 consumer prices were 9 % up on the corresponding level for the previous year, this rate of price increase fell to a figure of just under 4 % by the end of 1982. The success of stabilisation efforts was also reflected in the development of wages. The increase in

gross hourly earnings was reduced, compared to the previous year, by almost three percentage points to 5.5 %. There was an even clearer levelling-off of wage costs per unit of output as the number of employed declined faster than output and thus productivity rose markedly during the second half of 1982.

Deterioration on Current Account

The dollar grew stronger against most other currencies up until November last year. This more than offset the favourable development of costs in the USA and the competitiveness of American suppliers continued to weaken. Exports have been on the decrease now for two years and in terms of volume the 1982 level was 11 % down on that recorded in the previous year. At the same time, imports fell by 4 to 5 %, primarily as a result of the considerable reduction in oil imports. The balance of trade deficit thus recorded a marked increase during the course of the year. At US \$ 31 billion (f.a.s. figures) it was US \$ 4 billion up on 1981, and this despite the fact that the deficit towards the OPEC countries had been substantially reduced. During the second half of the year the balance on current account also moved into deficit.

Relaxation of Monetary Policy

The central bank departed from its tight monetary course last summer. The growth of the money supply M1 has since considerably overshoot the range announced. Due to the influence of institutional changes on M1, which are difficult to quantify, the central bank is at present paying more attention to more broadly defined money supply aggregates; M2 and M3 have only slightly overstepped their 1982 target corridor. In formulating the new monetary growth targets the central bank was clearly attempting to avoid the risk of braking economic growth and due to the uncertainty in the monetary field raised the target corridor, particularly for M1.

The tax increases during the summer of 1982 could not solve the budgetary problems. Following a deficit of US \$ 111 billion in the fiscal year 1981/1982, the government estimates the deficit for the current year at

ECONOMIC TRENDS

about US \$ 200 billion. The budget presented for the fiscal year 1983/1984, the year in which according to the original economic programme the budget was to be in balance again for the first time, envisages a deficit hardly any smaller than that of the preceding year. Medium-term fiscal plans also expect a structural deficit for the coming years. Nevertheless, defence spending is to be substantially increased whereas most of the other expenditures are to be reduced in real terms.

Outlook: Conflicting Influences

Despite the signs of a changing trend in the USA the overall conditions for economic policy are still characterised by conflicting influences. Even after the easing-up of monetary restrictions, real interest rates, particularly for long-term lending, are still very high. The most important reason for this is probably the lack of confidence in a speedy solution to the budgetary problems. If nevertheless a revival of demand and production is in the offing, which is not merely restricted to the automatic running down of stock-cyclical impulses, this is due to an interplay of a number of factors. On the one hand, the drop in nominal interest rates would already seem to provide stimuli for purchasing and investment decisions that have so far been postponed. On the other, the falling prices of oil and towards the middle of the year the forthcoming tax reliefs will lead to an increase in disposable real income.

Marked Expansion of Demand

Under these circumstances private consumption can be expected to increase further at a moderate pace. In addition, there will be a faster increase in construction activities. Furthermore, the budgetary estimates indicate that the public demand for goods and services will still grow. On the other hand, the decline in company

investments will probably continue for the time being, although at a slower pace. Finally, due to the deterioration in the competitiveness of American suppliers the gradual recovery of demand in other industrialised countries is only likely to very slightly increase imports from the USA. For the same reason, there will be a substantial increase in American imports. On the whole, demand and production will expand markedly this year. The speed of this expansion, however, will be more restrained than in earlier recovery phases due to the still effective retardative influences. In view of an only slight overhang, GNP in real terms will at most be 2% up on the previous year's level. Employment is expected to increase again and the rise in unemployment will taper off. The rise in prices during this economic phase – influenced among other things by the falling energy prices – will stay weak; the increase in consumer prices will probably figure at an annual average of 4%.

The revival of economic activity during the course of this year would appear to be determined to a large extent by cyclical factors; this applies above all to stockpiling behaviour. Whether this will lead to a lasting upswing with a considerable increase in capacity utilization and employment, is still not clear. On the one hand, the numerous institutional changes in the banking system have made it difficult to assess the monetary framework. Above all, however, due to the structural budgetary deficits the uncertainty concerning future fiscal policy weighs heavily on expectations regarding the conditions for economic growth, as shown by the high real interest rates. The supply orientation of economic policy must still face up to its main test.

Compiled by the Department of World Business Trends of the HWWA-Institut für Wirtschaftsforschung-Hamburg.

HWWA Index of World Market Prices of Raw Materials¹
(1975=100)

Raw Materials and Groups of Materials	1982				1983			
	AA ²	October	November	December	January	February	Feb. 25	March 11
Total index	228.6	224.3	224.6	225.0	225.2	225.8	226.1	225.9
Total, excl. energy raw materials	117.9	110.6	110.6	111.8	113.1	115.3	116.0	115.4
Food, tropical beverages	106.1	99.1	102.2	103.4	104.0	106.0	105.4	104.0
Industrial raw materials	126.4	119.3	117.1	118.2	120.0	122.4	124.0	124.1
Agricultural raw materials	127.1	115.3	113.3	114.3	114.5	115.4	117.0	118.5
Non-ferrous metals	134.9	131.4	128.5	128.7	135.3	141.2	144.0	141.7
Energy raw materials	293.4	290.7	291.1	291.1	290.7	290.3	290.4	290.5

¹ On dollar basis. - ² Annual Average. For the method of computation of the HWWA Index cf. INTERECONOMICS No. 5, 1980, p. 261 ff.