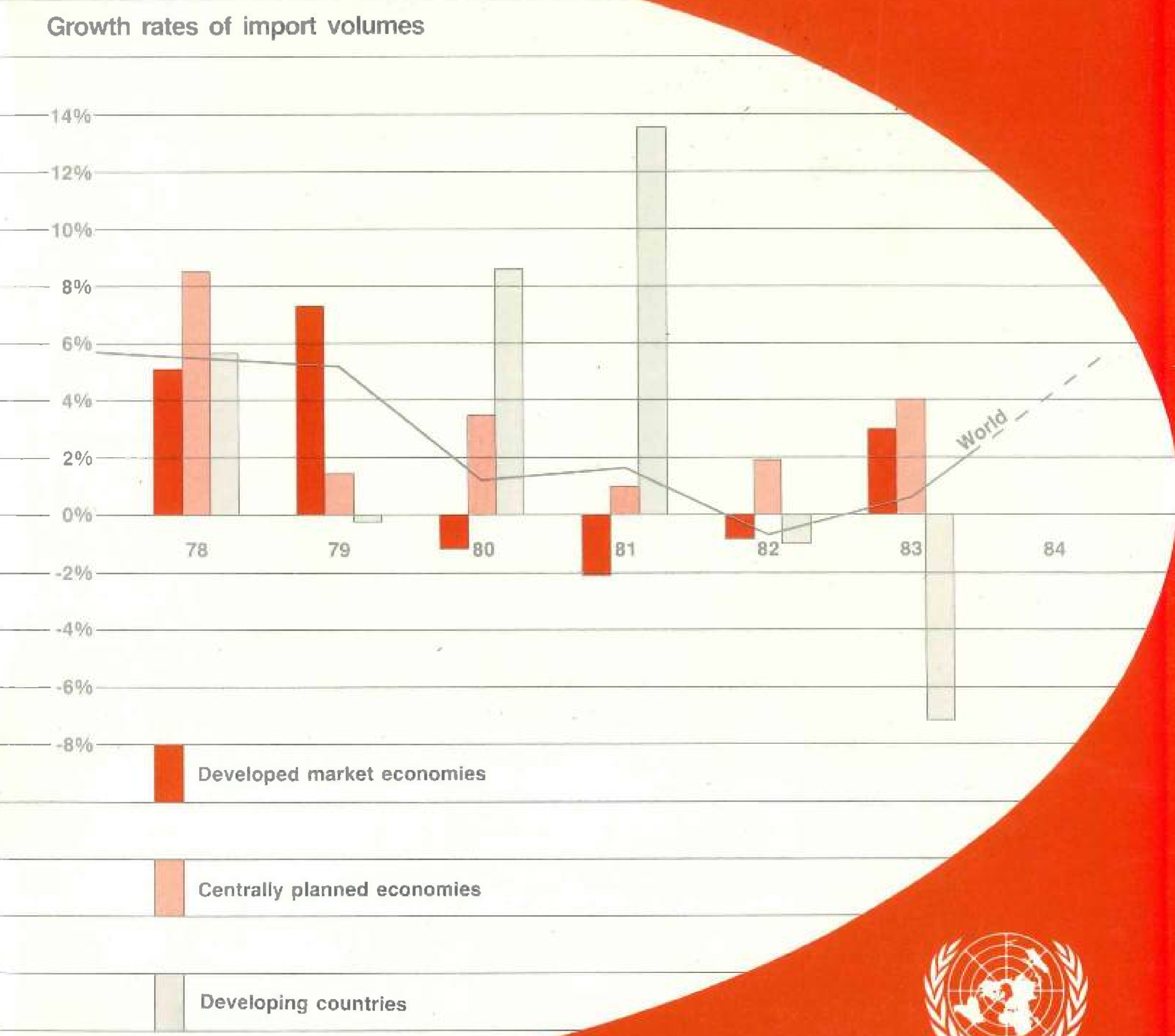
World Economic Survey 1984

Current Trends and Policies in the World Economy



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WORLD ECONOMIC SURVEY 1984

Current Trends and Policies in the World Economy

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PREFACE

After the most protracted global economic recession since the 1930s, the prospects for sustained and broad-based growth are still not satisfactory. This unresolved issue is the focus of the *World Economic Survey 1984*.

A major development in 1983 was the recovery in North America. The recovery of the developed market economies as a whole is expected to become more widespread this year, but further strengthening beyond 1984 is uncertain. Much will depend on the fiscal policy stances of the major countries. High interest rates are a major issue, of concern to the entire international community.

The performance of the centrally planned economies improved in 1983, yet remained on the whole well below post-war trends.

The developing countries as a group registered no economic growth in 1983, and the prospects for an early resumption of rapid growth are dim. The difficult international reserve position of low-income countries and payments problems of highly indebted countries are key concerns. The decline in investment that has occurred since 1981 in many countries, partly as a consequence of severe import constraints, is slowing down the process of structural adjustment. It is notable that several Asian countries, facing less severe payments pressures, were able to sustain their restructuring efforts and achieve relatively strong economic growth. The limited but successful experience with supply-oriented structural adjustment programmes deserves appropriate recognition at the policy level, nationally and internationally.

The situation in sub-Saharan Africa is most serious. These countries have experienced no economic growth so far this decade. Drought conditions were widespread in 1983 and critical food shortages are being experienced in many counties.

Trade among developing countries appears to have contracted substantially in 1983, an indication of the interregional impact of setbacks in the formerly rapidly growing developing regions.

World trade itself failed to pick up in 1983, which was atypical of any recovery phase in past decades. The protectionist trend of recent years accelerated last year, and there are fears that trade restrictions could become even more widespread in 1984, rather than abate with the current recovery. The strength of world trade will also depend on the adequacy of international liquidity.

The current situation thus gives rise to a number of specific policy measures which are summarized in the concluding section of chapter I. At this juncture, the importance of greater international economic co-operation cannot be over-emphasized. The prolonged world recession has left a difficult legacy. In many developing countries, per capita income at mid-decade will be below its level at the start of the decade. Co-operation in key policy areas, such as financial flows, debt and trade, is most urgent for an early reactivation of development.

The *Survey* was prepared in the General Analysis and Policies Division of the Department of International Economic and Social Affairs, on the basis of information available as of 31 March 1984. A supplement to the *Survey*, which includes a study on economic co-operation among developing countries, will be published later this year.

It is hoped that in addition to supporting the work of the Economic and Social Council and other United Nations bodies, the *World Economic Survey 1984* will be of interest to Governments and the general public.

Shuaib U. Yolah
Under-Secretary-General for
International Economic and Social
Affairs

CONTENTS

Chapter *Page*

I. WORLD ECONOMIC CONDITIONS: RECENT TRENDS AND PROSPECTS..... 1

1983-1984: Uneven recovery in world output.................................... 1
A weak recovery in developing countries.. 4
The short-term outlook: a modest expansion in 1984-1985................. 4
The impact of external economic developments in the early 1980s........ 4
Diverse adjustment experience among developing countries................ 8
The debt problem and the consequences of continued high interest rates... 11
The special difficulties of sub-Saharan countries............................ 15
Foundations for a sustained recovery in developed market economies.. 20
Broadening recovery and reactivating development: some requirements for international co-operation............................ 23
Policy conclusions: a recapitulation... 26
Notes... 29

II. INTERNATIONAL TRADE AND PAYMENTS.. 30

An overview of the main issues.. 30
The evolution of international trade... 33
Modest upswing in world trade volume....................................... 33
Protectionism threatens to slow recovery in world trade................... 37
Partial recovery in primary commodity prices.............................. 40
Effects of international price changes on the terms of trade.............. 42
International payments... 44
Major current account developments... 44
Intense current account adjustment by developing countries.............. 46
Capital flows to developing countries recede sharply....................... 46
Large shifts in current accounts among the developed market economies.. 52
Exchange rate instability among major currencies.......................... 54
Further improvement in the external payments position of the centrally planned economies... 57
Notes... 60

III. GROWTH IN THE WORLD ECONOMY AND CURRENT POLICY STANCES.. 63

Overview.. 63
Widespread stagnation in developing countries................................ 66
Uneven recovery in developed market economies............................. 74
A modest acceleration in some of the centrally planned economies......... 87
Notes...87

CONTENTS (continued)

Page

Annex. SELECTED SECTORAL TRENDS 98

The food crisis in Africa in the context of global production and trade 98

The situation in world energy markets 104

TABLES

Table

I-1. Growth of world output and trade, 1978-1985 1

I-2. Developing countries: average annual rate of growth in GDP, 1976-1985 4

I-3. Developing countries: growth trends and indicators of the external environment, 1978-1983 6

I-4. Selected economic trends in certain energy-importing developing countries of Asia, 1976-1983 9

I-5. Measures of the interest cost on the external debt of capital-importing developing countries, 1979-1983 13

I-6. Developing countries in sub-Saharan Africa: annual rates of increase in key variables, 1970-1983 16

I-7. Developing countries in sub-Saharan Africa: international trade reserves, 1978-1983 18

I-8. Annual growth of real GDP and volume of trade: 1960-1983 28

II-1. World trade: annual rates of change in volume and prices, 1976-1985 .. 34

II-2. Rates of change in the prices of internationally traded commodities, 1981-1985 40

II-3. World balance of payments on current account, by country groups, 1980-1984 45

II-4. Financing the current account deficit of capital-importing developing countries, 1978-1983 47

II-5. Net flow of IMF lending to the capital-importing developing countries, 1978-1983 50

II-6. Developed market economies: balance of payments on current account, 1980-1984 53

CONTENTS (continued)

Table		Page
II-7.	Selected developed market economies: exchange rate movements, 1981-1983	55
II-8.	Major developed market economies: net short-term and long-term capital flows, 1989-1983	56
II-9.	Centrally planned economies: trade balances, 1981-1983	58
III-1.	World: annual growth rates of output volume, by country groups and major sectors, 1976-1985	64
III-2.	Developing countries: rates of growth of GDP, 1979-1983	67
III-3.	Developing countries: annual rates of change in the consumer price index, 1976-1983	73
III-4.	Developed market economies: annual rates of growth of real gross national product, 1976-1985	75
III-5.	Developed market economies: rates of change of GNP deflator and consumer prices, 1976-1984	78
III-6.	Selected developed market economies: unemployment rates, 1976-1984	79
III-7.	Major developed market economies: real rate of change in broad money supply, 1979-1983	80
III-8.	Major developed market economies: real interest rates, 1975-1983	82
III-9.	Selected developed market economies: the unadjusted general government budget surplus or deficit as a percentage of nominal GNP, 1978-1983	83
III-10.	Centrally planned economies: basic economic growth indicators, 1976-1984	88
A-1.	Indicators of net world food production, 1971-1983	99
A-2.	World stocks and trade in cereals, 1979-1984	101
A-3.	Trade volume in food products, 1971-1982 indices and trends	105
A-4.	World oil production and consumption, 1980-1983	107

EXPLANATORY NOTES

The following symbols have been used in the tables throughout the report:

Three dots (...) indicate that data are not available or are not separately reported.

A dash (-) indicates that the amount is nil or negligible.

A blank in a table indicates that the item is not applicable.

A minus sign (-) indicates a deficit or decrease, except as indicated.

A full stop (.) is used to indicate decimals.

A slash (/) indicates a crop year or financial year, e.g. 1970/71.

Use of a hyphen (-) between dates representing years, for example, 1971-1973, signifies the full period involved, including the beginning and end years.

Reference to "tons" indicates metric tons and to "dollars" ($) United States dollars, unless otherwise stated.

Annual rates of growth or change, unless otherwise stated, refer to annual compound rates. In most cases, the growth rates forecast for 1984 and 1985 are rounded to the nearest half of a percentage point.

Details and percentages in tables do not necessarily add to totals, because of rounding.

The following acronyms and abbreviations have been used:

CMEA	Council for Mutual Economic Assistance
DAC	Development Assistance Committee of the Organisation for Economic Co-operation and Development
EEC	European Economic Community
FAO	Food and Agriculture Organization of the United Nations
GATT	General Agreement on Tariffs and Trade
GDP	Gross domestic product
GNP	Gross national product
IDA	International Development Association
IMF	International Monetary Fund
LINK	International Research Group of Econometric Model Builders

NMP	Net material product
ODA	Official development assistance
OECD	Organisation for Economic Co-operation and Development
OPEC	Organization of Petroleum Exporting Countries
SDR	Special drawing rights

The designations employed and the presentation of the material in this publication do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations concerning the legal status of any country, territory, city or area or of its authorities, or concerning the delimitation of its frontiers or boundaries.

The term ''country'' as used in the text of this report also refers, as appropriate, to territories or areas.

For analytical purposes, the following country classification has been used:

Centrally planned economies:	China, Eastern Europe and Union of Soviet Socialist Republics
Developed market economies:	North America, southern and western Europe (excluding Cyprus, Malta and Yugoslavia), Australia, Japan, New Zealand and South Africa
Developing countries:	Latin America and the Caribbean area, Africa (other than South Africa), Asia (excluding Japan) and Cyprus, Malta and Yugoslavia

For particular analyses, developing countries have been subdivided into the following groups:

Capital surplus countries:	Brunei, Islamic Republic of Iran, Iraq, Kuwait, Libyan Arab Jamahiriya, Qatar, Saudi Arabia and United Arab Emirates

Deficit countries (or capital-importing countries), subdivided into the following two subgroups:

Other net energy exporters:	Algeria, Angola, Bahrain, Bolivia, Cameroon, Congo, Ecuador, Egypt, Gabon, Indonesia, Malaysia, Mexico, Nigeria, Oman, Peru, Syrian Arab Republic, Trinidad and Tobago, Tunisia and Venezuela (in the text these countries are identified as the deficit energy exporters)
Net energy importers:	All other developing countries

The designations of country groups in the text and the tables are intended solely for statistical or analytical convenience and do not necessarily express a judgement about the stage reached by a particular country or area in the development process.

Chapter I

WORLD ECONOMIC CONDITIONS: RECENT TRENDS AND PROSPECTS

1983-1984: Uneven recovery in world output

While a reversal of recessionary trends began in 1983, recovery has not become general. There are contradictory influences at work in the world economy making for a diversity of experience among regions. Some parts of the world, especially North America and some developing countries of South and East Asia, are now experiencing quite a rapid pace of advance in income and output. Economic growth in the centrally planned economies has also accelerated, though its rate generally remains at a lower level than in past years. But most developing countries are beset by problems which seriously hinder their prospects for vigorous reactivation of development; and recovery in Western Europe has so far been weak. World output appears to have expanded at a rate of about 2 per cent in 1983, and may accelerate to between 3.5 and 4 per cent in 1984 and 1985 (see table I-1). While these rates are markedly higher than those attained in the first three years of the decade, they are modest for a period of economic recovery.

Table I-1. Growth of world output and trade, 1978-1985

(Percentage)

	1978	1979	1980	1981	1982	1983[a]	1984[b]	1985[b]
Gross domestic product								
World	4.5	3.4	2.0	1.7	0.8	2.2	4	3.5
Developing countries	4.1	5.0	3.2	1.6	0.5	0.0	3.5	3.5
Developed market economies	4.0	3.1	1.2	1.5	-0.2	2.0	4	3
Centrally planned economies[c]	6.2	3.1	3.7	2.4	3.7	4.3	4	4
International trade								
World imports	5.5	5.2	1.2	1.6	-0.7	0.6	4	5

Source: Department of International Economic and Social Affairs of the United Nations Secretariat.

[a] Preliminary estimates.
[b] Forecasts.
[c] Net material product.

The differences in performance among regions derive in no small part from the effects on each of the policies and trends at work in the others; the present effects of interdependence combine less to induce a shared and concurrent improvement than to generate considerable divergences in performance. While the upswing in North America has been exerting a decidedly expansionary influence on the exports of other countries, the uncharacteristically high interest rates prevailing in the United States have aggravated the debt-servicing burden of indebted developing countries and limited the room for pursuit of less restrictive policies in Western Europe. The severe deflation of economic activity in the indebted developing countries, implemented to accommodate debt service payments in their external accounts, has diminished the threat to the commercial banking system of developed countries, but this has been accomplished at the cost of greatly reduced imports. As numerous other developing countries have also experienced serious payments difficulties stemming from weak demand for oil and other primary commodities, and aggravated in some areas by drought, these countries generally have exerted a strong deflationary influence on world trade. This has again contributed to the limited recovery in Western Europe, a fact which goes far to explain the lack of a robust revival in primary commodity prices.

The situation in much of the developing world remains deeply troubling. Many countries are emerging from the recession with a legacy of difficulties which will not be dissipated by recovery elsewhere. The aftermath of a pervasive drought has left many sub-Saharan African countries with a very precarious payments position. Debt-service ratios, particularly in Latin America, are likely to remain unusually high even after recovery in industrial countries, and debtor countries will still be compelled to retrench drastically. While there is recognition of the need for adjustment of productive structures to allow higher levels of domestic activity that would be consistent with lower current account deficits, neither internal nor external conditions are conducive to the mobilization of sufficient resources for the needed investment. Apart from a number of countries, mostly in South and East Asia, per capita incomes have fallen for several consecutive years, and investment expenditures are generally well below the levels realized in the late 1970s. External loan financing from private sources has slowed down to a trickle, and the very stringent international liquidity situation restricts capital goods imports.

Among the developed market economies, a normal cyclical upswing in the United States and continued growth in Japan are being accompanied by a recovery in Western Europe that is so far limited to some countries and is cyclicaly weak. While an expansionary fiscal policy has aided recovery in the United States, a number of Western European countries have chosen to pursue relatively restrictive fiscal policies in order to reduce structural budget deficits and the overall size of the government sector. Lack of dynamism in demand has also restrained the expansion of output in Western Europe. Intra-European trade, which comprises a large percentage of total exports, has been adversely affected by weak aggregate demand; and exports to developing countries - more than half of total exports to countries outside the region - have contracted in absolute terms.

In these countries generally, a significant decline of inflation and a slow down in wage increases have improved business confidence, and rates of investment have recently been picking up. While the momentum of investment is likely to be maintained in the near future, the strength and duration of the cyclical upswing remain an open question. There are concerns that it may be vitiated by the persistence of structural budget deficits and high interest rates in the United States or a prolonged period of restrictive policies in Western Europe. Were the next downturn to come early or to approach the severity of the last recession, a number of developing countries could face a renewed debt-servicing crisis.

Among the centrally planned economies, the Asian countries have continued their strong recent performance, the Soviet Union has maintained its more modest pace of growth and the Eastern European countries have recovered from the very sluggish level of activity in 1982. Several of these latter countries had borrowed substantially in the 1970s and faced increased debt service payments and a drying up of new credit in recent years. Through vigorous export promotion and through import restraint, they have sought to generate growing current account surpluses in order to work down their external debt.

It is a mark of the weak and uneven character of world economic recovery in 1983 that world trade failed to pick up. Indeed, for the first time in decades, an increase in world output, albeit very modest, was not accompanied by a proportionately larger gain in imports. World imports, in fact, virtually stagnated. This largely reflected the pattern of recovery. Strong rates of growth in imports were registered only in North America, a few developing countries of Asia, and some centrally planned economies, notably China and the Soviet Union. Real imports fell in Japan and remained stagnant in Western Europe. In most developing countries, there was a sharp decline in import volumes.

The failure of world trade to pick up strongly during the current recovery has dampened the pace of economic activity in most parts of the world economy. Expansionary influences at work in individual countries act cumulatively on each other through international trade; and the same is true of deflationary influences. In the current situation, both expansionary and deflationary influences have been at work, though until mid-1983 at least, the latter appear to have been more dominant. For 1984, some improvement in trade is expected and world imports may rise roughly in line with world output.

The functioning of both the international trading and the international financial systems has been further impaired by events of the recent past. Protectionist measures have multiplied and the transfer of capital to developing countries has greatly diminished. If a reactivation of development is to take place over the next few years, it is not only immediate measures to broaden and strengthen recovery that are needed. Reinvigoration and improvement of the international trading and financial system are equally essential.

A weak recovery in developing countries

The short-term outlook: a modest expansion in 1984-1985

After several years of falling rates of economic growth in most developing countries, and a virtual stagnation in 1983, a reversal of trends is gradually emerging. As can be seen in table I-2, the annual rate of growth of GDP is likely to increase to 3.5 per cent

Table I-2. Developing countries: average annual rate of growth in GDP, 1976-1985

(Percentage)

	1976-1979	1980-1983	1984-1985
Africa	5.0	0.6	2.5
Latin America	5.2	0.4	3.0
Mediterranean	5.5	2.0	3.5
South and East Asia	5.9	5.3	5.5
West Asia	5.7	-1.9	4.0
Developing countries	5.5	1.3	3.5

Source: Department of International Economic and Social Affairs of the United Nations Secretariat.

in developing countries as a whole in 1984-1985. This rate, however, is well below the rate achieved in the second half of the 1970s. There is also a significant diversity of situations among regions. While countries in South and East Asia are likely to achieve rates of economic growth considerably higher than the growth of population, for a very large number of developing countries in other regions per capita GDP will remain stagnant in 1984-1985. These trends are in no small part a consequence of recent experience.

The impact of external economic developments in the early 1980s

The downward shift in the economic performance of developing countries in the early 1980s was widespread. A great many developing countries proved very vulnerable to the recession and have emerged with difficulties which are crippling their present and prospective performance. Generally, these countries entered the recession already weakened by serious structural problems or with an external debt whose level and structure left them exposed to sudden adverse changes in the availability of foreign exchange and to increases in interest rates. These weaknesses became critical when the recession turned out to be an unusually protracted recession which was, moreover, accompanied by uncharacteristically high interest rates.

Export earnings fell sharply during the recession, and they have since failed to recover fully. In fact, in many countries export earnings are still below their 1980 levels. Increasing protection in the main industrial countries has to some extent aggravated the cyclical decline in demand. Although the trend towards protectionism predates the recession, it received an important impetus during the prolonged economic downswing of the early 1980s. As regards the energy-exporting countries, a sharp and sustained declined in energy consumption in the developed market economies, partly the consequence of the recession and partly in response to previous price increases, adversely affected their export earnings.

The terms of trade of the energy importers had been deteriorating in the years immediately preceding the recession owing to rapid increases in the prices of petroleum and manufactures. With the advent of recession, these prices stabilized but the prices of primary commodities declined very sharply. The deterioration in terms of trade consequently continued until prices of primary commodities began to improve in mid-1983. As regards the energy exporters, their terms of trade improved markedly up to 1981, but have worsened substantially since then.

For the more heavily-indebted countries, the consequence of the sudden shift to uncharacteristically high interest rates that began in 1979, has been a dramatic rise in the share of export earnings that must be devoted to the payment of interest. Although nominal interest rates in the major capital markets began to recede in 1982 from the high levels they reached in 1980-1981, they ceased to decline in 1983 and have even begun to inch up recently.

Another adverse external factor has been the behaviour of capital flows. Since the early 1970s, countries with access to private international capital markets had relied on bank loans for financing long-term investments as well as for balance-of-payments financing. But since the Mexican debt-servicing crisis erupted in mid-1982, net private lending to developing countries has slowed to a trickle (see table I-3.) Most developing country borrowers have been affected, particularly those heavily indebted to the private banks. Indeed, it was when the banks became unwilling to continue to extend credit that an unprecedented number of borrowing countries fell into arrears and initiated negotiations to restructure their debt.

The combination of a series of disturbances tending to enlarge current account deficits with a drastic curtailment of available payments finance left countries with no option but to attempt to reduce their deficits as rapidly as possible. Given the severity and duration of balance-of-payments pressures, international reserves proved to be insufficient to prevent a major reduction in real imports. In most energy-importing countries, some measures to restrain imports have been in place since 1980, although their stringency has generally

Table I-3. Developing countries: growth trends and indicators of the external environment, 1978-1983

(Percentage)

	1978	1979	1980	1981	1982	1983[a]
Rate of growth of GDP						
Net energy importers	4.5	3.9	4.4	1.5	0.8	1.4
Deficit energy exporters	4.3	6.4	5.5	4.8	0.9	-0.7
Surplus countries	2.6	6.5	-4.1	-3.5	-1.3	-3.9
Rate of change in the volume of imports						
Net energy importers	7.8	5.2	2.8	6.1	-3.1	0.5
Deficit energy exporters	4.6	-10.4	18.7	23.4	-6.4	-19.0
Surplus countries	0.8	-3.3	15.5	23.5	11.9	-11.0
Rate of change in the terms of trade						
Net energy importers	-4.9	-3.0	-8.7	-3.9	-7.2	5
Deficit energy exporters	-8.3	15.8	30.3	9.6	-1.6	-3.5
Surplus countries	-9.7	24.7	47.7	14.7	0.2	-8
Interest payments as a share of foreign exchange earnings						
Net energy importers	8.8	10.9	12.4	16.0	19.4	18.0
Deficit energy exporters	8.1	8.4	8.4	11.4	15.5	15.0
Effective net borrowing from commercial banks (billion dollars)[b]						
Net energy importers	19.1	26.8	26.6	20.1	11.0	4.0
Deficit energy exporters	15.6	17.9	17.5	19.0	10.0	6.0

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on national sources, regional commissions, the International Monetary Fund, the World Bank and the Bank for International Settlements.

[a] Preliminary estimates.
[b] Change in debt outstanding to foreign banks, including short-term debt, based on quarterly banking data of the Bank of International Settlements.

increased as time passed. Balance-of-payments difficulties are a more recent phenomenon in the deficit energy-exporting countries, and policies to reduce current account deficits began to be widely adopted in 1982. In the capital surplus countries, it was not until 1983 that they began to run substantial and uncharacteristic current account deficits. This led them to make downward revisions in public expenditure programmes, and to effect some reduction in the volume of imports.

In a number of countries, the reductions in imports have been dramatic and without precedent in recent history. The decline of import volumes in the period 1981-1983 was about a sixth in the energy-importing countries of Africa and about a third in the energy-importing countries of Latin America. Some least developed countries and other developing countries such as Argentina, Brazil, Costa Rica, Chile, Ghana, Ivory Coast, Kenya, Uruguay, Zaire and Zambia experienced a drop in their import volumes ranging from a third to about a half in the same period. The decline in imports in the energy exporters started in 1982. In the period 1982-1983, the drop in import volumes was of the order of 50 per cent or above in Mexico, Nigeria and Venezuela and close to 25 per cent in countries such as Cameroon, Ecuador and Peru. In the reductions, imports from all sources were affected, including those from other developing countries.

The contraction in imports of the developing world was achieved by a variety of means. In many countries, policies geared to dampen aggregate demand were adopted, usually accompanied by significant devaluations. But as export revenues remained weak and international reserves continued to fall, a large number of countries introduced more direct forms of import controls. In many of these countries, this marked a departure from past trends of liberalizing trade policy as part of new policy thrusts toward raising domestic productivity through increased competition and more appropriate prices.[1] However, given the substantial reduction in the capacity to import of many of these countries, import controls were unavoidable: an adjustment through the exclusive use of macro-economic policies would have implied a fall in real incomes far larger than many of these countries were already experiencing and would have required even more personal sacrifices than the population had already been asked to bear.

In fact, the social cost in a number of developing countries of the sharp adjustment measures taken has already been very onerous.[2] Per capita output has fallen in each of the last four years in almost one out of every four developing countries. Fiscal austerity has led to the curtailment of assistance to lower-income groups in the form of consumer subsidies, and levels of open unemployment have risen to unusually high levels.[3] The economically weaker portions of the population have been experiencing particular hardship.[4]

Development prospects have been set back. The combined effect of import scarcity and demand restraint have fallen with singular force on investment. In 1983, investment in many countries of Latin America and sub-Saharan Africa was below its level of the late 1970s. In many countries, existing installed capacity has deteriorated and innumerable enterprises have gone out of business. Moreover, the investment outlook is limited since deflationary pressures are expected to remain strong.

Adjustment efforts have also resulted in some countries in a worsening in inflation. The destabilizing shocks of large devaluations and the sudden reduction in the availability of imports have had particularly adverse consequences for domestic price levels. In addition, the recession has led to a fall in tax receipts and to large budget deficits, which have intensified inflationary pressures from the demand side. Although considerable unemployment, idle capacity and slack demand already exist in such countries, the need to combat inflation will continue to restrict the options of policy-makers. The serious difficulties involved in reducing budget deficits that are much larger as a percentage of GDP than in the developed market economies imply that some countries will have to maintain stringent measures for quite some time.

The economic adversity presently faced by many developing countries has not only depressed investment, and with it prospects for growth, but has also re-focused attention on the relationship between prevailing economic conditions and the social health of nations. Recent social conflicts have many sources, some of which run deep. But shrinking incomes, rising joblessness or sudden shortages - especially when occurring after a long period of profound social and economic change, as that of the 1960s and 1970s - have in places heightened already present tensions or rekindled old hostilities. In such an atmosphere, expressions of discontent may easily spill over into violence or clashes between different elements of society. The belief that the current difficulties are merely transitory can be sustained by credible, fair and efficient economic policies. Such a belief would act as a powerful barrier against the social protests becoming destructive with all their immediate and, in the long-term, unforeseeable economic and political consequences.

Diverse adjustment experience among developing countries

While a great many developing countries proved vulnerable to the worsening of the international economic environment that was associated with recession, there was nonetheless some diversity of experience. Countries in all regions which entered the recession with relatively a large external debt have generally experienced severe difficulties, and the structural problems of many countries in sub-Saharan Africa also placed them in very exposed positions. The situation of such countries is discussed in greater detail in the next two sections. However, in a small group of Asian countries - Burma, India, the Republic of Korea, Pakistan, Singapore, Sri Lanka and Thailand - the average annual growth of per capita GDP during the period 1980-1983 exceeded 2.5 per cent. This is not to say that these countries grew steadily throughout this period. Some experienced individual years of very low or significantly negative growth. Nevertheless, compared to the 1980-1983 average for the other energy-importing developing countries of 0.7 per cent per annum, these countries experienced relatively strong economic growth (see table I-4).

While there are several reasons of varying importance which appear to explain why these countries weathered the international recession with less strain, a common characteristic is that their balance of payments was put under less severe pressure than in other countries. This is largely accounted for by the particular nature of their external links, the changes in the structure of domestic output brought about by past policies, and the kinds of adjustment policies pursued since 1980.

In some of these countries - particularly the Republic of Korea, Singapore and, to a lesser extent, India - manufactures comprise a predominant share of exports, and export

Table I-4. Selected economic trends in certain energy-importing developing countries of Asia, 1976-1983

(Percentage)

	Burma	India	Pakistan	Republic of Korea	Singapore	Sri Lanka	Thailand	All other energy importers
Average annual growth of GDP								
1976-1979	5.6	2.7	4.0	10.6	8.2	5.4	8.0	5.0
1980-1983	6.6	5.2	6.4	4.4	8.6	5.1	5.6	0.7
Average annual growth of agricultural output[a]								
1976-1983	5.2	3.3	3.6	3.3	-3.5	3.5	3.5	2.4
Average annual growth of primary energy production[b]								
1976-1982	8.4	6.2	8.7	2.1	-	5.6	25.0	3.7
Average annual growth of services exports,								
1976-79 to 1980-83[c]	23.0	19.2	21.6	15.9	24.5	38.9	29.1	12.8
Memorandum:								
Share of agriculture in GDP								
1979-1980	43	32	28	18	1	27	26	18
Ratio of services earnings to merchandise exports,								
1980-1983	17	60	115	29	43	50	34	45
Share of bank debt in total foreign debt,								
1982	22	10	13	66	...	33	54	68

Source: Department of International Social and Economic Affairs of the United Nations Secretariat, based in part on data of the International Monetary Fund and the Food and Agricultural Organization of the United Nations.

[a] Growth as measured by FAO production index (1974-76 = 100).
[b] Measured in tons of oil equivalent.
[c] Shipping, travel, overseas construction, workers' remittances and other non-merchandise exports (excluding interest and dividend income).

earnings from manufactures are less recession-sensitive than earnings from primary commodities. In addition, both Singapore and the Republic of Korea have sought to shift their industrial structures towards goods having more dynamic export prospects and greater domestic value added. Further, all the countries have been relatively successful in increasing foreign exchange earnings from the export of services (see table I-4). Most of the countries have supplied substantial amounts of skilled or semi-skilled labour to a number of oil-exporting countries. India and the Republic of Korea have also emphasized overseas engineering and construction services and, in addition, Singapore has concentrated on building upon its role as an international financial centre.

In contrast to other developing countries, capital flows to the these countries did not cease abruptly. Four of the countries (Burma, India, Pakistan and Sri Lanka) are relatively large recipients of unrequited official grant assistance in relation to their current account deficits. Moreover, the countries as a group have received substantial amounts of other official capital, including official development assistance (ODA) loans and non-concessional credits from the World Bank, the Asian Development Bank and other multilateral sources. In some countries, private capital inflows have also been large. During 1980-1982, net direct investment in Singapore exceeded that country's current account deficit by over a third. In addition, each of the countries has enjoyed a certain measure of access to international private capital markets, and these flows were not drastically curtailed.

It is true that the countries have maintained a generally cautious approach to external debt. Most of these countries had debt levels below the average of all other energy importers in 1982.[5] In addition, with few exceptions, the share of bank debt contracted at floating interest rates is much smaller in these countries than in the more heavily-indebted developing countries. Higher interest rates in international capital markets have accordingly affected these countries to a much smaller extent than other developing countries.

Success with longer-term policies of structural adjustment in the fields of agriculture and energy also contributed to the relatively good overall economic performance of these countries in the early 1980s. In those countries having substantial agricultural sectors, agricultural production has grown more rapidly since the mid-1970s than the average for the rest of the energy-importing developing world (see table I-4). Similarly, despite rapid increases in the consumption of energy, the degree of reliance on domestic energy supplies has remained the same or improved in most of the countries. For the other countries, as in many other parts of the energy-importing world, there apparently were no new, large-scale energy reserves to be discovered; and the limited opportunity for import substitution in energy made it necessary to place greater reliance on expanding export earnings for purchase of energy imports.

A further reason for the relative success of this group of Asian countries is that most adopted early adjustment measures. These policies consisted not only in fiscal and monetary restraint but they also included measures to effect adjustments in the structure of production, often through the use of public investment expenditures and changes in taxes, subsidies and administered prices.[6] These policies were supported by substantial amounts of IMF credit, a large proportion of which was provided as a medium-term basis from the Extended Fund Facility, and by structural adjustment lending from the World Bank. In particular, Burma, the Republic of Korea, and Thailand entered into stand-by arrangements with the IMF in the first half of 1981; while Sri Lanka in 1979, Pakistan in 1980 and India in 1981 obtained relatively large credit commitments from the Extended Fund Facility. Some of these countries subsequently returned to the Fund for additional stand-by arrangements. The Republic of Korea, Pakistan and Thailand also received structural adjustment loans from the World Bank. The credit provided by the IMF, in particular from the Extended Fund Facility, was specifically designed to support changes in the structure of the economy, as conditionality requirements were reinterpreted to include supply-side considerations.

In sum, the above-average economic performance of these countries can be attributed to the fact that they were less affected by the unfavourable external environment than other developing countries and to the early adoption of appropriate adjustment policies from both the supply and demand sides of the economy which were supported by substantial amounts of external financing. By contrast, for those countries currently caught in an adjustment process that entails working down an insupportable debt-servicing burden, the additional investments needed to accelerate structural adjustment seem currently out of reach; and in the low-income countries which have had to sustain a drop in personal consumption, particularly in sub-Saharan Africa, the possibilities of financing such investments out of increases in domestic saving are very slim indeed.

The debt problem and the consequences of continued high interest rates

The developing countries that had borrowed heavily in international capital markets during the 1970s and had therefore accumulated large external debts at floating rates of interest were among those most adversely affected by the recession. Now a large debt overhang and high interest rates are clouding their growth prospects.

During the 1970s, in spite of the rapid increase in the foreign indebtedness of the capital-importing developing countries, their debt-to-exports ratio did not change much, since exports rose at practically the same rate as foreign indebtedness (about 19 per cent per annum). This situation changed radically in the early 1980s. The relation between debt and exports, which stood at 1.36 in 1979, climbed to 1.60 in 1982 and further to 1.70 in 1983. There are two main reasons that explain this abrupt change. First, there was a marked slow-down in the growth of export earnings. While they grew substantially in 1980 and 1981, export earnings of the capital importing countries declined by about 6 per cent in 1982 and by more than 1 per cent in 1983. Secondly, borrowing countries expected this slow-down to be short-lived. Therefore, it was believed that cut-backs in ongoing investment programmes were unnecessary and that the temporary financing gap could be filled with further borrowing. In a few countries, one of the main objectives was also to maintain consumption at satisfactory levels. Thus, debt in many developing countries continued to increase at the pace of the preceding decade well into 1982. By the end of 1983, the total debt of the capital-importing countries stood at about $730 billion.

Debt increases were, of course, not homogeneous among countries since many developing countries had little access to commercial loans. A distinctive feature of the rise in debt was the growing importance of commercial debt at floating rates, most of which was contracted in dollars. In fact, the share of loans at floating rates in the total medium- and long-term debt of developing countries, which was about 20 per cent in 1975, climbed to more than 30 per cent in 1980 and stood at more than 35 per cent in 1983.

Dollar interest rates began a gradual increase in 1977; by 1981, when they reached their peak in most markets, they were more than twice the level of 1977. Dollar interest rates decreased during most of 1982, and from the last quarter of that year until early 1984 they remained virtually stable but still well above the levels of the late 1970s. In the early part of 1984, interest rates began to rise once again. Interest rates on developing country foreign debt, which rose with the jump in interest rates in the major capital markets 1984 they remained virtually stable but still well above the levels of the late 1970s. In the early part of 1984, interest rates began to rise once again. Interest rates on developing country foreign debt, which rose with the jump in interest rates in the major capital markets of the world in the beginning of the decade, began to come down rather slowly and with a lag, as may be seen in table I-5. Indeed, the effective interest rate paid by developing countries in 1982 was not below that of 1981, and the reduction in 1983 was only modest.

This disparity arose for two main reasons. First, as it became clearer that a number of developing countries had fallen into precarious debt-servicing situations, private bank lenders increased the margins or "spreads" above market interest rates, as well as various fees, which they charged developing country borrowers for both medium- and short-term credits. Secondly, the higher market interest rates of earlier years had raised the cost of funds borrowed by the official institutions which lend these funds to developing countries at fixed interest rates.

The difficulties encountered by one of the large debtors - Mexico - in making timely debt-servicing payments in August 1982 shook financial markets and prompted banks to reassess financial conditions in all debtor countries. Commercial loans dwindled. Partly because of this, but also because of sluggish export earnings, an exhaustion of international reserves, and high interest payments, many countries had to seek to restructure their debt-service payments through negotiations with their private and public creditors. There were more cases of bank debt restructuring in 1983 than in the whole period 1980-1982. Thirty capital-importing developing countries (16 from Latin America and the Caribbean,

Table I-5. Measures of the interest cost on the external debt of capital-importing developing countries, 1979-1983

(Percentage)

	1979	1980	1981	1982	1983[a]
Interest rates on total debt[b]	7.8	9.2	10.7	10.9	9.2
Official development assistance loans[c]	2.2	2.3	2.2	2.1	2.2
Export credits[c]	7.8	8.2	7.9	8.4	9.0
World Bank loans[d]	8.6	8.5	8.1	9.2	9.6
Use of IMF credit[e]	5.1	6.7	11.1	10.4	9.2
Medium-term debt at floating interest rates[c]	12.3	15.5	17.4	17.3	12.7
Interest payments in relation to foreign exchange earnings	9.9	10.7	14.1	17.9	17.0

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *Balance of Payments Statistics, International Financial Statistics, Annual Reports* (various issues), and quarterly financial statements; World Bank, *World Debt Tables* and *Annual Reports*; Bank for International Settlements data series on the maturity distribution of international bank lending; and Organisation for Economic Co-operation and Development, *Development Co-operation, 1983 Review.*

[a] Preliminary estimate.
[b] Annual interest payments made (rather than interest due) as a percentage of disbursed outstanding debt at the beginning of the year.
[c] Estimates of OECD secretariat; ODA and export credits from member countries of the Development Assistance Committee only.
[d] Interest and fees for all World Bank borrowers, excluding International Development Association loans, fiscal years ending 30 June.
[e] Interest accrued for all users of IMF credit for fiscal years beginning 1 May; estimate for 1983 based on two quarters of fiscal year.

10 from Africa, 3 from Asia and 1 from Europe) either restructured their commercial debts or initiated debt renegotiation processes.[7] Similarly, an unprecedented 17 developing countries from Africa and Latin America renegotiated their debt to one or more foreign official creditors during 1983. Almost $70 billion of debt servicing was restructured during 1983, more than 10 times the amount of developing country debt restructured in 1981 and 1982 combined.

The above notwithstanding, many high-debt developing countries have yet to reach a sustainable set of debt-servicing obligations. For the countries whose debt renegotiations had not been completed in 1983, at least $40 billion remained to be settled in 1984. Moreover, since many of the debt renegotiations of 1983 did not pertain to debt-servicing obligations through all of 1984 and very few included 1985 debt servicing, there is a possibility that there will be a significant number of new debt-restructuring negotiations over the near term.

In the restructuring process, emergencies were dealt with and are still being dealt with through *ad hoc* arrangements involving committees of private banks and committees of creditor Governments (in particular, the Paris Club), and including the participation of multilateral institutions. In this, the International Monetary Fund has played a central role, both in support of the debt-renegotiation process and in working out with member Governments adjustment programmes which would be supported with the use of IMF credit. As a consequence, a certain set of practices has been established which has regularized the steps in restructuring debt and thereby helped to reduce the likelihood of financial crises. Nevertheless, original plus rescheduled amortization payments and continuing high interest rates are still putting substantial financial pressures on high-debt countries.

Interest payments in capital-importing countries presently absorb about a sixth of export earnings on goods and services. For low-income countries, though on the increase, the corresponding figure is only about a twentieth. This lower figure is explained by the fact that a substantial part of their debt is either on concessional terms or debt from official sources contracted at fixed interest rates at a time when such rates were comparatively low. For other developing countries, the share of export earnings taken up by interest payments varies widely. Latin American countries have been particularly affected by rising interest rates. In 1983 two thirds of the countries in Central and South America paid interest on external debt that represented from 20 to 50 per cent of the total exports of goods and services. In half of these countries interest payments abroad absorbed more than 5 per cent of their national income that year.

As observed previously, most developing countries, as a reaction to increasing current account deficits, instituted policies leading to significant import cut-backs. As a consequence, current account deficits in capital-importing developing countries narrowed substantially in 1983. The magnitude of import cut-backs has been such that in a large number of countries a significant surplus in the trade balance emerged in 1983. In some of these countries, however, large interest payments caused the current account to remain in deficit, and consequently, debt levels increased further.[8] The dynamics of a large external debt when accompanied by high interest rates are such that even dramatic efforts on the part of the debtor - including considerable consumption cut-backs - and a significantly improved export outlook are not necessarily sufficient to achieve lasting solutions to the debt problem. Recent experience has shown, in fact, that certain heavily indebted countries have had difficulties in meeting payments even shortly after restructuring exercises were completed.

Clearly, debt restructuring exercises have significantly contributed to a short-term improvement in the payments positions of debtor countries. In 1983, if amortizations had been met out of current earnings, they would have absorbed about 10 per cent of the capital-importing countries' foreign exchange earnings. However, amortization requirements have only been postponed and only for a brief period. After 1985, rescheduled amortization payments begin to fall due in substantial amounts and will be added to previously-scheduled amortization payments falling due at the same time. In short, from the perspective of developing country repayment profiles, a more permanent solution to the debt-servicing crisis would have been a conversion of medium-term debt to long-term debt instruments.[9] Failing that, a renewed debt crisis will be avoided only if creditor banks remain sufficiently confident in the debt-servicing capacity of developing countries to roll over a substantial share of debt repayments with new loans in the latter half of the 1980s.

For the capital-importing developing countries as a whole, as well as for certain high debt countries in particular, the prospects for reducing the interest burden in the near term are not encouraging. Based on forecasts for exports contained in chapter II of the present *Survey* and the outlook for interest rates, at best a marginal reduction is expected in the 17 per cent share of foreign exchange earnings which was needed in 1983 to effect interest payments. In other words, if there were a modest 5 per cent annual growth in debt outstanding (less than the growth of debt in 1983) and if the effective interest rate on total debt were 10 per cent, then the ratio of interest payments to foreign exchange earnings would be almost 17 per cent in 1985. In order to return by 1985 to interest-servicing ratios roughly equivalent to those prevailing at the end of the 1970s, growth in export earnings would have to be about 20 per cent per annum and average interest rates would have to fall by two percentage points.

Therefore, if debtors are to avoid repeated interest-servicing difficulties, in addition to a substantially higher rate of growth of export earnings, interest rates must fall. In fact, the spreads that private banks are charging on new syndicated credits to the two countries with the largest outstanding debt, i.e. Brazil and Mexico, began to fall in late 1983. Further declines should be encouraged from the extremely high rates charged some developing country borrowers during the crisis of confidence in 1982 and 1983. However, a reduction of spreads will not lower the overall interest burden sufficiently, since lower spreads would apply only to new loans and would leave the cost of servicing the entire stock of floating-rate debt unaffected. A significant alleviation would come only from lower base interest rates, and this requires changes in macroeconomic policies in the main capital market centres.

The special difficulties of sub-Saharan African countries

The sub-Saharan African countries have been particularly vulnerable to the impact of the recession. Given the low level of income of most of these countries, decreases in output and employment cause great hardship. The average per capita income of the 45 countries in the region is only half that of developing countries as a whole. Among the group, 26 are least developed countries with a per capita income below $300 per annum. Even in mineral-exporting countries, rarely less than two thirds of the population works in agriculture, half of whose output is derived from subsistance production. Agriculture is still the mainstay of the economy in most countries, contributing about one-third of GDP.

During the early 1980s, the economies of these countries have on the whole stopped growing (see table I-6). In the energy-importing countries, growth rates of GDP were already

Table I-6. Developing countries in sub-Saharan Africa: annual rates of increase in key variables, 1970-1983

(Percentage)

	1970-1975	1976-1979	1980-1983
Real GDP			
Total	4.5	3.0	0.0
Energy importers	2.8	2.1	0.6
Energy exporters[a]	6.1	3.9	-0.4
Agricultural production			
Total	1.6	1.1	1.9
Per capita	-1.2	-1.5	-1.1
Food production			
Total	1.6	1.5	2.1
Per capita	-1.2	-1.4	-1.0
Memorandum item			
Percentage share of exports in exports of all developing countries[b]			
Total	11.8	8.6	7.5
Non-fuel exports	18.6	9.2	7.0

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics* and data provided by the Food and Agriculture Organization of the United Nations (FAO) and the United Nations Conference on Trade and Development (UNCTAD).

[a] Angola, Cameroon, Congo, Gabon and Nigeria.
[b] Data refer to 1970, 1978 and 1982.

low in the 1970s and declined to almost nil in the early 1980s. Owing to the oil price increases in international markets and significant oil findings, the energy exporters were able to maintain a considerable momentum during the 1970s, but since 1981 their combined output has contracted.

The adverse impact of the international recession and the current drought have compounded problems of a more long-standing nature. One of the reasons for the low rates of economic growth in the energy-importing countries since the mid-1970s is that several countries in the region delayed adjustment to the disturbances of the first half of the decade.

Overvaluation of the currency became common and, as a consequence, the volume of exports lagged considerably.[10] The share of sub-Saharan exports in the exports of all developing countries fell by more than a third between the early 1970s and the early 1980s. The fall in the corresponding share of non-fuel exports was even more pronounced. Thus, as compared to other developing countries, exports did not play a dynamic role in stimulating and modernizing the economy and allowing for increases in the capacity to import.

Another important factor has been the weak performance of the agricultural sector. In a large number of countries, the growth of food production and of agriculture in general has remained well below population growth as a result of low productivity per unit of land, inadequate investment, poor incentives to farmers, limited research, and institutional constraints.[11] Adverse climatic conditions also contributed to the weak performance of several countries, even before the 1980s.

Food shortages and famine remained more localized during the 1970s than in the early 1980s.[12] The drought that started in 1982 became widespread in 1983. It is estimated that 150 million people are at present threatened by hunger and malnutrition.[13] Moreover, the drought has coincided with a very strained external payments situation that has rendered these countries particularly vulnerable to any disturbance. As a result, many of them are experiencing difficulties in supplementing their dwindling food supplies with increased imports.

Despite lagging food production during most of the 1970s, certain developments prevented the situation from reaching a critical stage. Although the export earnings of the energy-importing countries grew less than those of other regions, they none the less registered some increases, particularly since export prices remained favourable during most the period. Rapid increases in the export earnings and incomes of the energy-exporting countries stimulated exports and migration from neighbouring countries.[14] In the energy importers, emigration alleviated the food situation, while exports to, and workers' remittances from, energy-exporting countries added to their capacity to import. Official financial flows also increased at a relatively fast pace in many countries during this period. Some countries (particularly among the energy exporters) also had access to private flows, and international reserves remained at levels equivalent to almost three months' imports. Thus, on the whole, there was some room for increased food imports without substantial cut backs in the imports of other essential commodities.

In the early 1980s the situation has changed radically. The export earnings of the energy-importing countries have declined markedly and persistently as a result of the international recession and of growing excess supplies for some primary commodities. The situation compares very unfavourably to that of the energy-importing countries of Asia and Latin America, whose exports have continued to grow, albeit at a reduced pace. The prices of cocoa, coffee, copper, groundnut oil and sugar, which constitute the main export products of these countries, experienced a significant decline after 1980, and by 1983 they were still below their 1979 levels. Meanwhile, the cost of imports has continued to increase, and ODA flows have stagnated (see table I-7). The rise in interest rates has

Table I-7. Developing countries in sub-Saharan Africa: international trade and reserves, 1978-1983

	1978	1979	1980	1981	1982	1983
Merchandise exports (billion dollars)	26.8	39.0	52.1	38.8	34.4	29.5
Energy importers	13.3	16.5	19.0	15.2	13.6	12.5
Energy exporters	13.5	22.5	33.1	23.6	20.8	17.0
Merchandise imports (billion dollars)	32.6	32.3	44.9	42.9	39.4	32.3
Energy importers	17.1	18.9	24.0	20.9	18.9	16.1
Energy exporters	15.5	13.4	20.9	22.0	20.5	16.2
Gross reserves (end of period) as percentage of imports	9.5	16.7	18.3	12.3	9.1	11.2
Energy importers	11.1	10.6	7.5	9.1	9.5	13.7
Energy exporters	7.7	25.4	30.6	15.6	8.7	9.2
Prices of main export commodities (1977 = 100)						
Cocoa	79	74	59	47	40	48
Coffee	65	74	65	46	49	55
Copper	104	151	166	132	112	121
Cotton	101	108	131	117	101	118
Groundnut oil	126	104	100	122	68	83
Sugar	121	145	179	169	147	143
Energy-importing countries[a]: unit value of imports (1977 = 100)	110	128	156	155	150	152
Real net ODA disbursements[b] (billion dollars)	4.7	5.1	5.5	5.7	5.6	...

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics* and *World Economic Outlook* (Washington, D.C., 1983); and Organisation for Economic Co-operation and Development, *Development Co-operation*, 1983 Review (Paris, 1983).

[a] Includes Cameroon, Congo, Gabon and Angola.
[b] In 1977 prices and exchange rates. Deflated by the ODA deflator of DAC member countries.

led to an additional outflow of resources, although not as large as in other developing countries. International reserves have been gradually exhausted in many countries, and imports have had to be compressed substantially.[15] Between 1979 and 1983, the fall in the volume of imports was virtually uninterrupted.

The export earnings of the energy exporters - Angola, Cameroon, Congo, Gabon and Nigeria - experienced a marked increase in 1979-1980. Although the export earnings of the smaller countries continued to increase in 1981, there was a substantial drop in Nigeria's oil exports. The latter was affected not only by soft oil markets but also by the OPEC agreement to cut oil export volumes. Nigerian export earnings continued to fall in both 1982 and 1983, by more than 15 per cent in each year. Coupled with a comparatively high private debt, this led to severe strains on the balance of payments and on overall economic activity. Furthermore, since this country's large economic size and rapidly expanding output had transformed it into a growth pole in the region, the contraction in its economic activity has had substantial effects on neighbouring countries. Problems were compounded for the latter as many migrant workers were asked to return to their home countries.

The downswing in export prices which began at the end of the 1970s clearly revealed the vulnerability of the balance-of-payments situation in many sub-Saharan countries. As a result, various adjustment measures were undertaken, often in conjunction with the IMF. However, as the world recession deepened and persisted longer than anticipated, adjustment programmes had to be repeatedly revised and extended. Thus, in each year since 1979, roughly a dozen sub-Saharan countries entered into stand-by arrangements with the IMF for Fund-supported adjustment programmes.

Programmes in the context of IMF assistance have contemplated substantial modifications in general economic policies aimed at correcting internal as well as external imbalances. Currencies have been devalued, in some cases, by a substantial amount. In an effort to reduce budget deficits and correct distortions in the domestic price system, there have been sharp increases in producer prices for agricultural goods, and the subsidies on basic foodstuffs and fuel have been phased out. In addition, in several countries reforms have been introduced in public enterprises.[16] This does not mean that the implementation of adjustment programmes has been easy. Indeed, smooth and timely achievement of adjustment objectives has been the exception rather than the rule owing, *inter alia*, to exogenous factors, difficulties in mobilizing sufficient political support for requisite adjustment measures, limitations in administrative infrastructure and delays or shortfalls in net inflows of ODA.[17]

Although most of these adjustment programmes were initially of about one year's duration (and many had to be extended), some of the adjustment programmes were originally understood to require longer periods and more significant domestic changes. Indeed, certain countries received support from the Extended Fund Facility, while some participated in the structural adjustment lending programme of the World Bank.

But despite the policy changes already implemented, balance of payments strains are unlikely to abate in the short term, particularly since the region's export markets are expected to remain sluggish in the near future. Oil export earnings are expected to remain depressed because of weak world demand, and large stocks in world markets for other commodities of interest to sub-Saharan Africa hinder prospects for sustained increases in their export prices. These dim short-term prospects make progress towards export diversification, energy transition and improved agricultural performance even more urgent.

Yet in addition to the reforms which these countries can undertake on their own, others require investments which are beyond their capacity at the present time. Adequate external support is therefore essential to help sub-Saharan countries accelerate progress in what has become a painful adjustment process. Firm commitments to policy reform should not be jeopardized by strained balance of payments situations and poverty-related social tensions that threaten political stability. The immediate situation requires the emergency provision of food aid in much increased amounts. Improvement in foreign exchange availabilities is also critical, since widespread shortages of basic inputs and raw materials have brought the investment effort and certain manufacturing activities to a virtual halt. Moreover, such shortages may jeopardize the positive impact of recent policy reforms by worsening inflation.

The special needs of the region have been recognized by such international agencies as the World Bank, which has allocated a greater share of concessional aid to sub-Saharan Africa for the next triennium. More recently, the Secretary-General of the United Nations has undertaken a major initiative to focus international attention on the present crisis, to help in mobilizing additional resources and to improve through concerted action, the effectiveness of efforts made in the international community.

Foundations for a sustained recovery in developed market economies

While the present situation offers little promise of an early and vigorous reactivation of development throughout the developing world, the strength and duration of the recovery now under way will be of key importance in shaping the prospects for these countries over the next few years. Were the recovery to fail to gather strength or were the next cyclical downturn to be early, the developing countries currently enmeshed in difficulties inherited from the last few years could find their difficulties stubbornly persist. But it is also possible that the emergence of an appropriate conjunction of policies and circumstances in the developed market economies may shift them on to a growth path which, though still cyclical, is on a higher plane than that of the last ten years. The central question on this score is whether policies and circumstances will combine to induce a higher level of fixed investment. While the annual rate of growth of gross fixed investment exceeded 6 per cent during the buoyant years between 1964 and 1973, it slowed to only 0.5 per cent in the much more sluggish years between 1974 and 1983. Since mid-1983, investment in the developed market economies experiencing a cyclical upturn, has generally been picking up. However, the question remains whether the changes in investment behaviour represent only a cyclical rebound or whether they presage a shift in longer-term trends.

It is certainly apparent that a number of circumstances are more favourable to investment than has been the case for quite a number of years. For one thing, anti-inflationary policies and the recent recession have substantially lowered the pace of inflation - by four percentage points between 1980 and 1983 in the major developed market economies as a group - and have dampened inflationary expectations; and they have also brought about changes in relative prices and costs which have improved the profitability of investments. Although the problem of wage rigidity continues to challenge policy makers in some countries where inflation remains high and unemployment rates are at double-digit rates, in many countries flexibility in wage setting has increased. There are increasingly more cases where existing long-term contracts have been re-opened, where wage rounds in one sector have been delinked from those in other sectors, or where the link between wage rates and price inflation has been broken. While high rates of unemployment are clearly a major reason for these changes, they may also be indicative of more lasting changes in wage-setting behaviour. As it stands now, the share of wages in manufacturing income, which until recently exhibited a secular upward trend, seems to be falling.

Some other costs - raw materials and energy - have fallen quite considerably. Current prospects for energy prices are that they will not exhibit any major increases in the near future, and primary commodity prices are recovering slowly. While these price declines have obviously had an adverse effect on the producing sectors or countries, they have also helped to improve the profitability of manufacturing industry.

An additional factor that has a bearing on investment decisions is the relationship between market valuation of existing firms and the reproduction cost of capital.[18] This relationship, partly on account of cyclical reasons, has increased very significantly in the last eighteen months. This suggests a strengthening of investment demand, at least in the short run.

For the longer run a major question is whether the change in the price and cost relationship will prove to be durable or whether it will be reversed as the recovery in economic activity matures. The greater wage flexibility evident in the last few years in a number of countries could tend to lessen as and when unemployment begins to decrease. By the same token, primary commodity prices could begin to rise more rapidly if the overall rate of economic growth were to accelerate sufficiently. But for the next few years growth rates are likely to be moderate in most parts of the world economy, and unemployment in most developed market economies may remain high or even increase in some countries.

There is, however, one element of costs which has not undergone a relative decline in recent years, and that is the financial cost of capital. Though price inflation has declined, real long-term interest rates remain high. It is true that high long-term interest rates are only a part of the net cost of capital relevant to business investment. Tax rates and capital consumption allowances, as well as debt-equity ratios, determine the net costs of capital for business; and in the United States, though less so in Western Europe, the tax deductibility of interest payments and the introduction of accelerated depreciation methods have reduced such net costs. Even so, the high level and uncertainty regarding the future direction of long-term interest rates remain important concerns for investment prospects.

At the present time, business confidence is strengthening in several major developed market economies. Besides the changes in the price and cost situation, the utilization of installed capacity, though still low, is increasing, and the prospective need for additional capacity is growing.[19] Indeed, presently recorded rates of capacity utilization may overstate the actual amount of idle capacity that remains to be brought into use since some proportion may well have become obsolete because of changes in relative prices of inputs, in the composition of demand and in international competitiveness. In addition, the recent spurt of innovations in fields such as micro-electronics, biotechnology, laser technology and optic fibres could also provide an impetus to new investment that could last for many years. The application of these technologies to industrial processes has barely begun, and they seem to have a vast potential for future commercial application.

However, equally as important as present demand is how its evolution over the next several years as perceived by those taking investment decisions. For them, the question is whether the growth of demand will be sufficiently strong and stable to give reasonable promise of an adequate rate of return; and this depends in no small degree on the economic policies that are adopted in the large industrial countries. In the United States, the conflict between an expansionary fiscal policy, reflected in large federal budget deficits projected well into the future, and a relatively restrictive monetary policy, is a major cause for concern. It is feared that, as the recovery matures, persistent budget deficits may put pressure on prices which would force the monetary authorities to practice greater monetary restraint. In this view, policy makers would have to choose between high interest rates and recessionary conditions or a return to higher inflation, neither of which would be conducive to the sustainability of investment.

In Western Europe, policies in the early 1980s have been non-accommodating and anti-inflationary and have acted to restrain the cyclical recovery. Monetary policies have been generally cautious and have been constrained by interest rate developments in the United States. Even in the midst of a recession, fiscal policies have been directed at reducing the size of the Government's budget deficit through raising taxes and cutting public sector investment. Fiscal austerity in a number of European economies has also been aimed at contracting the relative size of the public sector. This has been a central element of a policy to promote longer term economic growth by increasing the role of the private sector and reducing market rigidities. However, by restraining aggregate demand, these measures conflict with the short-term objective of raising levels of economic activity. Indeed, if policies were not to allow the progressive restoration of aggregate demand to high levels, they might fail to provide sufficient inducement to invest, thus frustrating realization of the longer term aim.

In Japan, too, economic policies have tended to be restrictive for some time and could remain so in the immediate future. The aim of reducing budgetary deficits is also important in Japan, so that planned changes in taxes and expenditures in 1984 may, on balance, have a deflationary impact on the economy.[20] Monetary policy has also contributed to the relatively restrictive stance of economic policy. The growth of monetary aggregates have tended to be within policy targets, and real short-term interest rates have been higher than in the United States. Whether such policies will be maintained in the longer run is the question.

In sum, the longer-term outlook for investment is still mixed. While certain changes have taken place in recent years that are favourable to a restoration of strong growth in investment, it is not yet clear that these changes are of a permanent nature. Moreover, high real interest rates persist, and perhaps most important, doubts about the consequence of economic policies for long-term growth of demand may deter investors. The strength of aggregate demand will depend significantly on whether economic policies can both be sufficiently expansionary and meet such other objectives as dampening inflation or making room for greater private initiative in the economy.

Broadening recovery and reactivating development: some requirements for international co-operation

Some aspects of the current world economic situation are encouraging. A number of developing countries in Asia have demonstrated a capacity for vigorous growth even in the face of world recession. The centrally planned economies of Eastern Europe have made substantial progress in adjusting to a much more difficult external payments situation. Inflation has subsided in most developed market economies, and recovery is under way.

But the current situation has major flaws and dangers. Prospects for a more sustained revival of investment and growth in the developed market economies are threatened in different ways by their present policy stances; these stances may either persist in leaning towards deflationary restraint or provoke a reversion to deflationary measures. At the present time, deflationary policies remain inescapable for much of the developing world as a consequence of the debt burden, high interest rates and the weakness of recovery in world trade. More important for the medium-term is the fact that the functioning of the international trading and financial system - within which the reactivation of development must take place - has been seriously impaired by events of recent years. Besides immediate measures for recovery, the restoration and improvement of that system is essential for the reactivation of development.

Changes in the policy stances of developed market economies could help both to broaden the present recovery and to improve the medium-term prospects in these countries themselves. A major contribution would be a lowering of real, long-term interest rates through a contraction in the prospective budget deficits of the United States combined with the pursuit of a less cautious monetary policy. In Western Europe and in Japan, lower interest rates in the United States should provide more room for economic expansion, at least in those countries that have already reduced their structural budget deficits. The current bias in demand-management policies there continues to be on the side of caution, which, in an interrelated group of countries, cannot but engender a greater deflationary shift than intended by each of the countries. A mutually supportive relaxation of these cautious fiscal policy stances in the majority of European countries and in Japan could result in a gradual convergence of growth rates around a much higher level. It is possible that in this context both objectives - higher growth and a smaller phase of government expenditure on gross national production - can be achieved concurrently in the medium term.

Many developing countries continue to face severe liquidity difficulties in their external payments. Though some part of these difficulties originate in the cyclical behaviour of the world economy and are therefore temporary, the international reserves and payments finance available to these countries have proved far from sufficient to cover such temporary deficits. Their reserves were generally drawn down in the earlier phases of the recession and payments finance from private markets dried up with the onset of the debt crisis. While the volume of official finance made available through the IMF increased substantially, recent experience demonstrates that the total international liquidity available to developing countries severely restricts the size of the temporary deficits that can be supported. An issue of SDRs in the immediate future would be one step towards correction of the situation.

The alleviation of the plight of sub-Saharan African countries is of particular importance. Food aid is critical, but it is not enough: sufficient supplies of seeds and fertilizers need to be made available to farmers now to improve the outlook for 1984-1985 harvests. Apart from providing for immediate needs, it is necessary for the future not to allow investment levels to deteriorate further. This underscores the contribution that the World Bank and regional financial institutions can make and the need for these institutions to be provided with the requisite resources. It also shows the crucial importance of the increased support from other multilateral agencies and bilateral donors.

For the more heavily indebted countries, the strengthening of their external payments situation is markedly aggravated by the high level of interest rates, as well as by the widened spreads on renegotiated loans. The source of these high rates is the particular mix of policies pursued in the United States, and some alleviation of the rates paid by the indebted countries is called for, either through a general decline in market rates or by more direct means. The ability of these countries to restore high levels of domestic economic activity while maintaining much reduced, or even negligible, current account deficits, could be long delayed if their present capacity to pay for imports is not substantially improved. The domestic investment needed to effect the appropriate adjustment in productive structures will be slow to occur if imports and domestic economic activity remain severely curtailed. The recent experience of South and East Asian countries points to the benefits of external loans in support of structural adjustments. Some restoration of lending to the countries now experiencing the severest balance of payments difficulties would both hasten the easing of these difficulties in the medium-term and lessen their presently deflationary influence on world trade and production.

The situation calls for an array of measures to strengthen existing, and to introduce new mechanisms for long-term resource transfers for development and to meet short-term international stabilization needs. Private international banks are not likely to resume the role they played as financial intermediaries in the 1970s, at least not to the same extent; and as recent experience with the banks bears out, there is no reason to presume that financial markets, left to themselves, will reach the most appropriate solution. The role of private markets can be enhanced through improvements in their functioning. But recent experience emphasizes the need to enlarge the flow of capital through official channels. Limited steps have already been taken in this direction: instances are the review of quotas of the IMF, the recent capital expansion of regional development banks and the preliminary agreement on the selective capital increase of the World Bank.[21] Nevertheless, these are far from sufficient. Neither the outlook for bilateral ODA, including IDA replenishment, nor the growth in lending forthcoming from the multilateral financial institutions yet seem adequate to create an environment favourable to a healthy reactivation of development.

Like mechanisms for the transfer of real resources, the functioning of the international trading system has been impaired by the events of recent years. Yet, like the transfer of real resources, an expanding trade has a central role to play in recovery of the world economy and the reactivation of development. It is not only that trade serves as a means through which countries, by pursuing their own comparative advantage, can make more productive use of their own resources; it is also that, through trade, the expansion of economic activity in individual countries can become mutually reinforcing. The interactive dynamics that work through trade are today a major element in shaping the climate for investment in most countries.

A consistently faster rate of growth of world trade than of world output has been an important characteristic of the post-war period. In both the developed and the developing market economies, the share of exports in gross domestic product nearly doubled between 1960 and 1980 (see table I.8). In 1983, however, there was a sharp reversal in the role of trade in the world economy; in failing even to keep pace with the small increase in world output, it became a deflationary rather than an expansionary influence.

No doubt, the reversal in the role of trade has been temporary and very largely a consequence of the particular pattern of recovery. However, it is troubling that it has followed a period of rising protectionist measures. Indeed, it is difficult to be sanguine about the expansionary role of trade in an increasingly protectionist climate. The recent call from several Governments for a new round of multilateral trade negotiations is therefore encouraging; it gives hope that a new period of trade liberalization may be in prospect. It is very likely that a prominent issue in such negotiations would be non-tariff barriers. But the possibility of new trade negotiations should not lead to complacency; actions to halt and reverse protectionist measures now are required: they are a key element in the restoration of growth and development.

Policy conclusions:

The analysis contained in this chapter, in conjunction with the assessments and forecasts of the chapters to follow, points to a number of directions that current policy should take in order to improve the international economic environment and set the stage for sustained, non-inflationary growth of the world economy. These may be summarized as follows:

1. That both domestic policies and the international economic climate are vital factors in successful adjustment can be seen from the diverse experiences of individual countries in the early 1980s. The growth prospects in many developing countries depend significantly on the effectiveness of domestic measures designed to ease import constraints and increase export capacities. In developed countries, there is a comparable need for progressive adjustment of productive structures to improve growth prospects.

2. Lower interest rates are required to provide a further stimulus to investment in developed and developing countries and to ease the debt service burden of many of the latter. The implementation of proposals being considered by the United States Government to reduce its prospective budget deficits could make a major contribution towards this end.

3. A mutually supportive relaxation of the cautious fiscal policies currently being pursued in Japan and Western Europe, particularly in those countries which have already reduced their structural budget deficits, could result in a gradual convergence of growth rates around a higher level. This could be facilitated by lower interest rates in international financial markets.

4. Most of the European centrally planned economies are pursuing adjustment policies to correct their current external imbalances. To achieve and sustain a higher pace of growth would require them to redesign their national and group-wide economic policies so as to reflect better their current development conditions. The economic summit of the CMEA countries scheduled for June 1984 offers a unique opportunity to do so.

5. Actions to halt and reverse protectionist measures are key elements in restoring dynamism to international trade and broadening the recovery. There are strong grounds for supporting the recent call for a new round of multilateral trade negotiations. Preparations for such a round should not detract from immediate action by governments to increase access to their markets.

a recapitulation

6. An increase in international liquidity is likely to impart a needed stimulus to international trade. An issue of SDRs in the immediate future could significantly alleviate the severe liquidity constraint faced by many developing countries.

7. A revival of trade among developing countries is an important element in fostering diversification and economic growth. A follow-up of the guidelines provided in the Economic Declaration of the Seventh Conference of Heads of State or Government of Non-Aligned Countries [22] and in the Quito Declaration and Plan of Action of the Latin American Economic Conference [23] could make a valuable contribution to this end.

8. An increase in food aid and an improvement in food distribution systems are vital to alleviate the critical situation brought about by the effects of the droughts in sub-Saharan Africa. Food aid requirements have almost doubled since 1982/83. Moreover, sufficient supplies to farmers of seed and fertilizer are required now to enhance the prospects for the 1984-1985 harvests. For the longer term, the implementation of effective domestic policies for agricultural development is central.

9. A greater flow of ODA, both bilateral and multilateral, is necessary to facilitate structural adjustment and to reactivate development in low income countries, particularly the least developed countries. It is essential that there be a timely replenishment of the resources of the International Development Association of the World Bank, bringing them at least up to previous levels.

10. The resumption of international lending to highly-indebted countries would avoid further retrenchment in these countries and its deflationary consequences for the world economy. One of the actions required is a more systematic conversion of medium-term debt to long-term debt instruments.

11. An increased availability of long-term capital should help revive investment in developing countries. Early agreement on the proposed Selective Capital Increase of the World Bank by at least $8 billion would be an important contribution.

12. Programmes to correct the balance of payments disequilibria of developing countries should contain a proper mix between demand management policies and supply side measures. An important step in this direction would be an expansion in the use of extended arrangements and the adoption of stand-by arrangements which normally exceed one year, as originally provided for in the IMF Executive Board's decision in 1981 establishing the Enlarged Access Policy.

Table I-8. Annual growth of real GDP and volume of trade, 1960-1983[a]

(Percentage)

Country groups	1961-1973	1974-1979	1980-1983[b]
Developed market economies			
GDP	5.0	2.6	1.2
Exports	8.4	5.1	1.6
Imports	8.9	3.6	-0.2
Developing market economies			
GDP	6.1	5.2	0.3
Exports	6.7	2.0	-3.2
Imports	6.0	8.9	3.9
Memorandum item:			
Ratio of exports to GDP[c]			
Developed market economies	10.7	15.5	21.0
Developing market economies	13.0	23.6	26.0

Source: Department of International Economic and Social Affairs of the United Nations Secretariat.

[a] Geometric means.
[b] 1983 estimates are preliminary.
[c] Merchandise imports as a percentage of GDP in current prices and United States dollar exchange rates; average of the beginning and end of period. (Figures for the 1980-1983 period for aggregate nominal GNP have been especially sensitive to the strength of the dollar. This explains why ratios increased significantly in this period despite sluggish growth in exports.)

At this juncture, the importance of greater international economic co-operation cannot be over-emphasized. While the world is beginning to emerge from the prolonged international recession, it is necessary to start taking the actions discussed above to avoid a recurrence of recent difficulties and to reactivate development in the developing world. A more detailed analysis of these and related actions appears in the recent report of the Secretary-General on review and Appraisal of the International Development Strategy for the Third United Nations Development Decade.[24]

This report addresses the main policy issues that result from an examination of long-term growth problems and of the new circumstances brought about by developments in the early 1980s. It describes the concrete policies required to accelerate growth in the different regions and to protect the development process from excessive fluctuations in the international economy. In the context of interdependence, it pays particular attention to the changes required in the international financial and trading system. Although the Report acknowledges some erosion of collective international action in the first years of the Decade, it reiterates that the "recognition of long-term mutual interest will counsel renewed efforts at co-operative approaches within a multilateral framework."

Notes

1 See *World Economic Survey 1980-1981* (United Nations publication, Sales No. E.81.II.C.2), pp. 74-76.

2 See "Social aspects of development: report of the Secretary-General" (A/39/171-E/1984/54).

3 An examination of employment trends and unemployment is presented in International Labour Organisation, *Background Sectoral Report of the International Labour Office on the Review and Appraisal of the Implementation of the International Development Strategy for the Third United Nations Development Decade* (Geneva, January 1984).

4 See, for example, United Nations Children's Fund, *State of the World's Children, 1984*, chap. IV: "The impact of world recession on children - a UNICEF special study" (New York, Oxford University Press, 1984.

5 Measured as the ratio of total external debt to total annual foreign exchange earnings. Although Burma's overall debt ratio exceeds the average, it is a relatively small user of private credit; i.e., 81 per cent of Burma's medium- and long-term debt at the end of 1982 was owed to official bilateral and multilateral creditors, much of it on highly concessional terms.

6 Policies towards the food, energy and export sectors to stabilize incomes and stimulate production in these and other Asian developing countries are reviewed in Economic and Social Commission for Asia and the Pacific, *Economic and Social Survey of Asia and the Pacific 1982* (United Nations publication, Sales No. E.83.II.F.1), pp. 171-188.

7 Based on International Monetary Fund, *Recent Multilateral Debt Restructurings with Official and Bank Creditors*, occasional paper No. 25 (December 1983); World Bank, *World Debt Tables*, 1983-84 edition (January 1984); and other sources.

8 For example, if interest payments in 1983 had been half their actual levels, three Latin American countries - i.e., Argentina, Bolivia and Uruguay - would have eliminated their current account deficits.

9 Specific proposals towards this end appear in United Nations, *World Economic Survey 1983* (United Nations publication, Sales No. E.83.II.C.1), p. 20.

10 World Bank, *Sub-Saharan Africa: Progress Report on Development Prospects and Programmes*, September 1983.

11 Economic Commission for Africa, "ECA and Africa's Development, 1983-2008" (E/ECA/CN.9/23), April 1983.

12 While in 1973-1974 drought problems were confined to relatively few countries in the Sudano-Sahelian area, the current drought has affected 24 countries in western, eastern and southern Africa.

13 The consequences of the drought and the current food and agricultural situation are discussed in more detail in the annex.

14 Another country that acted as a growth pole and attracted foreign workers during the 1970s was the Ivory Coast.

15 The increase in the reserves-to-imports ratio in 1983 shown in table I-7 is due mainly to a drastic reduction in imports.

16 Reforms of public enterprises have been particularly important in Ghana, Sudan, Uganda and Zambia. They have included the streamlining of operations and changes in pricing policies.

17 *Finance and Development*, March 1984, pp. 5-9.

18 See *Economic Report of the President* (Washington, D.C., United States Government Printing Office, 1983) p. 92; and Economic Planning Agency of Japan, *Annual Economic Report* (Tokyo, 1983) chap. 2.

19 The capacity utilization rate for five countries - Canada, France, Federal Republic of Germany, Japan and the United States - rose from 73 per cent in 1982 to 78 per cent in 1983. The average rate in the period 1976-1980 was 81 per cent, and in 1970-1974, 87 per cent. 1981 GDP weights were used.

20 Organisation for Economic Co-operation and Development, *OECD Economic Outlook*, No. 34 (December 1983), p. 34.

21 A selective capital increase of $8 billion was the tentative figure accepted by most member countries of the World Bank in their preliminary agreement in September 1983.

22 A/38/132-S/15675, annex, chap. III.

23 A/39/118-E/1984/45, annex.

24 United Nations, "Review and appraisal of the International Development Strategy for the Third United Nations Development Decade: report of the Secretary-General", (A/39/115-E/1984/49), April 1984.

Chapter II

INTERNATIONAL TRADE AND PAYMENTS

An overview of the main issues

Developments in international trade and payments since the beginning of 1983 have illustrated the crucial interaction between the evolution of international economic and financial variables, on the one hand, and the strength and spread of world economic recovery, on the other. The upswing in the business cycle in some developed market economies has given some impetus to world trade. With the exception of fuels, exports to these countries have been rising rapidly, and there has been a modest recovery in non-fuel primary commodity prices after their steep declines in the period 1980-1982. However, external financial constraints have been responsible for a broad decline in the imports of developing countries, and this has dampened the growth of exports and output in developed and developing countries alike. At present, there are few signs that a decisive turn-around in the imports of developing countries will take place in the near future. The weakness of the recovery in Europe and, to a lesser extent, in Japan has also made for rather subdued rates of growth of international trade volumes.

The year 1983 can be seen as a period of change, when international trade volume and prices stopped declining and a moderate expansion in world trade got under way. As the year progressed, the growth in the volume of international trade gathered momentum. None the less, for the year as a whole, the growth of world imports was rather weak, amounting to less than 1 per cent. In the coming two years, a significant acceleration in the growth of world trade may take place as the recovery in world economic activity continues.

Nevertheless, several problems are still clouding the horizon. The strength and spread of the recovery will have an important bearing on the evolution of international trade. Of particular concern are the economic prospects for Europe. If growth in Europe fails to rebound strongly, this could have adverse consequences for world trade, since the European economies are more open than other developed market economies. As of the time of writing, it is not clearly evident that a strong acceleration of growth rates will take place in Europe in the next two years.

Unless their export earnings grow sufficiently, developing countries will fail to make a significant contribution to the expansion of world trade, since their imports are constrained by an acute scarcity of foreign exchange. For most developing countries, neither export volumes nor prices are likely to increase strongly enough to permit a major expansion in their imports. Besides the limited recovery in European countries, protectionist actions have escalated in recent years. If the protectionist threats that have recently emerged are acted upon, the exports of developing countries would be further affected. Although non-oil primary commodity prices could continue to rise, no major boom appears to be in the offing. Thus prices could remain considerably below the peaks they reached in 1979-1980. As regards oil, little or no change in prices is expected to take place in the next two years. Meanwhile, increases in the prices of manufactures imported by developing countries could be at least as large as the average increase in export prices, so that the terms of trade of developing countries may change very little.

These rather subdued prospects for export earnings are of particular concern to countries in debt-servicing difficulties. These include a number of developing countries and some centrally planned economies. The drying up of capital inflows from international capital markets, large amortization payments coming due, and stubbornly high interest rates, forced many developing countries into unprecedented reductions in import levels in 1983. In spite of severe adjustment, several countries were unable to service their external debt normally. Arrears became common, and there were a number of formal rescheduling exercises. Since the capacity to reduce imports further has been all but exhausted and the growth of export earnings in the next two years is expected to be only moderate, many countries could still face severe difficulties in meeting their debt-servicing obligations as they now stand.

An alleviation of the debt problem entails a reduction in interest charges and a substantial lengthening of maturities. In the absence of such measures, fears of an international financial crisis may recur. Moreover, continued stagnation or economic decline in the indebted countries is a serious drag on the world economic recovery.

Inadequate international liquidity is an even more widespread problem among developing countries than that of external debt. Although some countries began to rebuild their reserves in 1983, in a large number of countries reserves remain well below the levels necessary to finance three months' worth of imports. The problem is particularly acute in Africa, where in many countries reserves are insufficient to finance even one month of imports. The inadequacy of international liquidity is another reason for believing that the economic recovery will spread in an uneven and delayed way throughout the world economy and that it may elude many developing countries. Instead of using increases in export earnings to finance needed developmental imports, many countries will be devoting a good part of any such increase to improve their international liquidity positions.

The strength of world trade will depend in no small measure on the ability of Governments to resist rising protectionist pressures. Unfortunately, in recent years there has been a strong increase in the share of world trade affected by protectionist actions. Partly as a consequence of the strength of the dollar, demands for import restraints have grown louder in the United States. In Europe, too, protectionist pressures and actions are on the rise. Trade disputes between the major trading partners have become more acrimonious and are giving rise to the possibility of an escalation of measures and counter-measures. Particularly ominous signs since early 1983 have been the use of retaliatory actions, the spread of protectionism from one sector to another, and the competitive subsidization of agricultural exports by some industrial countries. Although developing countries have been able to expand their exports of manufactures at a stronger pace than the growth of world trade, the exports of many countries have encountered increasing trade barriers in the developed market economies. Measures now being contemplated could reduce their market access significantly in several sectors.

Another important problem clouding the international picture is the continued fluctuation of exchange rates and the uncertainties to which it gives rise. Large and unstable capital movements have come to dominate exchange rate determination, with the consequence that, from the point of view of trade, exchange rates have often been misaligned.

During 1981-1983 large capital flows into dollar-denominated assets caused the dollar to appreciate persistently, in spite of a growing current account deficit in the United States and a widely held perception that the dollar was overvalued from the point of view of changes in the prices of tradeable goods in the United States *vis-à-vis* those of its major trading partners. A rapidly expanding current account deficit in the United States has been accompanied by growing surpluses in other developed market economies, particularly in Japan and the Federal Republic of Germany. These disequilibria are expected to become even more pronounced in 1984. The result could be a sudden turn-around in the direction of capital flows and a decline in the dollar. Signs that this was beginning to take place were already in evidence in early 1984. Of course, the magnitude and speed of a possible fall in the dollar depend on a variety of factors, the evolution of which cannot be determined with any degree of certainty. In any event, it is clear that exchange rate fluctuations could continue to be very large. A weakening of confidence in the dollar could result in capital outflows from the United States and a depreciation of the dollar that is sharper than would be warranted by underlying trading conditions.

An orderly decline in the dollar, especially if it were not accompanied by a tightening of monetary policy in the United States and by higher interest rates, would have some favourable effects on world trade and finance. In particular, it would help alleviate the debt burden of developing countries, since a large portion of their debt is denominated in dollars. In addition, it would contribute to greater equilibrium in the external accounts of the United States and other major industrial countries. The real dangers are that the dollar might fall very rapidly and that it could overshoot its equilibrium level from the point of view of trade fundamentals.

The longer-term consequences of turbulence in exchange markets and protracted misalignments of exchange rates have already been analysed in some detail in a previous *Survey.*[1] It is now time to take steps to ensure that exchange rates do not deviate excessively from their equilibrium levels.[2] Progress in this direction would help to build confidence and could have beneficial effects on investment in trade-related activities.

The evolution of international trade

Modest upswing in world trade volume

The volume of world trade is now well into an upswing after almost three years of stagnation and decline. The expansion began in the course of 1983, when the imports of some segments of the world economy began to rise at a relatively rapid pace. However, the upswing so far has been modest (see table II-1). Although a significant acceleration in the growth of world trade is expected to take place in 1984, and even more so in 1985, these rates of increase are relatively low for a period of world economic recovery. For example, during 1976-1979, world imports expanded at an annual rate of over 6.5 per cent. By contrast, the growth rates expected for 1984-1985, when averaged with the estimate for 1983, yield an average annual rate of growth of world imports of only 3.5 per cent during the upswing of 1983-1985.

The main characteristic of the growth of world import volume during the current recovery has been its geographical unevenness. There have been very few poles of strong import expansion in the world economy. The most notable have been North America, which is in the midst of a strong cyclical rebound, and a few centrally planned economies. In Western Europe and Japan import growth rates continue to be negligible or negative. External constraints have forced developing countries and most centrally planned economies to reduce their import levels in absolute terms or curtail their rates of increase.

The sharpest increases in imports have taken place in North America. The substantial gain in the imports of Canada and the United States has been due partly to a relatively strong recovery in aggregate demand. In addition, appreciation of the United States dollar (and, to a lesser extent, of the Canadian dollar as well) against practically all other major currencies have made imports very competitive with domestic production. In the developed market economies outside of North America, relatively sluggish economic growth and depreciating currencies led to little or no expansion in import volumes. In some of these countries, imports actually fell in real terms. The imports of North America should continue to expand strongly in 1984 but considerably less so in 1985. As regards other developed market economies, it is expected that their imports will rise during this year and the next, but growth rates could turn out to be moderate.

Developing countries have been under strong pressures to adjust their import volumes downward. In a large number of countries, foreign exchange constraints have increased in severity. During 1983, the energy-exporting countries were affected by falling oil prices and a slackening in the demand for oil in both the developed market economies and in energy-importing developing countries. As a consequence, their export earnings contracted sharply. In many deficit energy exporters, the need to make room for debt-servicing payments that were a large percentage of export earnings also contributed to reduce import levels in real terms. The contraction in imports was particularly sharp in the deficit energy exporters (estimated at close to 20 per cent), but even the capital-surplus countries saw their imports decline in absolute terms.

Table II-1. World trade: annual rates of change in volume and prices,[a] 1976-1985

	1976-1980	1981	1982	1983[b]	1984[c]	1985[c]
Volume of exports						
World	5.2	0.2	-2.2	1.5	4	5
Developed market economies	6.6	2.2	-2.2	1.5	4	5
Developing countries	2.0	-4.8	-4.8	-0.2	4.5	5
Capital-surplus countries	-2.4	-16.7	-20.5	-5	4	4
Other net energy exporters	3.4	-6.2	-2.5	-0.5	4	5
Net energy importers	8.0	11.0	8.1	3	5	6
Centrally planned economies[d]	5.6	1.0	6.5	6.5	3	3
Volume of imports						
World	5.6	1.6	-0.7	0.5	4	5
Developed market economies	5.5	-2.1	-0.9	3	5	5.5
Developing countries	6.1	13.6	-1.0	-7	2	4
Capital-surplus countries	11.8	23.5	11.9	-11	3	5
Other net energy exporters	6.5	23.4	-6.4	-19	2	4
Net energy importers	4.5	6.1	-3.1	0.5	2	4
Centrally planned economies[d]	4.7	1.0	1.9	4	4	4
Unit value of exports						
World	12.2	-1.8	-4.4	-3.5	4.5	5.5
Developed market economies	9.7	-4.2	-3.2	-3.5	5.5	6
Developing countries						
Capital-surplus countries	23.5	10.5	-4.1	-11	-	5
Other net energy exporters	21.0	6.2	-5.8	-6.5	1.5	4.5
Net energy importers	11.2	-4.7	-11.6	-	4.5	4
Centrally planned economies[d]	8.8	0.2	-1.4	-1.5	4.5	4
Unit value of imports						
World	11.6	-2.5	-5.0	-4.5	4.5	5.5
Developed market economies	12.2	-2.9	-5.3	-5	4.5	5.5
Developing countries						
Capital-surplus countries	10.4	-3.6	-4.3	-3	5	5.5
Other net energy exporters	10.8	-3.1	-4.3	-3.5	5	5.5
Net energy importers	13.0	-0.8	-4.7	-4.5	4	5.5
Centrally planned economies[d]	6.9	-0.6	-3.3	-1.0	3.5	3.5
Terms of trade						
Developed market economies	-2.2	-1.4	2.2	2	1	0.5
Developing countries						
Capital-surplus countries	11.9	14.7	0.2	-8	-5	-0.5
Other net energy exporters	9.2	9.6	-1.6	-3.5	-3.5	-1
Net energy importers	-1.5	-3.9	-7.2	5	0.5	-1.5
Centrally planned economies[d]	1.7	0.9	1.9	-0.5	1	0.5

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics*, and calculations and forecasts made by the Secretariat.

[a] Rates of change in prices estimated from unit value indices expressed in dollars.
[b] Preliminary estimates, rounded to the nearest half a percentage point.
[c] Forecasts.
[d] Eastern Europe and the Soviet Union only.

The net energy-importing countries are also facing severe external payments pressures stemming from continuing debt-servicing difficulties, an insufficient recovery in export earnings, and a drying up of external financing from the international private banks. In 1983, declines in import volumes were widespread among these countries, although as a group their imports were practically stagnant. Sharp declines in imports in the more heavily indebted countries were compensated by strong increases in the Asian countries whose economies expanded rapidly. In sub-Saharan Africa, drought and other natural disasters affected the domestic production of foodstuffs and raised food import requirements.

Import cut-backs have already reached unsustainable levels in many developing countries, and some increase in import levels is likely to take place in 1984-1985. In the capital-importing countries, improved export earnings and a temporary easing of the debt-servicing burden as a result of debt-restructuring exercises may allow for a measure of recovery in import levels. However, continuing balance-of-payments pressures and the need to replenish international reserves may limit the feasible rates of import growth. Although there may be some increases in the imports of the capital-surplus countries, import policies are likely to remain cautious in the light of continuing current account deficits.

The external payments situation and the policies adopted to cope with it have differed measurably in Eastern Europe, China and the USSR. The foreign trade policies adopted by China and the USSR have largely reflected domestic development conditions. China's real imports expanded strongly in 1983 (perhaps by about 10 per cent), and further increases are being planned for 1984. The Soviet Union, on the other hand, has continued to tailor its import stance to domestic needs and export prospects. Its import volume may have increased by 4-5 per cent in 1983. Eastern Europe has placed absolute priority on obtaining current account surpluses, if necessary by restraining imports, and some countries (especially Poland and Romania) have encountered very severe external payments problems. In spite of these obstacles, Eastern Europe's import volume appears to have expanded by about 4 per cent in 1983. This surge beyond plan targets needs to be seen against the contraction of roughly 10 per cent in import volume in 1981-1982. Therefore, real import levels are still below those in 1980. During the next two years, however, the aim of reducing their external debt further may hold back the growth of imports of these countries.

The countries whose exports have been most adversely affected by developments in international markets have been the energy-exporting developing countries. Since 1979, the volume of exports of the capital-surplus countries have declined by almost 50 per cent. Faced with falling demand, OPEC member countries decided to curtail production and exports in order to stem the decline in prices. Energy exporters that are not members of OPEC have gained in market share, and some smaller exporters have even been able to increase the absolute volume of exports. In the deficit energy exporters, non-oil exports appear to have expanded at a stronger pace than oil exports.

In recent years, the energy-importing developing countries have been able to increase their exports substantially faster than world trade. This trend continued in 1983. However, while some export markets were buoyant, demand in others either showed few signs of reviving or declined even further. Exports of manufactures and industrial raw materials from Asian and Latin American countries to North America were very dynamic. On the other hand, exports to Western Europe expanded slowly, and exports to other developing countries appear to have fallen significantly. Owing to weak demand in major consuming centres and supply problems in several countries, the exports of Africa appear to have declined rather sharply.

Several factors account for the relatively strong export performance of some developing countries. Stimulated by a firming in demand and the anticipation of more buoyant sales, raw material stocks in the developed market economies began to be rebuilt. In some industrial countries, particularly in North America, demand for manufactures was strong. In addition, the sharp devaluations undertaken by developing countries in balance-of-payments difficulties made their exports very competitive in the markets of the industrialized countries.

The somewhat better growth prospects for the European economies and a rebound in energy consumption in the developed market economies in the coming two years should result in stronger rates of growth of exports for most developing countries. Barring further drift towards protectionism, the exporters of manufactures should be the major beneficiaries, but even oil exporters are likely to see some gains in export volumes.

During the 1970s and up to the onset of the recession, trade among developing countries expanded at rates substantially above those of world trade or of the total non-fuel exports of developing countries. Since 1982, trade among developing countries has suffered a setback. While the industrial countries were entering into the upswing of the business cycle in 1983, most developing countries experienced a decline in per capita output. Therefore, trade among developing countries failed to participate in the recovery of world trade. In fact, preliminary information reveals that such trade may have contracted substantially in 1983. Intra-regional trade in Latin America, hitherto an important component of trade expansion among developing countries, was particularly affected by the generalized cut-backs in import levels in that region.[3] The exports of goods and services to the energy-exporting countries, another important source of demand for goods from other developing countries, also appear to have fallen off sharply. In view of the need to maintain a careful control of imports in order to manage external positions, flexible and imaginative policies will have to be adopted if trade among developing countries is to be revived. Concern over the future of economic co-operation among developing countries was expressed in the Economic Declaration of the Seventh Conference of Heads of State or Government of Non-Aligned Countries and in the Quito Declaration and Plan of Action of the Latin American Economic Conference. Both of these documents also outline new measures to foster economic co-operation among developing countries.[4]

As a result of exchange rate developments and the relative economic strength of their major trading partners, the behaviour of exports in the developed market economies has differed widely from country to country. In 1983, the exports of countries for which the United States market is important, especially Canada and Japan, expanded briskly. On the other hand, United States exports contracted by about 7 per cent in volume terms. The strong appreciation of the dollar reduced the competitiveness of United States products. Drastic cut-backs in import levels by Latin American countries in balance of payments difficulties also contributed to the decline in the exports of the United States. Owing mainly to better economic performance in Europe, trade among the developed market economies is expected to increase substantially in the near future. Accordingly, these countries' exports may begin to rise more rapidly.

The priorities accorded in Eastern Europe's plans to improving external balances as well as to some recovery in economic activity could be implemented only through strong export promotion. During 1983, sharp gains were attained in spite of the fact that circumstances in these countries' main trading areas were far from favourable. In spite of sluggish import demand in Western Europe and continued external constraints in most of the developing countries, Eastern Europe's exports to the market economies rose by nearly 10 per cent in real terms, while their total exports increased by about 7 per cent. China's and the Soviet Union's export potential was adversely affected by weak energy demand in the market economies and comparatively slow growth in the domestic output of key primary goods. In these circumstances, the increases in export volume of about 5 per cent in the case of the Soviet Union and perhaps 7 per cent for China are considerable. In 1984 and 1985, in spite of an improvement in demand conditions for their exports - mainly oil and other primary commodities - China and the Soviet Union may encounter some supply constraints to increasing their exports. The Eastern European countries are expected to continue to promote their exports of manufactures vigorously.

Protectionism threatens to slow recovery in world trade

Although there are signs that international trade is beginning to revive, further protectionist actions could significantly slow down its momentum. On balance, recent protective measures have far outweighed trade-promoting actions. The latter consisted mainly of the implementation of the fourth round of annual tariff cuts negotiated in the Tokyo Round, and the easing on the part of Japan of import regulations affecting a large number of industrial and agricultural products. Regarding the Generalized System of Preferences (GSP), some improvements have been made in schemes affecting the least developed countries; on the other hand, certain categories of products from some of the more advanced developing countries have been excluded from the GSP schemes of the United States and the European Economic Community (EEC). Some progress has also been made in the implementation of the directives of the GATT Ministerial Declaration of November 1982.[5]

The drift towards protectionism of recent years appears to have accelerated in the course of 1983 and in the first months of 1984. It is estimated that over half of world trade is now subject to some form of non-tariff barrier.[6] With increasing frequency, protectionist measures have been in violation of the GATT and have been directed against specific suppliers. What is particularly worrisome is the growing conviction in some quarters that some form of managed trade is preferable to an open trading system.

It has been suggested that protectionist pressures would tend to abate with economic recovery in the main industrial countries, and that protectionist actions would therefore diminish. This hope may turn out to be illusory, since the most protected sectors appear to have permanently lost their competitiveness and are suffering from high unemployment and excess capacity, problems which will not be remedied to a significant extent with the advent of economic recovery.

In the case of new, high technology industries, where a comparative advantage can be acquired and is less a matter of factor endowment, the industrial countries are struggling to enhance their competitive position and establish a stronghold in the emerging international structure of production.[7] In the process, questions are being raised as to how far it is permissible to go in promoting these industries by means such as restricting market access, subsidies, public funding of research and development, and government procurement provisions favouring domestic suppliers.

In the case of agriculture, the defence of farmers' incomes is the primary objective of farm policy, and the right to protect domestic markets so that farm prices can rise above world levels has long been tacitly recognized by the major trading partners. However, the practice of subsidizing agricultural exports has come under increasing attack by more efficient producers. During 1983, the struggle between the United States and the EEC to gain agricultural export markets through subsidization intensified. The United States Congress appropriated substantial funds to undercut subsidized European farm sales, some of which have already been used in sales to a number of developing countries. Meanwhile, a complaint submitted by ten sugar-producing countries[8] to the GATT in early 1982 against the EEC's sugar subsidies remains unresolved.

Recent developments have tended to weaken the commitment to an open trading system. The spread of protectionism from one country to another through retaliation has gathered strength. A recent instance of this spillover effect was the action taken by the EEC in March 1984 to restrain imports from the United States in retaliation against the curbs on specialty steel decreed by the United States in July 1983. In addition, there are indications that measures originally viewed as temporary are becoming more permanent. A particularly important case is that of steel, where trade restraints appear to be following the pattern of those in the textile sector. Restrictions on trade in textiles, embodied in the Multi-Fibre Arrangement (MFA), started off as temporary. The MFA has now evolved into a more or less permanent fixture of the international scene regulating almost nine-tenths of total trade in textiles and leaving practically no room for the growth of developing country exports to the developed market economies.

A large number of trade-restricting actions have been taken in the steel sector over the last two years.[9] Nine months after entering into a voluntary export restraint agreement with the EEC, in July 1983 the United States took measures to restrict specialty steel imports from all sources for the next four years. As noted above, the EEC has decided to retaliate by restricting imports of chemicals, sporting equipment and burglar alarms from the United States. Canada has also announced reprisals. The EEC, which has in effect export restraint agreements with its main foreign suppliers, has recently imposed anti-dumping duties on steel imports from several developing countries.

Since the beginning of 1983, a large number of trade restrictions have been imposed by several industrial countries in a wide range of industrial products, including textiles and chemicals.[10] These measures fell mainly on developing country exporters.

Beyond the restrictive actions actually taken, protectionist pressures continue to increase. Between August 1982 and July 1983, the industrial countries initiated no less than one hundred cases of anti-dumping and countervailing duty actions against exports from developing countries alone.[11] While not all of them will result in the imposition of duties, such investigations tend to disrupt trade and often lead to voluntary export restraint agreements and price undertakings.

Since the July steel curbs, two new petitions have been filed which, if acted upon, would limit all carbon steel imports into the United States. One of them, in particular, could be very detrimental to developing country exporters. It proposes to limit imports to 15 per cent of the United States market (versus 22 per cent now). In all likelihood, the EEC and Japan would retain their current market share of approximately 5 per cent each, while other suppliers would have to compress theirs significantly.

Trade restrictions could become even more widespread in 1984. In January alone, petitions for protection were filed in the United States by the steel, footwear, flatware, copper and tuna fish industries. Unlike most previous petitions, which were filed under ''unfair trade'' clauses of the Trade Act and thus required a determination of dumping or subsidization on the part of specific suppliers, the new petitions are all ''escape clause'' cases seeking industry-wide protection from all competitive imports, including those traded fairly. The retaliatory measures by the EEC against the United States steel curbs may well lead to counter-retaliation, given that the affected industries in the United States are unrelated to the original EEC grievance. Moreover, the EEC has warned that if the United States takes additional restrictive action in steel in response to petitions recently filed, it would abrogate the 1982 export restraint agreement. This could lead to a new round of protective measures in the steel sector and may escalate the chain of retaliatory and counter-retaliatory reactions.

Thus 1984 is shaping up as a critical year for the future course of trade policies in the major industrial countries. If Governments are successful in resisting the pressures for further protection stemming from high sectoral rates of unemployment, chances are that a change in mood could be brought about that is conducive to a gradual improvement in the trade climate. If, on the contrary, protectionist pressures are translated into further actions, the drift towards a managed system of world trade will be given an important impetus.

Partial recovery in primary commodity prices

In the course of 1983, the prices for internationally traded non-fuel primary commodities began to recover from the sharp slide of the preceding two years (see table II-2).

Table II-2. Rates of change in the prices[a] of internationally traded commodities, 1981-1985

(Percentage)

	1981	1982	1983	1984[b]	1985[b]
Non-fuel primary commodities	-15.6	-16.1	5.8	6	1
Food	-21.4	-30.1	6.3	1	-
Tropical beverages	-18.9	-4.4	5.8	11	-3
Vegetable oils and oilseeds	-3.2	-23.0	23.4	10	-12
Agricultural raw materials	-13.0	-12.9	7.0	6	6
Minerals, ores and metals	-12.3	-12.7	-	2	8
Crude petroleum	11.5	-5.6	-11.1	-	5
Manufactures					
Exported by developed market economies	-6.0	-2.1	-4.4	6	6
Exported by developing countries	0.0	-11.0	-5.0[c]	6	6

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on United Nations Conference on Trade and Development, *Monthly Commodity Price Bulletin*; United Nations, *Monthly Bulletin of Statistics*; and information provided by the National Institute of Economic and Social Research (London).

[a] Expressed in dollars.
[b] Forecasts.
[c] Preliminary estimates.

While some prices have experienced strong rebounds, other prices have remained depressed. On average, the upswing in prices can be characterized as moderate, and price increases have been much smaller than the preceding price declines. Given the expectation of a relatively weak recovery in Europe and Japan, the excess capacity prevailing in many markets for industrial raw materials and the large stocks of some commodities, prices are not likely to rise significantly in 1984-1985. As a result, by the middle of the current decade, prices on the average could still be about 20 per cent below their levels in 1980.

These forecasts for commodity price changes have important implications for both developing countries and developed market economies. For developing countries, they mean that export earnings are unlikely to receive a boost from substantial price increases. Therefore, the payments problems of countries may not be eased sufficiently to prevent renewed debt-servicing crises or protracted stagnation in their import levels. As regards the developed market economies, moderate increases in commodity prices would provide some room for more growth-oriented policies without threatening the gains already made against inflation.

As compared to their average levels in 1982, the prices for minerals, ores and metals have remained practically unchanged. With the exception of aluminium, the prices for most of these commodities continue to be depressed by a large overhang of producers' inventories and by an excess of productive capacity over demand. If, as presently expected, the pace of overall recovery will remain moderate, these problems are unlikely to be overcome in the next two years; therefore, prices are not expected to improve significantly.

The prices of agricultural raw materials have fared somewhat better, but the price advance for the group as a whole has been modest. The increase in prices has concentrated largely in two commodities (cotton and rubber). Rubber prices have been bid up by the strong revival of the automobile industry in North America. In the case of cotton, an acreage reduction programme in the United States and poor crops in some other major producing countries contributed to the upward price movement. In 1984-1985, for the group as a whole, competition from synthetics, large stocks and substantial increases in production should help moderate pressures on prices arising from the continued strengthening of demand.

The prices of grains and vegetable oils and oilseeds rose during 1983, in some cases markedly. Supplies were affected by poor weather conditions and the adoption of an acreage reduction policy in the United States in the wake of the sharp price declines of 1981-1982. As this acreage is returned to cultivation and assuming more normal weather, price increases should moderate in the next two years. In fact, grain prices began to ease in the closing months of 1983, and the decline was continuing in early 1984.

After several years of decline, the prices for sugar and tropical beverages have been rising for several months. In the case of cocoa, this is due largely to bush fires and disease, which affected supplies in the major African producers, and to smaller crops in Brazil. As for other commodities, low prices in recent years have discouraged production, so that there is now a better balance between production and demand. With the exception of tea, however, stocks are still large and could limit the increase in prices in the near future.

As a result of weak demand and the draw-down of inventories in the industrial countries, oil prices declined in the first quarter of 1983 and have remained stable since then. Oil consumption in the developed market economies has not yet responded to the pick-up in economic activity. In fact, the trend towards declining consumption prompted by past price increases has continued, albeit at a slowing pace. Consumption in developing countries has fallen sharply owing to depressed economic conditions. Only the adoption of production quotas by OPEC member countries has prevented further price declines.

In 1984, the demand for oil in the developed market economies is expected to begin to increase for the first time in several years. In addition, some recovery in consumption in developing countries could result from the somewhat higher rates of economic growth forecast for 1984-1985. Therefore, oil prices are unlikely to fall further and, by 1985, they could begin to rise at a rate roughly similar to the average rate of inflation in the developed market economies. As for the immediate future, increases in demand are likely to be met by rising supplies, given the large excess capacity that exists in producing countries and the need to earn foreign exchange of many oil producers which are facing tight balance-of-payments situations.

Reflecting the strong appreciation of the dollar, the prices for internationally traded manufactures declined in dollar terms in 1982 and 1983. Even in domestic currencies, the increase in these prices tended to moderate together with domestic inflation in the main producing countries. While underlying cost factors should remain largely unchanged during 1984-1985, dollar prices could begin to rise once again as the dollar depreciates against other major currencies.[12]

Little progress has been made to improve international institutions to stabilize the prices of primary commodities. In particular, the Common Fund has not yet been ratified by a sufficient number of countries so that it can go into operation. It is unlikely that commodity prices will experience a generalized decline in the next couple of years. But if this period is not used to improve international price stabilizing mechanisms, commodity prices and the export earnings of developing countries could continue to exhibit very wide fluctuations in the future.

Effects of international price changes on the terms of trade

Terms-of-trade movements since early 1983 have been quite different from those of previous years. For the first time since 1977, the terms of trade of the net energy-importing developing countries have been improving. International price movements have been favourable to these countries: the prices of non-oil primary commodities have been on an uptrend, and the prices for oil and imported manufactures have fallen. However, most of the terms-of-trade gains for this group of countries during the current recovery may have already taken place. While primary commodity prices may continue to rise, owing to dollar depreciation the dollar prices of manufactures imported from the developed market economies are likely to increase just as rapidly. Since nominal oil prices are expected to stay largely unchanged until 1985, the terms of trade of the energy-importing countries may improve in 1984, but by considerably less than in 1983. By 1985, renewed terms-of-trade losses are possible, but they are likely to be relatively small.

If the terms of trade of the energy-importing countries effectively do not continue to improve, the burden of alleviating external payments constraints would fall on a vigorous increase in export volume. But for many countries whose exports are heavily dependent on primary commodities, this is very unlikely to take place. World demand for food and beverages is unresponsive to increases in income. And increases in the exports of industrial raw materials may be restrained by relatively weak demand conditions in some developed market economies and in developing countries.

The change in direction in the price of oil has adversely affected the two groups of energy-exporting developing countries. Worsening terms of trade have contributed to the precarious balance-of-payments situation of most of these countries. For 1984, stable oil prices and rising prices for manufactures spell a further worsening in their terms of trade. Even if oil prices were to rise somewhat in 1985, the positive impact on the terms of trade is likely to be offset by the negative effect of higher prices for imported manufactures.

As with the energy-importing countries, in the near future the energy exporters cannot count on price increases to improve their external payments situation. Most of the surplus countries have large reserves of foreign exchange to draw upon. Thus, they can withstand temporary current account deficits without having to resort to significant net borrowing. However, many countries in the capital-importing group are facing severe debt-servicing difficulties and tight balance of payments situations. Since energy exports are not expected to rise very rapidly, these difficulties are unlikely to be eased except through continued cautious import policies and restrained growth.

The developed market economies have benefited from recent international price movements. Since, with the exception of the United Kingdom and Norway, the developed market economies are net energy importers, the sharp fall in oil prices has had a favourable effect on their terms of trade. In spite of declines in the dollar prices of exported manufactures and moderate increases in the prices of primary commodity imports, their terms of trade have improved. Relative international price changes are expected to continue to favour the developed market economies, whose terms of trade may continue to improve in 1984-1985.

Estimates of price changes in the external trade of the centrally planned economies show a sharp dichotomy between developments in intra-group trade as distinct from those observed in world markets. Regarding intra-CMEA relations, for a number of years now, there have been gradual increases in the relative cost of fuels and raw materials. In 1983, the forward absorption of past changes in world market prices into the intra-CMEA trade price structure, under the formula of averaging world prices of the preceding five years, resulted in a further shift in the regional terms of trade of the Eastern European countries, which are net importers of fuels and raw materials. Since most of the price movements occurred in trade with the Soviet Union, this country's terms of trade with the CMEA improved. By contrast, in trade with the market economies, there appears to have been a worsening in the terms of trade for both Eastern Europe and the USSR, attributed in large part to weak export prices for fuels and for the raw materials and foodstuffs exported by the Eastern European countries to the market economies. China's terms of trade appear to have remained largely unchanged for the past 12 to 18 months.

In the coming two years, the net importers of liquid fuels are likely to incur a further worsening in the terms of trade with CMEA partners. Changes in the terms of trade with the market economies may be relatively small, in the light of the limited changes in international prices that are foreseen at the present moment. The outlook for the next two years or so is therefore for a worsening in the terms of trade of Eastern Europe, while China's remain relatively unchanged, and those of the Soviet Union experience some gains.

International payments

Major current account developments

The principal recent shifts in current accounts in the world economy have been the large swing into deficit in the capital-surplus developing countries, the sharp reduction in the deficits of the capital-importing developing countries, and a very significant increase in both the deficit of the United States and the surpluses of other major industrial countries, particularly Japan and the Federal Republic of Germany. Expectations are that this broad configuration of current account positions will remain largely unchanged in the near future, except that the United States' deficit could become substantially larger while the combined surplus of the other developed market economies may also increase from current levels (see tables II-3 and II-6).

At the present time, current account positions are not a constraint to rising levels of economic activity in most developed market economies. With the exception of the United States, where current account deficits are self-financing, most of the other major industrial countries, and particularly the Federal Republic of Germany and Japan, are in a strong surplus position. By contrast, the state of the current account is a severe constraint to economic expansion in most developing countries and centrally planned economies. Since 1981, the unavailability of financing has forced the capital-importing developing countries to reduce their current account deficits very sharply. In 1984, external payments difficulties are expected to remain strong.

The turn-around in the current account of the capital-surplus countries since 1980 has been spectacular. These countries, which since the early 1970s had been important contributors to the supply of international loanable funds, have now begun to draw down their accumulated international assets. Despite lower export earnings, the other net energy exporters managed to reduce their combined current account deficit quite substantially, essentially through compressing imports. The contraction in the current account deficit of the net energy-importing developing countries was unexpectedly sharp. These countries have

Table II-3. World balance of payments on current account,[a] by country groups, 1980-1984

(Billions of dollars)

Country group	1980	1981	1982	1983[b]	1984[c]
Developed market economies	-37.8	- 6.6	- 7.4	2	-15.5
Major industrial countries	-11.9	19.2	15.1	6.5	-20
Other countries	-25.9	-25.7	-22.6	-4.5	4.5
Developing countries	36.5	-37.5	-96.2	-67.5	-67
Capital-surplus countries	101.7	60.3	3.9	-6.5	-11
Other net energy exporters	1.5	-25.7	-32.3	-11	-12
Net energy importers	-66.7	-72.1	-67.8	-50	-44
Centrally planned economies[d]	0.9	3.5	16.8	18.5	17.5
China	-1.3	-	3.1	2	-1
Eastern Europe	-5.8	-2.7	4.4	5.5	6.5
USSR	8.0	6.2	9.3	11	12
Residual balance[e]	0.4	40.6	86.8	47	65

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics*; other official national and international sources; and forecasts by the Secretariat.

[a] Excluding government transfers.
[b] Preliminary estimates rounded to the nearest half billion dollars.
[c] Forecast.
[d] Trade balances only.
[e] The world current account discrepancy reflects timing asymmetries, the balance on services of the centrally planned economies, errors in trade balances and under-recording in the receipts of services. Particularly large sources of discrepancy are investment income channelled through off-shore financial centres and non-factor services exported by the developed market economies to OPEC member countries. For a discussion of the sources of discrepancy in the world services balance, see Organisation for Economic Co-operation and Development, *OECD Economic Outlook*, No. 34 (December 1983), pp. 140-142.

already achieved a substantial degree of adjustment in their external accounts. When deflated by import prices, their combined deficit in real terms is now at levels that are not much larger than those prevailing before the oil price increases of the early 1970s.

Since 1981, the centrally planned economies of Eastern Europe have been under strong adjustment pressures. During this period they have succeeded in converting a current account deficit into a growing surplus. This has enabled them to reduce their external debt for two consecutive years. The Soviet Union, on the other hand, has benefited from terms-of-trade gains and has recorded increasing current account surpluses. The surpluses of both the Eastern European countries and the Soviet Union are expected to be even larger in 1984. Deliberate policies to increase imports account for the decline in China's current account surplus observed in 1983 and for a further fall expected in 1984.

Intense current account adjustment by developing countries

The capital-importing developing countries underwent an unusually large adjustment in their balance of payments in 1983, reducing their aggregate deficit on current account for the first time in the 1980s. The size of the change, according to most recently available data, was much larger than anticipated.[13] Adjustment policies have now been adopted throughout the developing world. In the energy-importing countries, the trend toward lower current account deficits, which began in 1982, accelerated dramatically in 1983. For the deficit energy exporters, 1983 marked a sharp reversal in current account trends. Up to 1982, their combined current account had deteriorated to what appeared to be an unsustainable level.

The current account improvements in the capital-importing developing countries in 1983 were mainly the result of deliberate policies to reduce import levels. In the energy-importing countries other favourable factors were better terms of trade and a surge in exports, particularly exports of manufactures to North America. With economic recovery in the developed market economies gaining strength, exports could expand somewhat faster in 1984 than in 1983. On the other hand, the imports of many countries will continue to be constrained by external payments difficulties. In addition, in a number of countries improved performance in the agricultural and energy sectors in 1983 should lessen the need for food and petroleum imports in 1984, further contributing to lower current account deficits. By contrast, the drought-affected countries of Africa will need to increase their imports of food, and this will make further adjustment of their external positions very difficult.

For the capital-surplus countries, 1983 was the first year since before the 1970s that their aggregate current account position moved into deficit. The deficit arose primarily from a fall in the value of their exports by over 15 per cent since 1982. This was the third consecutive year of falling export earnings for this grouping; in fact, 1983 exports were only 60 per cent of their 1980 value. Certain countries of this grouping, most prominently Saudi Arabia, were in a position to absorb a disproportionate share of the cutback in oil production agreed to in March 1983 by OPEC member countries. Having accumulated substantial foreign exchange reserves and other foreign assets in the past, most countries of the group have been able to finance their export shortfalls without difficulty, for example, by drawing down deposits in international commercial banks. In 1984, the current account deficit of this group of countries as a whole may become larger, owing mainly to a further worsening of the terms of trade.

Capital flows to developing countries recede sharply

A major cause of the need to adjust external positions rapidly in the capital-importing developing countries has been the drying up of external financing from private sources, particularly of bank lending. As a result, countries have been forced to reduce import levels in an attempt to restore equilibrium in their external payments. Current attitudes of both lenders and borrowers suggest that, for the foreseeable future, these flows are unlikely to resume their strong upward movement of the 1970s.

As can be seen in table II-4, there has been a sharp decline in private lending to developing countries, particularly on a long- or medium-term basis. Direct foreign investment has also fallen considerably. The loss of confidence by the private banks in developing country borrowers has had a pervasive influence on lending to most countries. Indeed,

Table II-4. Financing the current account deficit of capital-importing developing countries,[a] 1978-1983

(Billions of dollars)

	1978	1979	1980	1981	1982[b]	1983[c]
Current account balance	-49.1	-49.9	-60.6	-91.4	-94.2	-57
Net external private finance	38.0	40.3	38.7	48.3	27.5	22
Direct investment	7.4	9.8	9.9	14.1	11.8	9
Long-term credits	29.1	23.4	22.8	40.9	29.7	25
Short-term capital[d]	1.5	7.2	6.0	-6.6	-14.0	-12
Net external official finance	22.4	29.6	38.7	40.4	42.0	42
Official long-term resources	18.9	25.8	30.1	31.7	30.0	31
Unrequited transfers[e]	6.4	11.5	12.0	12.6	10.7	11
Long-term credits	12.5	14.3	18.1	19.2	19.3	20
Payments-related official credit	3.5	3.8	8.6	8.7	12.0	11
Net use of IMF credit	-0.4	0.5	1.9	5.4	5.5	11
Other official credit[f]	4.0	3.3	6.7	3.2	6.5	-
Recorded arrears	0.8	-0.1	-	0.5	7.9	-2
Use of reserves[g]	-12.1	-19.9	-16.9	2.3	16.8	-5

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *Balance of Payments Statistics* and *International Financial Statistics*; World Bank, *World Debt Tables*; national data and other sources.

[a] Sample of 86 developing countries accounting for almost 95 per cent of the aggregate current account deficit of the capital-importing developing countries.
[b] Partially estimated.
[c] Preliminary Secretariat estimates based on incomplete data, particularly with regard to the timing of the flows arising from various debt-restructuring agreements in 1983.
[d] Includes errors and omissions.
[e] Includes SDR allocations, 1979-1981.
[f] Includes IMF Trust Fund (to 1981) and subsidy accounts, STABEX, and other multilateral and bilateral payments finance, including short-term bridging credits.
[g] Minus sign indicates additions to reserves.

a good share of the recent gross international bank lending to developing countries was arranged as part of debt-restructuring packages and can thus be considered to have been in a sense involuntary. In 1983, such loans accounted for $14 billion out of a total of $32 billion in gross medium- and long-term bank credits to the capital-importing countries. The implicit $18 billion in voluntary gross lending in 1983 may be contrasted with the $41 billion lent in 1982 and $50 billion in 1981.[14]

Not only have private bank flows declined in volume, but their cost has remained high. Although base interest rates have fallen since 1982, they are still very high when compared to expected trends in export prices. Moreover, spreads over base rates have tended to widen, reflecting a higher subjective assessment of risk on the part of lenders. In recent months, though, there has been some decline in spreads, particularly on restructured debts. Another factor that has served to maintain borrowing costs high for developing countries in debt-servicing difficulties were the special fees charged by banks for rescheduling their debt.

A further dimension of the difficulty developing countries have recently faced in mobilizing private financial resources has been in the behaviour of short-term capital flows. From 1981 to 1983, the capital-importing developing countries as a whole recorded a large net outflow of short-term capital (see table II-4). Moreover, up to 1982, these net outflows coincided with an extremely rapid build-up in gross short-term inflows in the form of borrowing from international banks. The implied gross outflow of short-term capital from these countries was thus extremely large. This outflow represented many and widespread private decisions in developing countries to transfer personal wealth on a temporary basis to the developed market economies, particularly the United States.

The decline in private flows over the past two years has not been compensated by increases in official financing. Although some categories of official flows have risen, in the aggregate these flows have remained virtually stagnant since 1980 despite the protracted payments crisis of recent years.

This is not to deny that certain efforts have been made, especially in 1983, to increase some categories of official resource transfers in response to current needs. In particular, the World Bank and regional development banks did adopt measures to alleviate the payments difficulties of borrowing countries. For example, they increased their share of total project financing and accelerated the disbursement of funds. The World Bank, as part of its Special Assistance Programme, also sought to expand its structural adjustment lending and programme lending in support of sectoral adjustment.[15] On the other hand, these departures from past practice must be financed out of the regular resources of these institutions, which implies that they must either restrict other lending programmes or acquire new capital resources. One capital expansion under negotiation in 1984 is the selective capital increase of the World Bank, which provides an opportunity for a significant increase in its resources.

Official development assistance (ODA) has behaved erratically in recent years. In real terms, the ODA receipts of developing countries were practically unchanged in 1981 and dropped sharply in 1982. Aid flows from DAC member countries decreased in 1982, as did concessional financial co-operation from OPEC member countries.[16] There were no indications that a significant overall increase in the sum of these flows had taken place in 1983.

As regards multilateral development co-operation, recent trends have become disquieting. Following a decade of rapid expansion averaging 22.5 per cent per annum, net multilateral disbursements in the 1980s are going through a phase of slow growth and, in some cases, absolute stagnation. Difficulties in arranging adequate levels of future multilateral flows have been only imperfectly resolved. Major donors have agreed that the delayed seventh replenishment of the International Development Association should be at a level of $9 billion for three years, in contrast to the initially agreed $12 billion for three years (and later extended to a fourth year) under the sixth replenishment. The tentative agreement on the second replenishment of the International Fund for Agricultural Development reached in March 1984 makes it virtually certain that contributions during the next three years (1985-1987) will not exceed those originally pledged for 1981-1983 (and then extended to 1984). Pledges to the World Food Programme for the 1985-1986 biennium amounted to less than 50 per cent of its target of $1.35 billion. With respect to operational activities for development funded through the United Nations system, the favourable results of the 1983 United Nations Pledging Conference for Development Activities raised hopes that the negative trends of recent years might be finally arrested.

Official and officially guaranteed export credits have also lost their former dynamism. Here, however, a prime adverse factor has been the need of developing countries to cut back on their imports. To the degree that imports recover, the provision of officially supported export credits may increase *pari passu*. This notwithstanding, the concessional element embodied in official export credits will be reduced. The countries participating in the OECD Arrangement on Guidelines for Officially Supported Export Credits agreed in October 1983 to phase out by July 1986 all subsidies inherent in existing interest rates on export credits.[17] Under the existing Arrangement, minimum interest rates are set for credits of differing maturities for different groups of countries, with the lowest income countries now receiving the most favourable rates.

International reserves, the first line of defence in a balance-of-payments crisis, were extensively drawn down in 1981 and 1982. Since then, the erosion of reserve levels in the capital-importing developing countries as a whole has been halted, and in many countries a reserve rebuilding process has begun. On the other hand, certain other countries with unresolved external debt problems have had to continue drawing down their reserves. Furthermore, about 15 per cent of the energy-importing countries ended 1983 with reserves insufficient to purchase even one month's imports,[18] despite import compression in 1983 as well as in previous years. Indeed, less than half of the energy importers had reserves which met the minimum rule-of-thumb level of three months' import coverage. The energy-importing countries are thus expected to rebuild their reserve levels to some extent in 1984. Even though beginning at a high level in some cases, the reserve levels of the deficit energy-exporting countries have also been heavily drawn down during the recent crisis. Therefore, some rebuilding of reserves in these countries is also likely to take place in 1984.

In recent years, balance-of-payments financing from the IMF has expanded considerably (see table II-5). Nevertheless, in 1983 official balance-of-payments credit as a whole

Table II-5. Net flow of IMF lending to the capital-importing developing countries, 1978-1983

(Billions of dollars)

	1978	1979	1980	1981	1982	1983
Low conditionality flows	0.2	0.2	1.3	-	1.4	2.2
Buffer stock financing	-	-	-	-	0.1	0.3
Compensatory financing	0.2	0.2	0.3	0.6	1.7	2.0
Oil Facility	-0.9	-0.6	-0.7	-0.7	-0.4	-0.1
Trust Fund	0.9	0.7	1.6	0.1	-	-0.1
Higher conditionality flows	-	1.0	2.3	5.7	4.2	9.1
Credit tranche drawings	-0.1	0.7	1.5	3.3	1.9	4.2
Extended Facility drawings	0.1	0.3	0.7	2.4	2.3	4.9
Total flows	0.2	1.2	3.6	5.7	5.7	11.3

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics*.

actually fell, since declines occurred in other forms of official payments finance. In particular, the bridging loans arranged in 1982 by countries in debt-servicing difficulties with the Bank for International Settlements and national authorities were replaced to a large extent by formal programmes with the IMF.[19]

The provision of support to countries experiencing debt-servicing difficulties assumed an important role in IMF lending in 1983. Of the 40 stand-by or extended financing arrangements between the IMF and developing countries in existence at the end of 1983, over half were with countries which had found it necessary to seek a restructuring of their private or public debts since 1982. Furthermore, as many of the countries concerned had relatively large payments financing requirements, countries in debt-related difficulties accounted together for about two thirds of the $22 billion of total lending agreements in effect.

The overall predominance of lending through stand-by or extended arrangements - as opposed to lending through relatively automatic, low-conditionality facilities - intensified in 1983. The two low-conditionality facilities - the Buffer Stock Financing Facility and the Compensatory Financing Facility (CFF) - increased their level of lending considerably. However, the absolute amounts of financing provided through these facilities remain relatively small.[20]

IMF lending under conditional arrangements is provided in support of balance-of-payments adjustment programmes. In view of the persistance of many developing countries' adjustment needs, numerous IMF lending agreements were renewed in 1983. As the adjustment process continues in an international trade and financial environment that is less supportive than would be desired, it appears likely that many of the 27 IMF lending agreements with developing countries which are set to expire in 1984 will also have to be renewed.

The ability of the IMF to increase its net lending in 1984 was assured by the end of November 1983 when the requisite minimum number of member countries of the Fund consented to increases in their quotas under the Eighth General Review of Quotas. Interim financing of SDR 3 billion was arranged with the Bank for International Settlements, which increases the short-run financial flexibility of the Fund. Its potential recourse to financing was also improved by the coming into force of the revised and enlarged General Arrangements to Borrow and the parallel arrangement between the Fund and Saudi Arabia.

None the less, decisions taken by the Executive Board in early January 1984 may restrict the degree to which the IMF can lend to member countries in 1984. With the increase in quotas, all member countries would have been eligible for additional borrowing from the Fund. However, the limit to outstanding borrowings was reduced from 600 per cent of quota to 408 or 500 per cent, depending on the seriousness of the country's balance-of-payments needs and the strength of its adjustment efforts. Annual limits were reduced from 150 per cent of quota to 102 or 125 per cent. At the same time, maximum allowable drawings from the CFF and the Buffer Stock Financing Facility as a percentage of quota were also scaled down.[21] Although the Fund retains the ability to exceed these limits in exceptional circumstances, lending is expected to remain within the established guidelines. Furthermore, the continuation of the Fund's ability to lend up to even these lowered multiples of quota is not assured, as extension of the Enlarged Access Policy itself beyond the end of 1984 requires a further decision by the Executive Board.

One source of compensatory finance for export fluctuations which has served as a significant form of highly concessional payments support for many generally small and low-income developing countries is the STABEX scheme, operated by the EEC for the benefit of the 63 associated African, Caribbean and Pacific (ACP) countries. Loans and grants under the scheme in 1983 fell to about $58 million, compared to transfers of $187 million in 1982 and $124 million in 1981.[22] Despite a special effort made in May 1982 to supplement its resources, in recent years STABEX has not had enough resources to meet all qualifying applications. The future conditions and financing of the scheme are now being decided as part of the ACP-EEC negotiations begun in October 1983 for a new agreement to succeed Lomé II, the most recent ACP-EEC co-operation agreement.

Thus the availability of balance of payments financing, particularly of a compensatory nature, is still very inadequate. As a result, the development process continues to be very vulnerable to the international effects of the business cycle in the developed market economies.

Large shifts in current accounts among the developed market economies

The trends in current accounts since 1981 in the developed market economies became considerably more pronounced during 1983. Largely as a result of differing cyclical positions and the continued appreciation of the dollar, the current account deficit of the United States increased sharply, while the combined balance of the remaining countries swung from a small deficit in 1982 to a large surplus in 1983 (see table II-6).

The major factor behind the increase in the United States' deficit in recent years has been a deterioration in the real trade balance. In 1983, real imports rose very rapidly, while export volumes contracted. In spite of a lower oil import bill and improvements in the terms of trade, the trade deficit is estimated to have risen by over $23.5 billion. The traditional surplus on services also appears to have declined by almost $3 billion, owing largely to lower nominal interest rates and a rapid erosion in the country's net creditor position.[23] The continuation of massive inflows of capital, mainly in the form of portfolio investments, would transform the United States into a net international debtor.

In the other developed market economies combined, there was a strong swing from a small aggregate current account deficit to a considerable surplus. With the exception of the United Kingdom and a few small economies, the shift was generalized. Improvements in competitive positions, relatively weak domestic demand conditions and better terms of trade all worked in the direction of substantially enlarging the aggregate trade surplus of these countries. In addition, their combined deficit on services and private transfers declined, also contributing towards a larger current account surplus.

The current account surplus of Japan exhibited a particularly strong increase in 1983. Since 1980, the shift into surplus of the Japanese current account has exceeded $30 billion. Most of the swing has been due to a sharp increase in the trade surplus, with more moderate declines occurring in the deficit on invisibles. Nearly all the increases in the trade surplus

Table II-6. Developed market economies: balance of payments on current account[a], 1980-1984

(Billions of dollars)

Country or country group	1980	1981	1982	1983[b]	1984[c]
Developed market economies	-37.8	-6.6	-7.4	2	-15.5
excluding United States	-44.8	-17.8	-3.9	32	54.5
Major industrial countries	-11.9	19.2	15.1	6.5	-20
Canada	-1.3	-5.3	2.0	3	3
France	-2.5	-2.8	-9.5	-3	-
Germany, Federal Republic of	-8.0	0.7	10.6	12	14
Italy	-9.7	-7.9	-5.2	-1.5	-
Japan	-9.5	6.2	8.1	21	28
United Kingdom	12.0	17.1	12.5	5	5
United States	7.0	11.2	-3.5	-30	-70
Other countries	-25.9	-25.7	-22.6	-4.5	4.5
Surplus countries[d]	-0.7	5.5	9.4	10	12.5
Others	-25.2	-31.2	-31.9	-14.5	-8.0

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics*, and forecasts of the United Nations Secretariat.

[a] Excluding government unrequited transfers.
[b] Preliminary estimates rounded to the nearest half billion dollars.
[c] Forecast.
[d] Netherlands, Norway and Switzerland.

were due to volume effects. In fact, between 1980 and 1983, Japan's export volume expanded by nearly 18 per cent, while its imports fell by more than 3.5 per cent. It should be added that export growth would have probably been even stronger had it not been for the trade restrictions imposed on Japanese products by its major trading partners.

In the Federal Republic of Germany, a moderate decline in the invisibles deficit caused the current account surplus to rise somewhat in 1983. The trade surplus remained roughly constant as a result of compensating price and volume movements. Though the swing in the German current account since 1980 has been less than in Japan's, it has none the less been quite significant (about $20 billion).

The trends observed in current accounts among the developed market economies in the past two years are expected to become accentuated in 1984. The current account deficit of the United States is expected to increase by about $40 billion, with the combined surplus of the other countries rising by over $20 billion. Economic activity is expected to be very buoyant in the United States and considerably less so in other countries. In addition, the lagged effects of the strong appreciation of the dollar in the past three years are likely to continue to be felt throughout 1984. As a result of both of these forces, while real imports rise strongly and real exports continue to stagnate in the United States, export volumes should be comparatively stronger than import volumes in other industrial countries.

The short-run impact of dollar depreciation would tend to exacerbate the situation. While exchange rate changes have a delayed impact on quantities traded, their price effects are felt rapidly. Countries whose currencies depreciate tend to experience worsening terms of trade, since import prices in domestic currency increase more than export prices (the so-called J-curve effect). Conversely, the short-term consequence of currency appreciation is usually an improvement in the terms of trade. Therefore, were the dollar to depreciate, the short-term impact would be to increase the trade deficit of the United States and the trade surpluses of countries with appreciating currencies (most likely the Federal Republic of Germany and Japan).

Exchange rate instability among major currencies

During 1983, exchange rates continued to fluctuate widely (see table II-7). The salient feature of exchange rate movements was the continued strength of the dollar. Despite the United States' growing current account deficit, the dollar continued to appreciate for the third consecutive year, albeit less than in the preceding two years. In the early months of 1984, there were some indications that there might be a reversal in this trend, since the dollar began to decline against other major currencies. During 1983, however, the excess demand for the dollar resulting from net capital inflows that far exceeded the current account deficit caused the dollar to appreciate against most other major currencies. The dollar also appreciated on a real effective basis, that is, after differentials in inflation rates among major trading partners are taken into account in estimating average changes in exchange rates. This indicates that the average nominal appreciation of the dollar was greater than the percentage that would have been necessary to offset a lower rate of inflation in the United States than in its major trading partners.

For the past three years, the dollar has been sustained by strong capital flows into the United States (see table II-8). To a large extent, these flows have been stimulated by the persistence of an interest rate differential in favour of dollar-denominated assets in nominal terms. In addition, expectations as to the rate of inflation in the United States are likely to have been revised sharply downwards. Not only has inflation in the United States receded rapidly, but the monetary authorities appear to be less willing to accommodate a new surge in inflation. Therefore, interest rate differentials in favour of the dollar may have more than compensated for differentials in expected rates of inflation, giving rise to expectations that the dollar would appreciate and to flows of capital into dollar-denominated assets. More generally, capital flows were attracted to the United States by

Table II-7. Selected developed market economies: exchange rate movements, 1981-1983

(Year-end percentage change)

Country	Spot exchange rate against $US			Nominal effective exchange rate[a]			Real effective exchange rate[b]		
	1981	1982	1983	1981	1982	1983	1981	1982	1983
Canada	0.7	-3.7	-1.2	3.4	-2.2	0.9	4.6	-2.3	3.0
France	-27.3	-16.9	-19.4	-6.9	-5.7	-7.5	-3.2	-2.2	-1.3
Germany, Federal Republic of	-15.1	-5.4	-12.7	2.1	7.2	-	-0.9	2.7	-3.3
Italy	-28.9	-14.2	-17.4	-10.2	-2.5	-4.4	-4.7	1.7	-0.3
Japan	-8.3	-6.8	1.2	1.8	-3.9	8.9	-6.6	-8.8	-3.7
United Kingdom	-20.0	-14.4	-10.1	-8.0	-4.7	-1.3	-6.9	-3.2	-0.9
United States	.	.	.	9.0	10.9	6.0	10.4	10.2	3.4
Belgium	-22.0	-21.9	-15.1	-3.1	-9.6	-2.8	-5.0	-8.0	-2.2
Denmark	-21.8	-14.4	-17.7	-3.8	-1.0	-4.2	-2.6	0.0	-3.4
Netherlands	-15.9	-6.3	-14.3	1.4	5.6	-1.5	2.2	3.6	-2.2
Switzerland	-1.9	-10.9	-8.5	15.0	-1.2	6.0	9.8	-3.7	3.5

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics*; and Morgan Guaranty Trust Company of New York, *World Financial Markets*.

[a] Based on 1980 weights derived from bilateral trade in manufactures with 15 major trading partners.
[b] Nominal effective exchange rate adjusted for differential rate of change in wholesale prices of manufactures.

favourable expectations among investors regarding its economic prospects. The dollar was also strengthened by capital flight seeking a safe haven from other parts of the world, including certain developing countries.

In the near future, it is unclear to what extent capital inflows will be large enough to offset the net outflows of dollars stemming from current account transactions. As already noted, the current account deficit is expected to rise markedly in 1984. Therefore, considerably larger inflows of capital would be needed to sustain the dollar. This would probably require a widening of interest rate differentials in favour of dollar-denominated assets. Even if this were the case, the rapid increase in the current account deficit of the United States, and rising surpluses in the Federal Republic of Germany and Japan, could cause a significant change in perceptions about the strength of the dollar *vis-à-vis* other major currencies (particularly the deutsche mark and the yen) and a change in the direction of short-term capital flows. If so, the dollar could depreciate substantially.

Table II-8. Major developed market economies: net short-term and long-term capital flows, 1980-1983

(Billions of dollars)

Country or country group	Short-term capital flow (net)			Long-term capital flow (net)			Total capital flows plus errors and omissions (net)		
	1981	1982	1983[a]	1981	1982	1983[a]	1981	1982	1983[a]
Major industrial countries	5.5	1.3	57.0	-6.0	-20.4	-24.9	16.0	16.8	36.0
Canada	12.7	-6.7	2.3	0.4	5.8	2.1	5.5	-4.2	0.7
France	11.1	8.3	5.0	-6.7	1.1	7.6	2.1	8.4	11.8
Germany, Federal Republic of	2.7	6.6	-1.0	3.7	-6.9	-2.3	7.8	-0.6	-0.8
Italy	-	-4.3	7.2	8.1	4.5	1.2	7.5	1.1	7.8
Japan	4.9	-	-2.4	-6.4	-16.3	-19.9	-1.1	-11.6	-19.8
United Kingdom	3.6	15.6	6.5	-18.1	-15.0	-8.9	-13.5	-5.8	-8.6
United States	-29.5	-18.2	39.4	13.0	6.4	-4.7	7.7	29.5	44.9

Source: International Monetary Fund, *Balance of Payments Statistics*, and *International Financial Statistics*.

[a] Based on data for the three quarters (Federal Republic of Germany, Japan, United Kingdom and United States) or the first half of the year. All figures are annualized

The situation is now reminiscent of that of the middle and late 1970s, when the United States saw its deficit increase rapidly while the Federal Republic of Germany and Japan were running large and increasing surpluses. During the earlier period, large current account deficits in the United States were accompanied by an erosion of confidence in the dollar, outflows of short-term capital, and a steady depreciation in the dollar against other major currencies. By contrast, as already noted, since 1981 capital flows into the United States have been massive. As shown in table II-8, while direct investments and long-term portfolio flows were dominant up to 1982, more recently they have increasingly taken the form of short-term flows, mostly bank deposits and purchases of United States Treasury bills. These flows could be easily reversed if further increases in the United States' current account deficit caused investors to lose confidence in the dollar. Therefore, the dollar could come under sudden and intense downward pressures.

Since short-term capital flows can be destabilizing, the possibility of protracted dollar weakness and overshooting in a downward direction (from the point of view of changes in relative trade prices) is a very real one. However, in the recent past widely held expectations of an impending dollar depreciation have been confounded, and capital flows into the United States continued at a strong pace even in the face of a clear overvaluation of the dollar from the point of view of trade fundamentals. Therefore, while everything indicates that there should be a fall in the international value of the dollar beginning in 1984, it is difficult to predict the extent to which the dollar might fall or how long the correction could take.

Further improvement in the external payments position of the centrally planned economies

The priority of the national economic plans of the majority of the Eastern European centrally planned economies remains the holding down of domestic absorption, containing imports and promoting exports, in order to improve external balances with both the transferable rouble and the convertible currency trading areas. This policy goal was fairly closely adhered to in 1983, even though actual circumstances in the course of the year, connected with a surge in investment and an upturn in industrial activity, diverged somewhat from the major assumptions underlying the plans.

The policies that have been adopted in recent years underline the determination of policy makers in Eastern Europe to restrain absorption in order to reduce their actual vulnerability to uncontrollable external events. Recent policies are also indicative of the course that these countries are likely to pursue in the immediate future. Further improvement in the current account with market economies and a reduction of the convertible currency debt without worsening imbalances in intra-group trade remain on the agenda for 1984.

As shown in table II-9, the adjustment measures in Eastern Europe have yielded a growing trade surplus with the market economies, in spite of only modest growth of import

Table II-9. Centrally planned economies: trade balances, 1981-1983

(Billions of dollars)

	Eastern Europe			USSR			China		
	1981	1982	1983[a]	1981	1982	1983[a]	1981	1982	1983[a]
World	-2.7	4.4	5.4	6.2	9.3	11.2	-	3.1	1.9
Centrally planned economies	-3.2	-1.0	-1.0	6.0	4.4	4.1	0.1	-0.3	-0.4
Developed market economies	-2.9	1.3	2.6	-1.2	-0.1	1.2	-4.6	-3.7	-4.6
Developing countries	3.5	4.1	3.9	1.4	4.9	5.9	4.6	7.0	6.8

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on official national and international data sources as well as independent estimates.

[a] Preliminary estimates.

demand in the latter countries. The group's export drive has been most conspicuous in relations with the developed market economies, with which the 1983 trade surplus of $2.6 billion was double that attained in the previous year. The Soviet Union, on the other hand, increased its overall trade surplus by about $2 billion by reversing its small deficit with the developed market economies and increasing its trade surplus with developing countries. China's trade surplus fell by over $1 billion, largely owing to an increase in the deficit with the developed market economies.

The current account balances of the Soviet Union and the majority of the Eastern European countries, especially in convertible currency transactions, have remained less in surplus than what the trade balances might suggest. Net outflows on account of interest payments have been sizeable, especially for the Eastern European countries. None the less, rough estimates indicate that both the Eastern European countries and the Soviet Union recorded surpluses on current account in both 1982 and 1983.[24] In 1983, the combined surplus on current account of these countries was probably of the order of $14-15 billion in all trade relations and $6.5-7.5 billion with convertible currency partners. Thus for the second consecutive year, Eastern Europe and the Soviet Union experienced net outflows of financial resources and a corresponding reduction in their foreign debt with the developed market economies. China also ran a sizeable current account surplus in 1983, which must have been around $3-4 billion.

Most Eastern European countries, and particularly Poland and Romania, continue to encounter severe external payments difficulties. The magnitude of the problem is particularly pronounced with regard to convertible currency transactions. In 1983, these countries' access to credit was seriously restricted,[25] but the experience gained in the two preceding years enabled negotiators to reschedule satisfactorily the convertible currency debt falling due in the course of 1983. Although a few other countries obtained some fresh loans, net inflows from world financial markets to Eastern Europe and the Soviet Union were negative for the second consecutive year. The net external debt of the European planned economies probably contracted by a larger amount than in 1982, to perhaps about $60 billion at the end of 1983.

Especially large shifts have occurred in the composition of the convertible currency debt of the European planned economies over the past two to three years. Eastern Europe's net debt to private banks in the market economies declined from about $40 billion at the end of 1980 to some $33 billion at the end of 1982 and appears to have fallen by a further $5-7 billion in 1983.

The overall debt of the region has probably declined less than bank debt, for several reasons. In the first place, debts to Governments have longer maturities than bank debts and, therefore, are being paid back at a slower pace. Second, there has been a shift in the composition of debt, since a part of the unpaid debt to the banks that had government guarantees has been transferred to the guaranteeing Governments. Third, some Eastern European countries have, in essence, used suppliers' credits to work off their bank debt. These have been especially important in the case of re-exports on the spot market of crude petroleum obtained on a credit basis from some oil-exporting developing countries. However, even after all of these factors are taken into account, Eastern Europe has undergone a significant measure of external adjustment, and this has had a favourable impact on the group's external indebtedness with the market economies.

On the other hand, in recent years there have been no noticeable changes in the CMEA's mechanisms of regional economic co-operation, which require that approximate bilateral balance in the reciprocal exchange of goods and services be attained annually. The worsening in Eastern Europe's terms of trade with the CMEA has been absorbed mainly through export promotion.

Furthermore, the prospects for an acceleration of regional economic integration, and hence for underpinning a more expansionary medium-term policy stance by the Eastern European countries, remains uncertain. Nearly all CMEA members are supporting the convening of a summit meeting of top decision makers in order to formulate improvements to the traditional mechanisms of regional economic co-operation and to re-examine the development goals to be served by intra-CMEA economic integration. This high-level meeting, which has been under preparation for several years, is now scheduled to be held sometime in 1984 and may provide an important impulse to economic growth and trade within the group in the medium to long run.

There are two other noteworthy aspects of the adjustment efforts undertaken in the early 1980s. The first refers to changes in the geographical distribution of exports. Over the period 1981-1982 Eastern Europe shifted the geographical direction of exports towards outside markets, especially the developing countries. In 1981, a substantial contraction in exports to the developed market economies was offset by large gains in exports to developing countries. This suggests that some Eastern European countries were very actively searching for alternative export outlets in the face of economic recession in the developed market economies. This strategy gradually ran into difficulties and could not be sustained in 1983. Demand in developing countries was far from buoyant, and their external financial constraints called for greater balance in reciprocal trade, thus making it difficult for the Eastern European countries to continue to enlarge their trade surpluses with developing countries in order to service their external debt with the developed market economies. During 1983, most of the increase in export volumes was in trade with the developed market economies, at a time when the latter were slowly emerging from their longest recession of the post-war period.

Another important aspect of Eastern Europe's adjustment efforts has been the changing commodity composition of trade. In intra-group trade, the composition of exports has remained relatively stable, and the fastest-growing exports have been in the categories of investment goods and semi-finished manufactures. By contrast, the most dynamic categories in exports to outside partners have been, paradoxically, energy products, raw materials and consumer goods.[26] The export drive was implemented by dampening consumer demand, by stringent energy and raw material conservation measures, and by permitting the emergence of imbalances in some domestic markets, especially foodstuffs. Since these policies are unlikely to be sustained for long, export growth could be more moderate in the next couple of years. On the other hand, the upturn in Western Europe in 1984 may open up some room for the exports of manufactures from Eastern Europe. However, success with that endeavour will depend on further structural adjustments in most Eastern European countries.

Notes

1 *World Economic Survey 1983* (United Nations publication, Sales No. E.83.II.1), pp. 33-34.

2 An interesting proposal in this connection has been recently advanced in J. Williamson, *The Exchange Rate System* (Washington, D.C., Institute for International Economics, September 1983).

3 See United Nations Economic Commission for Latin America, *Balance Preliminar de la Economía Latinoamericana durante 1983* (E/CEPAL/G.1279), Santiago, 16 December 1983, p. 13.

4 See General Assembly documents A/38/132-S/15675 and Corr.1 and 2 (8 April 1983); and A/39/118-E/1984/45 (29 February 1984).

5 A Committee on Trade in Agriculture and a Group on Quantitative Restrictions and Other Non-Tariff Measures have been set up and are due to report their findings and recommendations in late 1984. The Committee on Trade and Development has undertaken a review of the implementation of the provisions granting preferential treatment to developing countries, and it has held a round of consultations on tropical products. At the same time, the Working Party on Textiles and Clothing has begun to study the possible effects of phasing out the MFA. However, the most pressing item on the agenda remains unsolved: despite protracted negotiations, it has not been possible to reach a new comprehensive understanding on safeguard action against a surge in imports threatening domestic industry.

6 "Non-tariff barriers affecting the trade of developing countries and transparency in world trading conditions: the inventory of non-tariff barriers", (TD/B/940), report by the UNCTAD secretariat, 2 February 1983, pp. 6-9.

7 For instance, the EEC is considering the adoption of a plan combining the injection of new funds into high technology sectors and a significant, though temporary increase in external tariffs to protect Europe's infant high technology industries.

8 Argentina, Australia, Brazil, Colombia, Cuba, Dominican Republic, India, Nicaragua, Peru and the Philippines.

9 The industry is currently suffering from overcapacity due to the entrance of new suppliers, slack demand, and the growing use of steel substitutes.

10 In the field of textiles, the United States availed itself of the right to call for consultations seeking to renegotiate 50 bilateral agreements under the MFA. In addition, the United States imposed countervailing actions on, or initiated proceedings against, certain textile imports from a number of developing countries. The EEC imposed 20 new quotas on imports from MFA countries. Canada, Greece and Ireland also took measures to curb textile imports further. However, the United States and China lifted mutual trade sanctions and entered into a new textile agreement. More recently, China has applied to enter the MFA. In another, unrelated action, the EEC renewed for another year its voluntary export restraint agreements with Japan, covering 10 categories of sensitive products which account for 40 per cent of Japan's exports to the Community. The voluntary export restraint agreement limiting Japanese automobile exports to the United States was extended for a fourth year, raising the limit from 1.68 to 1.85 million units.

11 General Agreement on Tariffs and Trade, "Report of the Sub-Committee on Protective Measures" (COM.TD/SCPM/6), 20 October 1983, pp. 8-9.

12 It is extremely difficult to forecast exchange rate variations. For the purpose of the forecasts contained in this *Survey*, it has been assumed that the dollar will depreciate against major convertible currencies by 5 per cent in nominal effective terms in both 1984 and 1985 on a year-to-year basis.

13 For example, forecasts by the Secretariat at the beginning of the year for the current account of the capital-importing countries as a group yielded a reduction in their combined deficit of about $9 billion in 1983 relative to 1982. Current estimates suggest that the reduction could have been of the order of $39 billion. For earlier forecasts of 1983 current account balances, see *World Economic Survey 1983*, p. 47.

14 Organisation for Economic Co-operation and Development, *Financial Statistics Monthly*, February 1984.

15 World Bank, *Annual Report 1983* (Washington, D.C., 1983), pp. 39-40.

16 Data in 1981 prices and exchange rates. Organisation for Economic Co-operation and Development, *Development Co-operation, 1983 Review* (Paris, 1983), p. 52.

17 *OECD Observer*, November 1983, p. 19.

18 Based on a sample of 56 energy-importing developing countries for which adequate data were available to estimate imports for the year and year-end reserves.

19 International Monetary Fund, *Recent Multilateral Debt Restructurings with Official and Bank Creditors*, Occasional Paper No. 25 (Washington, D.C., 1983).

20 The other two low-conditionality facilities shown in table II-5 are no longer disbursing any funds. Loans under the Oil Facility have now been fully repaid. Loans from the Trust Fund, which had been established with some of the proceeds from the sale of IMF gold holdings in the 1970s, began to be repaid on a small scale in 1983.

21 *IMF Survey*, 9 January 1984.

22 Derived from data presented in *The Courier* (ACP-EEC), January-February 1984 and previous issues.

23 It should be noted, though, that large amounts of investment income channelled through so-called "tax havens" may have remained unrecorded. See *Economic Report of the President* (Washington, D.C., United States Government Printing Office, February 1984), pp. 43-44.

24 Official balance-of-payments data are not available for most centrally planned economies. Only Hungary, Poland and Romania publish balance of payments statistics on a fairly regular basis.

25 However, Hungary and Romania were able to borrow some funds from the IMF under stand-by arrangements. In early 1984, Romania abrogated its stand-by agreement with the IMF, owing to the perceived onerous conditions attached to the release of the last credit tranche.

26 Although the Eastern European countries are net importers of energy products, in 1983 some of them engaged in the re-export of crude petroleum from some developing countries. In addition, success in conservation allowed for some exports of domestically produced energy.

Chapter III

GROWTH IN THE WORLD ECONOMY AND CURRENT POLICY STANCES

Overview

In 1983, the level of economic activity in the world as a whole expanded by about 2 per cent (see table III-1). Though this mild upturn brought a welcome relief from three consecutive years of sharp deceleration in the pace of growth, economic performance in 1983 was very unevenly divided not only among but also within major country groupings. The growth observed in 1983 derived from the sharp economic recovery in North America, the measurable rebound in the pace of activity in some of the Eastern European countries, and the rather high levels of activity in many of the Asian economies. Elsewhere, however, growth remained exceedingly weak and very uneven. Prospects for a moderate expansion in levels of economic activity in the other developed market economies in 1984 are rather good, but for the majority of developing countries they remain fairly gloomy.

The economic upswing in the developed market economies that had been forecast for 1983 turned out to be much stronger in North America than had been anticipated early in the year, but started to become noticeable in some other large developed market economies only towards the end of the year. The economic upturn should spread further in 1984. But the strength and durability of the recovery beyond 1985 remain uncertain at this stage, owing partly to the still unsolved conflict in the macroeconomic policy mix pursued by the United States. On average, the pace of economic activity in the Eastern European planned economies accelerated somewhat in 1983. However growth there was virtually independent of economic events elsewhere in the world and stemmed mainly from the fairly strong recovery in Poland. This moderate growth in the industrial economies alleviated the situation of most developing countries only to a small measure. Because of the latter's generally precarious external payments situation, they were compelled to resort to further import cuts, which constituted an important drag on world economic expansion. In fact, the room for policy flexibility in these countries continued to be severely constricted by the very limited volume of external finance, the only modest recovery of some commodity export prices and the very high debt-service burden.

A number of different factors determined the pace of global economic activity in 1983. Perhaps the most important were the effects on prices, real disposable incomes and saving ratios of the economic policy stance of the United States. That country's expansionary fiscal policy was accompanied, from the third quarter of 1982 to the third quarter of 1983, by an accommodating monetary policy. This particular combination contributed to very substantial, and widening, budgetary and current account deficits. While nominal interest rates declined, real interest rates remained high. Because of the latter, as well as increased confidence in the United States economy, the dollar strengthened further in spite of

Table III-1. World: annual growth rates of output volume, by country groups and major sectors, 1976-1985

(Percentage)

Item and country group[a]	1976-1980	1981-1983	1982	1983[b]	1984[c]	1985[c]
Gross domestic product[d]						
World	4.0	1.6	0.8	2.2	3.8	3.5
Developed market economies	3.5	1.1	-0.2	2.0	3.8	3
Developing countries	5.0	0.7	0.5	0.0	3.5	3.5
Centrally planned economies[e]	4.6	3.5	3.7	4.3	4	4
Agricultural production[f]						
World	2.2	1.1	2.6	-0.3	...	...
Developed market economies	2.3	-2.5	1.8	-6.5	...	...
Developing countries	2.7	1.9	1.1	2.9	...	...
Centrally planned economies[e]	1.5	3.8	6.0	3.8	...	...
Industrial production[g]						
World	4.4	0.4	-1.4	1.7	...	...
Developed market economies	4.1	-0.9	-4.0	0.8	...	...
Centrally planned economies[e]	5.3	3.7	3.3	5.2	...	...

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on international and national sources.

[a] For a specification of the country groupings, see the explanatory notes at the beginning of the present document.

[b] Preliminary estimates, derived in some cases from data for a period of less than 12 months. Estimates for the developing countries are based on a sample of 83 countries, which jointly account for more than 90 per cent of the population and for 95 per cent of the aggregate GDP of the group.

[c] For the developed market economies, Secretariat forecasts based on Project LINK country models and other institutional forecasts; plan figures for centrally planned economies; and Secretariat forecasts for developing countries.

[d] Net material product in the case of the centrally planned economies. 1980 prices and exchange rates were used to obtain regional and global averages.

[e] China, Eastern Europe and the USSR only.

[f] Based on gross output indices prepared by the Food and Agriculture Organization of the United Nations, except for the centrally planned economies in 1981-1984, for which national statistical sources were used. Data for 1983 are estimates as of December. The average annual growth rates, measured over a multi-year period, reflect exponential trends obtained by fitting regression lines to the data points. The data for the groups were aggregated with the FAO's weights for 1974-1976.

[g] Based on indices of value added in developed market economies, indices of gross output at constant prices in the centrally planned economies, and Secretariat estimates of gross output for the developing countries. The coverage is International Standard Industrial Classification categories 2-4 (that is, mining, manufacturing, and electricity, gas and water). The data for the groups were aggregated with 1980 weights.

an increasing trade deficit. While the rise of the dollar contributed to holding down the pace of inflation in North America, it complicated policy choices in other developed market economies, particularly in Europe.

Policy makers in many European countries were determined to reduce fiscal deficits and to avert a rekindling of inflation. Monetary policies in most of these countries remained cautious. This combination of tight fiscal policies and cautious monetary policies did not support economic expansion. Moreover, the trade-related stimulatory effect of the recovery in North America in the second half of the year, while positive, was weak owing to the comparatively small share of the United States in Europe's exports. The major external impulse to the European market economies can emerge only from mutually supportive expansionary policies as well as from a strong revival of economic activity in the developing countries. In actual practice, the policies pursued by the major developed market economies had important - sometimes negative - repercussions through financial and trade links on developing countries in particular.

The economic performance of the centrally planned economies, although it improved over 1982, remained on the whole well below post-war trends. While the planned economies of Asia maintained the comparatively brisk pace of economic expansion registered in 1982 and Poland reversed the sharp contraction in economic activity levels of the past four years, the pace of economic growth in most other countries was modest. In Eastern Europe, this resulted from cautious output and distribution policies that were focused on the correction of current account imbalances and the gradual reduction of external debt levels. However, imports accelerated well beyond planned levels in Eastern Europe and remained strong in China and the Soviet Union, and so this group of countries imparted a modest impulse to world trade.

The economic situation in the developing countries as a group continued to be a cause of serious concern. Because of the lack of a sharp pick-up in international trade, the severe external constraints on their policy flexibility were not substantially alleviated. This was especially the case for the countries with a large foreign debt. While the decline in interest rates provided some relief, the magnitude of the debt-service burden was such that a very substantial share of export revenues had to be appropriated for factor services; as a result, imports were further compressed.

In the late 1970s, a large number of developing countries had been making progress in effecting structural adjustments, partly by mobilizing additional resources and changing the structure of public investment, and partly by relying more on market-determined prices. This process has been seriously hampered by the length and severity of the global economic recession. The difficulty of financing external deficits has severely restricted short-term domestic policies to expand output and has depressed feasible activity levels; many of these countries have been obliged to embrace policies aimed at reducing aggregate demand substantially. In many countries, the consequence of adjustment measures since 1980 has been the scrapping or postponement of investment projects, which will seriously limit attainable rates of growth in the medium-term, even if the world economic environment were to improve considerably in the near future. The compression of investment activity is slowing down the structural adjustment process in these countries and inhibiting a sharp acceleration in economic activity levels. As a result, the alleviation of their current external payments problems through domestic policy efforts and external financial resources has been proceeding much more slowly than would be desirable.

While sluggish international demand and only a weak recovery of export prices slowed down the growth of export earnings for the year as a whole, the turn-around in international trade since the latter part of 1983 is starting to improve the outlook for export earnings. However, policy flexibility in the developing countries remains constrained by serious financial problems: the expansion of long-term official financial flows is still well below past trends; the persistent debt problem has implications that extend well beyond developing countries themselves; high interest rates are still being engendered by the macroeconomic policies of some industrial countries; and international reserves in a large number of developing countries are at exceedingly low levels. On top of an already constrained external financial setting, a pervasive drought is further complicating the situation in Africa. Food output has fallen in many countries and, as a consequence, malnutrition is spreading.

The recession of the early 1980s was the longest of the post-war period and the sharpest for a number of countries. The recovery already under way in North America and now spreading to Japan and Europe, may lead, on the basis of current forecasts, to an acceleration of overall global growth to perhaps 3.8 per cent in 1984. The developing countries as a group are expected to attain about 3.5 per cent growth, which, if realized, would yield the first, albeit small, increase in GDP per capita since 1980.

This acceleration in global economic activity levels would certainly constitute a welcome change from four years of recession in most market economies and very slow growth throughout the world economy. However, because of a number of uncertainties in the policy stances of major actors in the world economy and considerable unevenness in the recovery, it is at this stage difficult to prejudge how sustained the recovery will be or how severe the next cyclical downturn. Present policies are characterized by a conflict between the monetary and fiscal policies of the United States, by perhaps overly cautious fiscal policy stances in a number of European market economies, and by commercial policies that increasingly inhibit trade among the developed market economies as well as with other countries and by vigorously deflationary policies in the more indebted developing countries. If these policies remain in place, the current recovery might remain lop-sided and might not last very long. This would have particularly detrimental consequences for the developing countries.

Widespread stagnation in developing countries

The severe development crisis affecting the economies of developing countries since 1980 was prolonged through 1983 as aggregate output for the group as a whole stagnated (see table III-2). Per capita GDP, on average, declined for the third consecutive year. The number of countries experiencing stagnation or negative growth increased markedly

Table III-2. Developing countries: rates of growth of GDP,[a] 1979-1983

(Percentage)

Regions and country groupings	1979	1980	1981	1982	1983[b]
Africa	4.8	1.9	-1.0	0.5	1.0
South and East Asia	2.5	6.0	6.6	3.5	5.2
Western Asia	6.0	-2.9	-1.1	-0.5	-3.1
Western hemisphere	6.5	5.3	0.7	-1.4	-2.8
Mediterranean[c]	2.9	1.2	2.6	2.5	1.8
All developing countries	5.0	3.2	1.6	0.5	-
Capital-importing developing countries	4.7	4.8	2.6	0.8	0.7
Least developed countries	2.4	2.3	1.2	1.5	2.0
Memorandum item: frequency distribution of GDP growth rates for 83 countries					
Zero or below	10	17	30	32	40
0.1-2.5	8	12	11	22	12
2.6-5.0	28	25	16	18	17
5.1-7.5	20	12	12	9	9
7.6 or over	17	17	14	2	5

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on national and international sources.

[a] The data for the regional groups are aggregated with weights based on constant 1980 prices and exchange rates.
[b] Preliminary estimates.
[c] Cyprus, Malta, Turkey and Yugoslavia.

and most developing countries incurred a fall in per capita GDP. However, there were significant differences in economic performance among the various regional groups. Whereas most countries in South and East Asia and some in North Africa[1] experienced an acceleration in the rate of economic growth, per capita incomes continued to decline elsewhere. Absolute levels of real GDP fell in Latin America for the second year in a row and in Western Asia for the fourth. These contrasts in economic performance need to be viewed against the backdrop of the global economic environment and the type of domestic policies that these countries have pursued in the past five years or so.

The pace and character of economic growth in most developing countries in 1983 were determined by a number of factors. In the first place, the unfavourable international financial environment and sluggish expansion in global trade severely constrained the choice of policies open to many of these countries. Second, adverse weather affected the agricultural performance of a number of developing countries. Third, many countries kept in place, or even reinforced, restrictive domestic fiscal and monetary policies in order to cope with external payments constraints, fiscal imbalances and high inflation rates. In many cases, the measures adopted in earlier years to come to grips with internal and external imbalances, which, until 1981, had been allowed to widen, were continued and strengthened in 1983. While some countries have implemented policies that will in time lead to a restructuring of their productive potential and to shifts in demand which will ease the recent imbalances, their effects in the short run, especially in 1982 and 1983, have been to constrain output. Other countries need to strengthen further their domestic efforts to overcome the imbalances in the medium run. A significant improvement in the external environment in the near future would certainly facilitate the restructuring efforts of the developing countries. However, this should not be viewed as a strong reason for postponing further domestic adjustment measures designed to ease import constraints and enlarge their export capacities in the medium-term.

The state of the world economy during most of 1983 was not conducive to the reactivation of growth in the developing countries. Because the economic recovery in the industrial countries was uneven, the impulse to growth provided by their demand for the exports of developing countries was generally weak. As noted in chapter II, oil prices fell substantially and the upswing in other commodity prices remained modest. Among the markets for exports of manufactures from the developing countries, only North America exhibited a strong expansion. Exports to other developed economies remained sluggish. Oil exports to the developed market economies contracted in volume terms for the fourth consecutive year and to other developing countries they fell for the second year in a row. This fall translated directly into a sharp decline in aggregate output in most of the countries where petroleum represents an important share of GDP. But the drop in oil prices eased somewhat the external payments constraint of the net oil-importing countries.

Besides the direct impact on their export sectors, the evolution of the international economic environment had an indirect effect on the developing countries' domestic economies through the foreign exchange constraint. With the exception of most countries in South and East Asia, and some in North Africa and Western Asia, external payments pressures were pervasive throughout the developing world. Governments were compelled to compress import volumes by a variety of direct measures and by strict demand management policies. As a result, output levels fell sharply. The contraction in the volume of the imports of key intermediate and capital goods must be counted as one of the major causes for the poor economic performance of the developing world. The policies of overall demand restraint required by the state of the external accounts had an additional adverse effect on output.

The precarious liquidity positions and the serious balance-of-payments problems of most developing countries have been a binding constraint on economic growth throughout the early 1980s. However, since the middle of 1982, the large overhang of external debt and the associated burden of debt service have considerably worsened the already tight external payments situation, especially in Latin America. With interest rates remaining high, export prices stagnating or increasing only slowly, export demand growing only modestly, and large amortization payments coming due, these countries had no option but to attempt to compress their imports as rapidly as possible. Although there were many instances of debt renegotiation, these were as a rule insufficient to prevent imports from falling. Pressures to reduce imports emanated not only from insufficient growth in export revenues, despite some increases in export volumes and some recovery in prices, but also from the need to make room for servicing the external debt. In addition, capital flows experienced a violent contraction, owing mainly to retrenchment by private banks involved in lending to these countries. For the second consecutive year, net remittances of profits and interest in Latin America far exceeded the net inflow of capital, so that in practice none of that capital was available to purchase imports.[2] In fact, the volume of Latin America's imports declined by an unprecedented 28 per cent in 1983.

Policies in those developing countries facing severe balance-of-payments problems have turned highly restrictive. Since most energy-importing countries have experienced deteriorating terms of trade and worsening payments difficulties for several years, the drift of policy since 1980 has been in the direction of increasing restraint. Adjustment efforts in the deficit countries have been impressive. In the period 1980-1983, the export volume of the energy-importing countries expanded by 36 per cent while their import volumes rose by barely 2 per cent. The deficit energy-exporting countries, on the other hand, maintained an expansionary posture up to 1982 as they benefited from very favourable terms of trade. The drastic deterioration in the external payments situation of most of these countries and the drying up of external capital since then has brought about a sharp change in their policy orientation. Most of their adjustment efforts during 1982-1983 resulted in falling imports - there was a contraction of over 22 per cent - and in no significant increase in real exports.

Adjustment has been particularly severe in countries with high debt-servicing obligations. The austerity measures embraced in an effort to come to terms with the external payments constraints have thrust a number of highly indebted countries into severe recession. Not only has total output fallen, but the decline has affected particularly the modern sectors. Industrial production has dropped sharply over the last two to three years, in some countries by 10 to 20 per cent. In the context of the postwar growth experience, the absolute contraction in output and employment levels in manufacturing is a new phenomenon that has had alarming consequences for economic growth and urban unemployment. The fall in activity levels did improve the current accounts of many of these countries in the manner envisaged in the debt-restructuring programmes worked out with private and official financial institutions. It has also, though, prevented the creation of the productive capacity that would enable these countries to meet future debt obligations. Rather than opt for downward adjustment of activity levels, which becomes mutually reinforcing as other countries join the process, these economies need to be re-activated through a vigorous expansion of their exports.

During the period 1979-1981, many developing countries adopted specific programmes of structural adjustment, often designed to increase self-sufficiency in food and energy; and they stepped up investment to achieve this end.[3] Since then, the severity of the overall contractionary adjustment that has taken place in these countries has sharply reduced the potential for investment. The tight foreign exchange situation has left little room for the import of capital goods. Moreover, restrictive financial policies have made credit for investment very scarce and costly. Most countries are fast approaching the limits of contractionary adjustment: import levels cannot be further reduced without unforeseeable economic, social and, in some cases, political consequences. The continuation of adjustment without further adverse consequences on development will require substantial new investments to re-orient the structure of the economy away from the production of non-tradables to that of goods that can be either exported or substituted for imports. This process needs to be supported by the infusion of additional medium- and long-term external resources. As already noted, the sharp fall in the availability of such resources from private capital markets has been one of the reasons for the austerity in government policies and the decline in investment.

Although the price rises experienced in 1983 in the developing world cannot solely be attributed to the external environment, the severe balance-of-payments pressures often had an additional adverse impact on growth through their aggravating inflation. Many countries, especially in Latin America, were forced to devalue their currencies sharply in an attempt to stimulate exports and substitute domestic production for imports. This contributed markedly to the acceleration of inflation to historically unprecedented levels. The dismal inflation picture in 1983 provided a further inducement to intensify some of the restrictive monetary and fiscal policies that had earlier been adopted for balance-of-payments reasons. In Latin America, these policies, necessitated by the incidence of exogenous factors, contributed to the worst recession of the last 50 years and caused a 3 per cent contraction in aggregate GDP.

All in all, the application of restrictive economic policies was intensified in most countries in the course of 1983. Although budget deficits did rise in many countries, this increase did not result from a deliberately expansive policy stance and, given the massive underutilization of resources, can hardly have been the root of the current external imbalance. On the contrary, in most cases the rising fiscal deficit was a consequence of the recession. Moreover, since most developing countries depend heavily on foreign trade taxes to raise government revenue, declines in foreign trade values have also worked to enlarge fiscal deficits. None the less, Governments have attempted to contain these endogenous increases in fiscal deficits through a variety of means, including cutting public expenditures, particularly investment, eliminating subsidies, enacting new taxes and increasing tax rates. Monetary conditions have also been tight, as witnessed by the unprecedentedly high level of real interest rates. A degree of monetary accommodation to the strong inflationary pressures stemming from devaluations and other factors was inevitable if an even larger contraction in economic activity was to be avoided. However, increases in the money supply in most countries have remained considerably below inflation rates.

The overall adverse economic performance of the developing world in 1983 masks some substantial differences among countries and regions. Indeed, some developing countries, mostly in Asia, recorded substantially higher rates of growth of output than other developing countries. As discussed in chapter I, these countries have managed to maintain relatively strong rates of economic advance throughout the 1980s. Although they were also buffeted by external disturbances, these were not as harmful as for other developing countries. They generally adopted adjustment policies sooner than other countries, especially in the areas of export promotion and import saving, and enjoyed a stronger agricultural performance.

In 1983, favourable weather conditions and continued success with agricultural modernization efforts resulted in pronounced increases in agricultural production in many countries of South and East Asia. In some cases, this good performance amounted to a recovery or mild rebound from the previous year's weak crops. In the Indian subcontinent in particular, the agricultural sector still accounts for a large share of GDP. Therefore, strong agricultural performance was associated with a marked improvement in overall economic growth.

Industrial activity accelerated significantly in developing Asia, particularly in the relatively more industrialized economies. For example, manufacturing output rose sharply in Hong Kong, Malaysia, the Republic of Korea and Singapore, which helped to reduce urban unemployment. In these countries, the recovery during 1983 was based largely on exports of manufactures to the developed market economies, in the first instance to the United States. Exports to this country were encouraged by the consumer-led recovery there and by the real effective depreciation of the exporting countries' currencies. The first factor provided a significant boost to demand and the second made the exports of manufactures from Asian developing countries very competitive with domestic production in the United States and with imports from developed countries.[4]

In other parts of Asia, notably India, Pakistan and Thailand, the expansion of manufacturing production was related more to domestic factors than to export demand. In countries experiencing an improvement in agricultural performance, stronger domestic demand and increased availability of inputs for agro-industries encouraged manufacturing production. Some countries with manageable debt levels continued to pursue vigorous industrialization policies, aimed at producing for the domestic market, through external borrowing. Elsewhere, increases in industrial production reflected the coming on stream of projects designed to attain greater self-sufficiency in energy production or to expand energy exports.

Adverse weather conditions, such as floods and drought, had a negative impact on agricultural production especially in Africa but also in a number of countries in Asia (Fiji, Malaysia, Philippines, Thailand and Western Samoa) and Latin America (Bolivia, Brazil and Peru). In sub-Saharan Africa, a severe drought devastated agricultural production which led international authorities to declare 24 countries to be suffering from critical food shortages.[5] Coming on top of a long-term decline in per capita food production, the drought is a cause for serious concern. In order to stave off hunger and malnutrition, the affected countries are diverting significant amounts of foreign exchange to food imports. Even if commercial imports and food aid were forthcoming at the required levels, as examined in the annex to the present report, it remains as yet unclear whether this effort will suffice to avert severe malnutrition or even starvation, especially in rural areas where food supplies are normally provided locally. Prospects for the near-term are not encouraging, owing to the low seed and fertilizer stocks for the next crop and the sluggish recovery in export revenues. The North African countries have also been experiencing drought. Despite the comparatively greater strength of their economies, additional cereal imports are digging into their foreign exchange reserves and thus jeopardizing their development plans.

Although the average rate of inflation, as measured by consumer prices, intensified in all developing regions (see table III-3), the medians indicate that in many countries inflation remained on the whole unchanged from the magnitudes recorded in 1982. It can thus not have been a major factor behind the current external payments problems of many of these countries. In South and East Asia the increase in the average inflation rate was modest and reflected mostly higher import costs stemming from currency devaluations. The acceleration of average price inflation in Africa, as measured, is probably not an accurate reflection of the overall situation on the continent; the medians appear to be more representative of conditions in most countries. However, acute shortages of foodstuffs as well as of imported goods in general have been putting upward pressure on prices. In any event, the sharpest increases - in many cases to historical records - in inflation were observed in Latin America. Triple-digit inflation rates were experienced by four countries, and the intensification of inflation was widespread throughout the region.

Inflation in Latin America has historically been higher than elsewhere in the developing world (see table III-3). Since 1981, and particularly in 1983, a number of developments contributed to a sharp acceleration in the region's average rate of inflation. The very substantial devaluations required by the scarcity of foreign exchange and the need to effect a rapid shift of resources from the domestic to the foreign trade sectors put strong upward pressures on price levels. Cost pressures were also intensified by the widespread elimination of subsidies on such basic items as food and certain social services, and by changes in pricing policies for fuels and public utilities. There were some demand factors as well. As noted above, the recession caused public sector deficits to widen sharply in some countries. Since capital markets in these economies are not well developed, large deficits are usually financed through borrowing from central banks, which accelerates the growth of the monetary aggregates. Finally, as inflation gathered momentum, changes in expectations led to further increases in prices.

Table III-3. Developing countries: annual rates of change in the consumer price index, 1976-1983[a]

(Percentage)

Regions	1976-1980	1979	1980	1981	1982	1983[b]
Africa						
Mean	17.2	14.7	14.9	21.2	11.6[c]	19.9
Median	13.5	13.8	12.2	13.1	12.5	10.8
South and East Asia						
Mean	9.1	11.8	15.8	13.6	7.9	10.2
Median	9.0	10.0	14.7	12.7	7.9	10.7
Western Asia						
Mean	15.3	11.5	20.4	19.7	16.9	24.5
Median	11.6	10.5	18.9	18.4	14.3	8.1
Western Hemisphere						
Mean	62.0	55.5	57.8	64.7	79.1	160.8
Median	13.0	17.8	21.5	19.7	11.8	16.4
Mediterranean[d]						
Mean	31.7	38.1	66.4	37.5	31.2	40.9
Median	18.0	21.3	29.9	36.6	30.8	34.4
Total						
Mean	33.5	31.1	36.0	37.3	39.3	75.2
Median	11.5	12.5	15.5	13.3	11.6	11.7

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics*; and United Nations, *Monthly Bulletin of Statistics*.

[a] Based on data for 79 countries. The means are aggregated using 1980 GDP weights.
[b] Preliminary estimates based on partial data.
[c] The considerable decline of the average rate of inflation in Africa in 1982 is largely explained by the abrupt fall, from over 100 per cent in 1981 to about 20 per cent in 1982, in the recorded rate of inflation of Ghana; it surged again to the three-digit level in 1983.
[d] Cyprus, Malta, Turkey and Yugoslavia.

Information on employment trends is still incomplete. Unemployment appears to have climbed further and has now reached unprecedented levels in many countries. In those Asian countries exhibiting relatively fast economic growth, some progress appears to have been made in reducing the rates of unemployment. But in Africa and particularly in Latin America, unemployment continued to rise rapidly during 1983. For many of these countries, it has now reached alarming levels in urban centres.

The prospects for an early resumption of rapid economic growth throughout the developing world are dim. The recovery now under way in the industrial countries and the revival of world trade that is widely forecast for 1984 and 1985 is expected to provide only a moderate stimulus to the exports of developing countries.

Countries where petroleum production is a high proportion of GDP are likely to benefit from the recovery in industrial countries which should bring a moderate increase in oil consumption and imports, after four years of precipitous decline. These developing countries' GDP may, therefore, rise by about 4 per cent per year during 1984-1985. A slight expansion in oil production should be accompanied by a robust increase of the non-oil sectors of many of these countries. Among the other developing regions, only the exporters of manufactures in Asia are expected to achieve growth rates more or less in line with their experience of the two decades preceding the recent global recession. Most of these countries are favourably positioned to continue to expand their exports to the industrial countries as the recovery gathers some momentum. Although several of them have encountered debt problems, by and large the servicing of their foreign debts should not present great difficulties.

The remaining two groups of developing countries - Africa and Latin America - are expected to see only a very modest measure of recovery in 1984-1985. While primary commodity prices could continue to recover, the lags expected in the upward movement of the price of key commodities, particularly metals, are bound to restrict the increase in export revenues of many developing countries. The drought and its after-effects permit only cautious output policies in the majority of African countries, especially in view of the strain on their balance of payments resulting from their food imports. The debt-restructuring exercises of the past two years have temporarily alleviated debt-servicing requirements - but at most until the scheduled resumption of amortization payments. However, if net capital inflows do not recover, the countries with large debt-servicing problems, including most of Latin America but also several other developing countries, will have to divert a sizeable proportion of any increase in export earnings to debt servicing. At present, there are widely held expectations that interest rates in capital market centres will, if anything, rise in the near future. Therefore, there will be no relief from this quarter for the highly indebted countries.

These forecasts for the likely economic performance of developing countries in 1984-1985 imply that, after three years of declining average per capita output, the pace of economic growth will still remain low. Although the room for manoeuvre in domestic policies continues to be very narrow, it is crucial that these countries sustain their own efforts aimed at restructuring their economies. If no change occurs in key policy areas, such as capital flows, interest rates and trade, in the years ahead little progress will be made to resolve the development crisis that has engulfed most countries in the developing world since the beginning of the decade.

Uneven recovery in developed market economies

Led by a vigorous economic upturn in North America, several developed market economies began to emerge from their longest post-war recession in the course of 1983.

However, growth averaged only a modest 2.1 per cent (see table III-4). Although the recovery in the United States and Canada has been remarkably similar to other post-war

Table III-4. Developed market economies: annual rates of growth of real gross national product,[a] 1976-1985

(Percentage)

Country or country group	1976-1980	1979-1983	1981	1982	1983[b]	1984[c]	1985[c]
All developed market economies	3.5	1.6	1.6	-0.2	2.1	3.8	3.1
Major industrial countries	3.7	1.7	1.7	-0.3	2.4	4.1	3.2
Canada	3.1	1.2	3.4	-4.4	3.0	4.0	3.5
France	3.3	1.3	0.3	1.8	0.2	0.5	1.5
Germany, Federal Republic of	3.5	1.1	-0.3	-1.1	1.4	3.0	3.0
Italy	3.8	1.4	0.1	-0.3	-1.2	2.0	2.5
Japan	5.1	4.1	4.0	3.3	3.2	4.5	4.0
United Kingdom	1.6	0.4	-2.0	1.5	2.7	3.0	2.5
United States	3.7	1.3	2.6	-1.9	3.3	5.5	3.5
Other industrial countries	2.7	1.4	0.9	0.3	0.5	2.2	2.5
Memorandum item:							
North America	3.6	1.3	2.7	-2.1	3.3	5.4	3.5
Europe	3.0	1.1	-0.3	0.4	0.9	2.1	2.4
Others	4.6	3.7	4.1	2.6	2.3	4.3	3.9

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on various official national and international sources.

[a] Constant 1980 prices and dollar exchange rates. For France, Italy, the United Kingdom and all of the "Other industrial countries", the measure used is gross domestic product.
[b] Preliminary estimates.
[c] Secretariat forecasts (based on Project LINK country models and other institutional forecasts).

cyclical upturns, that of Europe has been weak, hesitant and erratic. Japan began a modest recovery from its growth recession in the second half of 1983. In fact, the pace of recovery of real output outside North America is estimated to have been much slower in comparison to the cyclical upturn in 1976;[6] for Canada the rate has been a bit lower than that in 1976. For the Federal Republic of Germany, Japan and the United Kingdom, the rate of recovery thus far has been only half of their respective rates in 1976.

While the economic upturn in industrial countries other than North America has remained weak in comparison with earlier experiences, inflation rates in most countries have come down appreciably and have begun to converge; in 1983, the average change in consumer prices was less than 5 per cent. But the average unemployment rate remained unusually high at about 9 per cent, although its rate of increase slowed down significantly. Because of the strength of the recovery, the unemployment rate actually decreased sharply in the United States.

Industrial production on a year-end basis rose by about 16 per cent in the United States, 18 per cent in Canada and 10 per cent in Japan; more moderate gains, in the range of 4 to 6 per cent, were attained by the Federal Republic of Germany and the United Kingdom. There were also modest increases in Australia, Belgium, the Netherlands and Sweden. However, industrial activity continued to contract in France and Italy. By the end of 1983, the rate of capacity utilization in manufacturing showed significant increases over the 1982 low in Canada, Japan, the United Kingdom and the United States; none the less, it remained generally far below the high levels of late 1978.[7]

Given the existing pattern of trade interdependencies, the surge in import demand in the United States during 1983 directly benefited the economies of Canada, Japan and some of the net energy importing developing countries in Asia and Latin America. However, since the share of the United States in the total exports of most European economies is relatively small (about 7 per cent), the direct benefits of the North American upturn have been much less significant for Europe than for Japan and some of the exporters of manufactures among the developing countries. Also, because the sharp downturn in the pace of economic activity in the developing countries, particularly the oil exporters, has not been arrested by the upswing in North America, the indirect effects of this recovery upon Europe's exports have remained weaker than in earlier upturns.

In 1983, the strengthening of demand in the United States was led by consumer durables and residential construction.[8] Towards the end of the year, a gradual build-up in inventories and a fairly strong increase in investments in plant and equipment took place. Especially important for investment in the current recovery has been the considerable improvement in business profits. This has manifested itself most markedly in the United Kingdom and the United States, but to a lesser extent in other developed market economies. It resulted not only from the upturn in production levels and pro-cyclical gains in labour productivity, but also from the significant moderation in wage increases, particularly in manufacturing where unemployment rates have been the highest. Private investment in machinery and equipment picked up noticeably in the latter part of 1983 and early 1984 in the Federal Republic of Germany and to a lesser extent in Japan and the United Kingdom.

In Canada and the United Kingdom the major determinants of the sizeable rebound in the pace of economic activity in 1983 were the strength of consumer spending, the sharp rise in residential investment and the start of inventory rebuilding from the very low levels reached in 1982. The strength of private consumption demand in these economies, and to some degree also in the Federal Republic of Germany and France, partly resulted from falling saving ratios. This fall was associated with the slowing of inflation and improved consumer confidence.[9] However, the overall rate of economic activity remained weak in the Federal Republic of Germany. Because of the anti-inflationary stance of macroeconomic policy, the economies of France and Italy stagnated during 1983. Although the rate of inflation remained relatively high in these two countries, it showed a significant decline relative to 1982. This was a result of looser wage indexation in Italy and wage and price controls in France. Rising exports, mainly in the latter half of 1983, and falling imports were the main sources of the modest 3 per cent growth in Japan's GNP. However, wage moderation, fiscal austerity and high real interest rates adversely affected domestic demand through most of the year.

As a consequence of the economic conditions in the major European economies described above,[10] as well as the lack of strength in international trade, their own cautious macroeconomic policies, and their deeply embedded structural problems,[11] real output in most of the small European developed market economies either rose only marginally or declined in 1983.[12] However, some support for the small European economies was provided by their net exports of goods and services, especially in intra-European trade. Nevertheless, the recession in most of the small countries continued through 1983.

Until 1982, progress in cutting inflation had on a whole been slow and uneven among countries,[13] in spite of the restrictive monetary policies that had been adopted to break the back of inflationary expectations by demand contraction. In 1983, inflation continued to abate in all the major developed market economies, and also in many of the smaller members of the group, and tended to converge to a lower level. Record unemployment levels restrained wage demands in most countries. Moderation in the rate of wage increases, pro-cyclical productivity gains,[14] lower energy prices and the fall in nominal interest rates were key factors leading to a low 4.8 per cent average rate of consumer price inflation in 1983 in comparison with 7.9 per cent in 1982 (see table III-5). In the United States and Japan, the relative strength of the national currencies was an additional factor in keeping import prices low. While there was some progress too in the smaller countries, the pace of consumer price inflation on average remained relatively high and in some (Iceland and Portugal) it actually accelerated.

Unemployment rates in most developed market economies, particularly in Europe (see table III-6), have remained stubbornly high for a number of reasons. An improvement in the employment situation, especially in the smaller European countries, is not in sight.[15] These high, and in some countries rising, levels of unemployment have started to put downward pressure on wage demands. In addition to high levels of unemployment, fiscal austerity measures have also had a direct bearing on wage demands in a number of the European countries. In line with efforts to foster greater flexibility in labour markets, widespread cut-backs in public sector wages and transfer payments, and modifications of wage indexation schemes, including the temporary lifting of indexation altogether, have slowed down the rate of increase in real wages. This has been a major factor behind the

Table III-5. Developed market economies: rates of change of GNP deflator and consumer prices, 1976-1984[a]

(Percentage)

Country or country group	1976-1980	1980	1981	1982	1983[b]	1984[c]
GNP deflators						
All developed market economies	8.2	9.4	8.7	7.3	5.4	5.1
Major industrial countries	8.0	9.4	8.6	6.9	5.0	4.9
Canada	9.0	11.1	10.6	10.1	6.5	4.0
France	10.2	12.2	11.3	12.7	9.1	8.5
Germany, Federal Republic of	3.9	4.5	4.2	4.8	3.5	2.2
Italy	17.6	20.6	17.4	17.2	15.5	13.0
Japan	4.4	2.8	2.6	2.0	1.1	1.5
United Kingdom	14.5	18.5	12.4	7.5	5.0	5.5
United States	7.2	9.2	9.4	6.0	4.2	5.0
Other industrial countries	9.5	9.3	9.4	9.8	7.9	6.2
Consumer prices						
All developed market economies	9.0	12.2	10.3	7.9	4.8	...
Major industrial countries	8.8	12.3	10.0	7.2	4.2	...
Canada	8.8	10.3	12.4	10.9	5.8	...
France	10.4	13.8	13.4	11.8	9.3	...
Germany, Federal Republic of	4.0	5.5	5.9	5.3	3.0	...
Italy	16.3	21.2	17.8	16.5	14.6	...
Japan	6.5	8.0	4.9	2.7	1.9	...
United Kingdom	14.4	17.9	11.9	8.6	5.3	...
United States	8.9	13.5	10.4	6.1	3.2	...
Other industrial countries	9.9	11.0	11.4	11.0	8.0	...

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics*; Organisation for Economic Co-operation and Development, *OECD Economic Outlook*; Project LINK; and other official, national and international sources.

[a] Base year is 1980.
[b] Preliminary estimates.
[c] Forecast.

improvement in corporate profits. An immediate side effect of these developments, however, has been that gains in personal disposable incomes, and hence in consumer demand in some countries, have been limited.

Table III-6. Selected developed market economies: unemployment rates,[a] 1976-1984

(Percentage)

Country or country group	1976-1980	1981	1982	1983[b]	1984[c]
Major developed market economies	5.3	6.5	7.9	8.0	7.9
Canada	7.7	7.6	11.0	11.9	10.7
France	5.3	7.3	8.0	8.2	9.2
Germany, Federal Republic of	3.4	4.8	6.9	8.5	9.2
Italy	7.1	8.5	9.1	10.0	10.3
Japan	2.1	2.2	2.4	2.7	2.6
United Kingdom	6.4	10.6	11.0	11.5	11.6
United States	5.2	7.5	9.7	9.6	7.7
Other economies					
Belgium	8.2	10.7	12.6	14.5	15.3
Denmark	5.7	8.3	9.7	10.7	11.8
Ireland	8.5	10.2	11.7	14.6	16.6
Netherlands	4.3	7.1	12.7	15.6	17.6

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based in the case of the major countries on Organisation for Economic Co-operation and Development, *OECD Economic Outlook* and other official national sources, and in the case of other economies on Commission of the European Communities, *Annual Economic Report 1983-1984.*

[a] Number of unemployed persons as a percentage of the civilian labour force. Period average.
[b] Preliminary estimates.
[c] Forecasts.

The large degree of unevenness in the timing and strength of the recovery among the developed market economies,[16] particularly between North America and Europe, stems chiefly from the particular combinations of monetary and fiscal policies pursued in Europe and the United States. Especially important have been the structural fiscal deficit of the United States and the consequences of fiscal restrictiveness in many other countries. The fiscal policies of many countries in Europe have retarded the recovery there and may even be weakening it; they also may hasten the onset of the next downturn. Moreover, serious structural impediments to the growth of output and employment in Europe may be impeding the strengthening of the recovery there. The European market economies are intricately intertwined through trade and, owing to their integrated capital markets, cannot pursue monetary policies independently from those in the United States without repercussions on exchange rates and inflation. So far, the recovery has proceeded even though the policy stances of the major market economies have been unco-ordinated; in some countries, they have actually been inconsistent. This feature has been an obstacle to the strengthening and widening of the conomic recovery, particularly in Europe.

In 1983, the monetary policies of nearly all developed market economies continued to be constrained by high interest rates in the United States. Early in the second half of 1982, the Federal Reserve in the United States had gradually allowed the growth of the narrow monetary aggregate (M1) to overshoot its preset target range (see table III-7),[17] a policy that was maintained through the first half of 1983.[18] This easing of monetary policy was an important factor in the decline in nominal interest rates in nearly all the

Table III-7. Major developed market economies: real rate of change in broad money supply,[a] 1979-1983

(Percentage change from previous period-end)

Country	1979	1980	1981	1982	1983[b]	1983[c] 1st half	1983[c] 2nd half
Canada	5.6	6.6	1.0	-2.1	-5.3[d]	-4.5	-3.0[d]
France	3.8	-1.8	-1.5	1.0	-0.5	-3.0	1.0
Germany, Federal Republic of[e]	2.0	1.8	0.3	2.0	2.8	-2.5	6.5
Italy	2.8	-6.5	-6.6	-2.5	-4.0	-1.0	-5.0
Japan[f]	7.1	3.3	8.5	6.6	6.4	3.0	10.0
United Kingdom[g]	-5.0	3.0	3.1	2.1	5.0	8.2	1.7
United States	0.1	-1.0	0.4	4.5	7.0	12.1	2.0
Memorandum item: narrow money (M1)							
United States	-0.7	-2.7	-3.5	3.9	5.3	10.2	2.0
Canada	-7.6	0.1	-8.7	-6.0	12.5[d]	11.1	-5.0[d]

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on International Monetary Fund, *International Financial Statistics*; Organisation for Economic Co-operation and Development, *Main Economic Indicators*; and Commission of European Communities, *Annual Economic Report, 1982-1983*.

[a] M2, that is currency in circulation plus demand deposits (M1) plus quasi-money. The rate of change in real money supply is measured by calculating the end of period to end of preceding period change in the money stock and deflating it by the rate of change in the GNP deflator of the same period.
[b] Preliminary.
[c] Annualized half-yearly growth rates.
[d] Based on end-September data.
[e] Money stock M3 (M2 plus large time deposits).
[f] M2 plus certificates of deposits.
[g] Sterling M3 (normal M3 without foreign currency deposits in the United Kingdom).

major developed countries and provided room for them to increase credit so as to accommodate the recovery in economic activity.[19] However, since August 1983 the monetary stance in the United States has been tightened and M1 has been growing close to the floor of the announced target range.[20] This increased the potential for conflict between the large budget deficit and the monetary policy stance, and thus was an important factor in keeping real interest rates high (see table III-8).

Monetary policy in Europe and Japan has remained cautious and restrained largely because of the impact of the macroeconomic policy mix in the United States on interest rates. Indeed, the re-emergence of the clash between fiscal and monetary policy in the United States, and the restrictive monetary policies in the other industrial economies have been major factors in the persistence of high real interest rates.

An issue of particular importance in the current recovery phase has been the strength of the United States dollar and high interest rates. As inflation moderated in the latter part of 1982, both long- and short-term nominal interest rates began to decline in most developed market economies. During the first half of 1983 they remained virtually unchanged and, since then, they have increased somewhat. Real interest rate differentials remained generally in favour of the United States. These differentials, positive expectations about the recovery of the United States as well as other economic, and also political, factors elicited a substantial capital inflow from abroad which brought about a further appreciation of the United States dollar in real terms in spite of growing trade deficits. The dollar's appreciation in 1983 bolstered exports to the United States and helped to keep down inflation. But it put upward pressure on costs in countries with a depreciating currency, thus complicating their anti-inflationary policies.[21]

High interest rates have not just had appreciable effects on exchange rates and capital flows. They have also markedly increased the size of government budget deficits;[22] weakened investment prospects, particularly in interest-sensitive sectors; and, by imposing a substantial debt-servicing burden on economies with a large foreign exposure, they have reduced the import ability of these countries.[23]

In 1982-1983, the budgetary stance of the United States remained highly expansionary: whilst the unadjusted general government deficit remained nearly unchanged (see table III-9), [24] the cyclically adjusted general government budget deficit relative to GNP in 1983 increased by nearly one percentage point in comparison to 1982. Based on present trends and announced policies, the size of the federal budget deficit of the United States is expected to remain at around $200 billion per year in the foreseeable future because of a continuous increase in the structural deficit.[25] In most European countries and Japan, however, fiscal policy has been restrictive. In fact, in sharp contrast to the policy stance during the 1975 recession, most European economies have recently tried to reduce their structural budget deficits, in some cases by raising taxes, even in the midst of the recession. Such a restrictive fiscal stance may in the medium run stimulate private investment. However, it can be argued that these programmes of fiscal austerity undertaken

Table III-8. Major developed market economies: real interest rates,[a] 1975-1983

(Percentage)

Country	1975	1976	1980	1981	1982	1983[b]
Canada						
Short-term	-3.1	-0.5	1.0	6.4	3.5	2.7
Long-term	-1.6	-0.3	1.3	4.2	3.7	4.9
France						
Short-term	-4.8	-1.4	-0.3	3.6	1.8	3.3
Long-term	-2.6	0.5	1.4	4.5	2.8	4.8
Germany, Federal Republic of						
Short-term	1.7	0.4	4.4	6.7	3.7	1.8
Long-term	3.9	4.3	3.8	5.7	3.8	4.4
Italy						
Short-term	-6.5	-2.0	-3.1	1.9	1.9	4.5
Long-term	-5.2	-4.0	-7.2	-2.9	-0.4	4.8
Japan						
Short-term	2.2	0.3	7.9	4.7	4.8	5.2
Long-term	1.2	0.7	6.0	6.2	6.1	6.6
United Kingdom						
Short-term	-13.7	-3.2	-3.2	-1.3	2.1	2.5
Long-term	-10.5	-0.9	-4.5	1.5	4.4	5.2
United States						
Short-term	-3.2	-0.2	3.7	6.3	5.9	4.4
Long-term	-1.0	2.5	1.9	4.1	6.4	6.6
Memorandum item: nominal rate of interest						
United States						
Short-term	5.8	5.0	13.3	16.3	12.2	9.0
Long-term	8.2	7.8	11.4	13.9	12.7	11.3

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on Morgan Guaranty Trust Company, *World Financial Markets*; and International Monetary Fund, *International Financial Statistics*.

[a] Both short- and long-term rates are period averages net of the change in the GNP deflator. The short-term rate is the bank rate in Canada and the United Kingdom; call money rate in France, Federal Republic of Germany, Italy and Japan; and the Federal Funds rate in the United States. The long-term rate for Federal Republic of Germany is the yield on Public Authorities Bonds and for others the yield on long-term government bonds.

[b] Preliminary estimates based on data up to and including November 1983, except for Italy, whose data extend to the end of October 1983.

Table III-9. Selected developed market economies: the unadjusted general government budget surplus or deficit (-) as a percentage of nominal GNP,[a] 1978-1983

Country	1978-1980	1981	1982	1983[b]
Major developed market economies[c]				
Canada	-2.5	-1.1	-5.3	-5.7
France	-0.9	-1.9	-2.6	-3.4
Germany, Federal Republic of	-2.8	-3.9	-3.5	-3.1
Italy	-9.1	-11.7	-11.9	-12.0
Japan	-4.9	-4.0	-4.1	-3.4
United Kingdom	-3.6	-2.8	-2.0	-2.7
United States	-0.1	-0.9	-3.8	-3.9
Other economies[d]				
Belgium	-7.3	-12.8	-11.7	-12.2
Denmark	-1.9	-7.0	-9.1	-8.8
Netherlands	-3.7	-5.2	-7.0	-6.7
Sweden[c]	-2.4	-5.3	-6.7	-6.8
Memorandum item: budget deficit as a percentage of net private saving[e]				
United States	3.5	15.0	71.0	68.0

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on Organisation for Economic Co-operation and Development, *OECD Economic Outlook*, December 1983; and Commission of the European Communities, *Annual Economic Report, 1983-1984*.

[a] Budget surplus or deficit (-) of central, state and local governments.
[b] Preliminary.
[c] Based on OECD secretariat estimates.
[d] Based on estimates of the Commission of the European Communities.
[e] Net private saving is defined as the difference between gross private saving and capital consumption allowances.

simultaneously at a time of severe recession by a number of countries that are intimately intertwined through trade has aggravated the severity of their recession.

With regard to the fiscal policy stance of most European and Far Eastern developed market economies, there are several important issues concerning the relationship between medium-term objectives and short-term effects. First, countries in recent years have sought not only to reduce budget deficits but also to bring down the share of the public sector in GNP. The sharp rise in the ratio of public sector expenditures to output in the 1970s has been viewed by many policy makers as an undesirable, and in many instances inefficient, use of resources that may have been one crucial determinant of the deterioration of economic conditions in recent years.[26] Second, there has been a significant shift in the composition of government outlays from investment to mainly interest payments and social transfers. If the fiscal measures designed to change the composition of public outlays and to reduce its share in total output stimulate private investment then the overall medium-term effects of these shifts in policy will be favourable.

Except in the Federal Republic of Germany, Japan and the United Kingdom, automatic stabilizers sharply increased as a result of the recession and this largely offset the impact of the above structural policy measures on the size and composition of budget expenditures. In 1983, for the six major economies as a group, but especially the Federal Republic of Germany, Italy and Japan, the cyclically adjusted budget deficit relative to GNP showed a significant change toward fiscal tightening in comparison to 1982.[27] However, the ratio of the general government budget deficit to GDP increased for all major economies, except the Federal Republic of Germany and Japan. The budget deficit averaged over 6 per cent of GDP for the group of small market economies, but for some (Belgium, Greece, the Netherlands and Sweden) it exceeded 10 per cent.

The recovery is expected to become more widespread in the near-term. This spreading in 1984 is taking place in spite of the growing conflict between fiscal and monetary policy in the United States; the continuing restrictiveness of the fiscal policy stances of the European economies; and only weak demand impulses from developing countries. However, these policy conflicts give rise to a number of uncertainties regarding the strength of the recovery and the medium-term outlook for economic expansion, particularly in Europe. In 1984, output growth for the group as a whole is forecast to accelerate to nearly 4 per cent, mainly on the strength of the anticipated expansion of over 4 per cent in Japan and 5.5 per cent in the United States. The average inflation rate, as measured by the GNP price deflator, will probably inch up moderately in the few countries that will be in the second year of their recovery. Elsewhere, however, inflation is likely to continue to fall, but at a slower pace than in 1983. While the unemployment rate in North America is forecast to decline further, albeit at a slower pace, it is still expected to rise somewhat in Europe. Therefore, the unemployment rate for the group as a whole is likely to remain at around 9 per cent of the civilian labour force in 1984.

The continuation of the recovery in 1984 and beyond in the United States will increasingly depend on private investment. Factors in favour of a sustained, albeit moderate, increase in capital formation in the near future are the considerable rise in company profits, improved equity prices and tax incentives. A major, still unsettled, issue is the evolution of interest rates. During the first months of 1984, a gradual upward movement in interest rates could already be observed. Any further sharp increase in interest rates, possibly owing to the financing of very large budget deficits through sales of bonds that increasingly conflict with private credit demand, would threaten investment in structures, expansion in plants, as well as demand for durable consumer goods. Increases in employment, which boost total personal disposable income and hence consumer spending, and growing defence outlays are expected to keep domestic demand strong in 1984. This might be partially offset, however, by an increase in the saving ratio, the scheduled higher social security taxes and the possibility of "fiscal drag" effects.[28] Foreign demand for exports is not likely to exert a strong positive effect, even in the event of a decline in the value of the United States dollar, at least for a while. However, if the budget-gap is to be financed partly through foreign savings, higher interest rate differentials would have to emerge if the dollar depreciated as expected. In combination with the large and growing current account deficit, a sharp fall in capital inflows could adversely affect interest rates in the United States and would exert downward pressure on the value of the United States dollar *vis-à-vis* other major currencies. Such an outcome, though benefiting the export prospects of the United States, would have adverse effects on the rate of inflation and nominal interest rates.

Against the above backdrop of expansionary fiscal and cautiously restrictive monetary policies, growth in the United States is likely to be about 5.5 per cent in 1984 with a moderate slow-down towards the end of the year and into 1985 as the rates of increase in consumer spending and private investment begin to decelerate. Inflation is expected to be around 5 per cent in 1984 as the effects of lower oil prices, the strong dollar, pro-cyclical gains in productivity and wage moderation begin to fade. The unemployment rate will probably fall below 7.5 per cent by year-end.

In both the Federal Republic of Germany and Japan, increasing private consumption and investment, and rising exports will provide the main impetus to non-inflationary growth which, in 1984, should reach 3 and 4.5 per cent, respectively. Further increases in private consumption and considerable buoyancy in private investment will be the main determinants of an expected 3 per cent growth in the United Kingdom during 1984. Because of stronger domestic demand resulting from still increasing real wages and relatively buoyant exports, real GNP in Italy could rise by nearly 2 per cent in 1984. However, due to sluggish private investment, output in France is expected to continue to stagnate through most of the year. Inflation rates in both countries are likely to subside somewhat, but will remain by far the highest among the seven major economies.

The outlook for the strengthening of the recovery in Europe beyond 1984 and for it being sustained is more uncertain. The reason is that the prolongation of the recovery critically depends on private investment activity. There are several grounds for optimism in this regard. Business investment attitudes are likely to be favourably stimulated by the recent moderation of inflation and of real wage increases. Barring sharp fluctuations in commodity prices and exchange rates, inflation is likely to slow down during 1984-1985. Wage demands, in turn, will remain moderate as a result of the inflation outlook and the fiscal policy measures discussed above, and also of the substantial levels of unemployment.

As already noted, the unemployment rate in Europe is expected to increase further. This is partly a consequence of the lack of dynamism in the exports of these countries. However, a number of structural factors that cannot be remedied by any cyclical upturn loom large over their employment situation. These include limited downward flexibility of real wages, other rigidities in labour markets and social or political provisions that act to discourage mobility out of declining sectors (such as steel).[29] In addition, many of these countries have incurred a significant erosion of their competitive positions and shares in world markets as their adjustment to shifts in world trade has been incomplete, in part because of the prolonged period of weak investment activity. Many of them have also experienced sharp increases in the labour force for demographic reasons. All these factors impose formidable constraints on economic policies to foster employment.

Regarding the prospects of sustaining the recovery in the United States, much will depend on the fiscal policy stance there. The low levels of capacity utilization and the inflow of capital from abroad, partly in response to favourable interest rate differentials, have so far facilitated the accommodation of large budget deficits at prevailing interest rates. However, as business investment in the United States gathers further momentum in the course of 1984 and begins to exhaust the internal financial resources of firms, interest rates are likely to move upward. Also the pressure from the supply side of savings is bound to intensify if the direction of short-term capital movements were to be reversed sharply.[30] These expected movements, through their effect on real long-term interest rates, will adversely affect the investment outlook. Indeed, interest rates are likely to assume greater weight as the composition of investment changes from inventory restocking and equipment to the expansion of plants and new structures. In turn, future interest rates will, to a large extent, be influenced by the course of macroeconomic policy in the United States.

These prospects have already begun to complicate policy choices in Europe, particularly in the smaller economies. For example, in order to counteract the inflationary pressures that might arise from a depreciation of their currencies against the dollar, in most of these economies the authorities abruptly halted the decline in interest rates that was taking place in response to the shift in the monetary policy of the United States.[31] The outlook with respect to the sustainability of the recovery in Europe also depends importantly on favourable expectations of future demand. These could in turn be bolstered by a more flexible fiscal stance and a sharp rebound in exports, and the successful overcoming of those structural inflexibilities that have inhibited economic activity in recent years. Budget deficits in these countries continue to be very high, in part because of high interest payments by the public sector.

Given the policies that had been announced as of early 1984 and the expectation of only a moderate increase in interest rates in the course of the year, the projections for 1985 indicate that the growth rates of real output in the developed market economies will begin to converge as the rate of expansion in the United States moderates and the expected mild upturn in Europe takes hold. The rate of growth for the group as a whole is forecast to be within the range of 3 to 3.5 per cent. Japan's growth is projected to be above this average. Barring sharp exchange rate swings and large increases in commodity prices, inflation rates should remain well below those experienced in the 1970s. The moderate increases in nominal wages that are forecast and continued improvements in productivity should keep the average rate of inflation to an annual 6 to 7 per cent.

A modest acceleration in some of the centrally planned economies

The pace of economic activity in the centrally planned economies as a group inched up from 3.7 per cent in 1982 to an estimated 4.3 per cent in 1983, which was substantial in comparison with much of the rest of the world. However, this average masks a number of important differences in the economic performance of the various countries. These were evident not only for aggregate output and distribution, but also with respect to activity levels in the main economic sectors.

Buoyed by record or near-record output levels in most agricultural sectors and rapid industrial growth, the Asian planned economies repeated their strong overall economic performance of the preceding year. Aggregate output grew by about 6 per cent, with somewhat higher growth in China (see table III-10).[32] China's expansion of the past three years was such that the targets of the 1981-1985 plan for industry and agriculture have already been achieved; and the overall growth target will be fulfilled ahead of time in the course of 1984. Good agricultural performance, though below plan, and a rebound in industrial activity enabled the Soviet Union to attain several key plan targets: overall output growth was about 3.5 per cent,[33] with industry and agriculture reaching 4 and 5 per cent growth, respectively.

The 3.4 per cent growth of Eastern Europe in 1983 was in sharp contrast to the very sluggish performance of the preceding four years. However, the acceleration was uneven not only among but also within the various countries. The comparatively good average showing stems from a variety of factors, including the economic recovery in Poland, less constrained conditions in external trade and finance, stringent fuel and raw material conservation measures, and a pronounced gain in labour productivity. Though 1983 was on the whole a good year, it bears stressing that the current pace of growth in Eastern Europe remains well below the post-war trend, that the group's 1983 plan targets for overall and industrial output were only just fulfilled, that the upswing required the selective abandonment of import restraints which led some countries to an uncontrolled rise in investment, and that further efforts will be needed to work off internal and external imbalances in the medium run.

During the past three years, most of the European planned economies have made substantial adjustments to the changing internal and external economic environment. Policy makers still remain cautious with respect to accelerating the growth of output. At the same time they are determined to curb domestic absorption in order to ease external constraints. The continuation of the austerity measures first adopted in the early 1980s in several Eastern European countries, because of the shifts in the internal and external economic environment, makes the short-term outlook for growth not too bright. Therefore, it will be extremely difficult to achieve a number of the key output growth targets of the current (1981-1985) medium-term plans, as these had been based on policy precepts of the mid and late 1970s that could not be pursued. However, the policies actually implemented in

Table III-10. Centrally planned economies: basic economic growth indicators, 1976-1984

(Average annual and annual percentages)

Country or country group	1976-1980	1981-1985[a]	1981-1983	1981	1982	1983[b]	1984[a]
Eastern Europe[c]							
Net material product	3.9	3.2-3.3	0.4	-1.8	-	3.4	3.9
Industrial gross output	5.6	3.7-3.8	1.7	-0.6	1.2	4.6	4.3
Agricultural gross output	0.8	2.5-2.9[d]	1.0	1.8	1.7	-0.4	2.3
Gross fixed investment	2.7	-0.1[d]	-3.3	-7.2	-4.5	2.0	1.4[e]
Export volume[f]	6.4	...	5.1	1.5	6.8	7.0	...
Import volume[f]	4.0	...	-2.0	-4.8	-4.7	3.9	...
Soviet Union							
Net material product	4.3	3.4[g]	3.4	3.3	3.9	3.1[g]	3.1[g]
Industrial gross output	4.5	4.7	3.4	3.4	2.9	4.0	3.8
Agricultural gross output	1.6	2.5[d]	2.6	-1.0	5.5	5.0	6.4
Gross fixed investment	3.4	2.1[d]	4.1	3.8	3.6	5.0	3.9
Export volume[e]	4.8	...	3.9	0.4	6.3	5.0	...
Import volume[e]	5.8	...	7.2	8.2	9.1	4.2	...
China							
Net material product	6.0	4.0	6.2	4.8	7.4	6.5	...
Industrial gross output	9.2	4.0	7.5	4.1	7.7	10.2	...
Agricultural gross output	5.1	4.0	8.2	6.6	11.0	5.0	...
Gross fixed investment	6.5	1.7[d]	10.2	-20.5	26.6	18.0	...
Export value (in dollars)	20.3	8.1[h]	6.3	14.4	4.5	0.5	...
Import value (in dollars)	21.2	9.2[h]	-1.0	-0.4	-10.3	8.5	...

Source: Department of International and Economic and Social Affairs of the United Nations Secretariat, based on national statistical publications, plans and plan fulfilment reports.

[a] Plan targets.
[b] Preliminary estimates based on plan fulfilment reports and other partial information.
[c] Bulgaria, Czechoslovakia, German Democratic Republic, Hungary, Poland and Romania.
[d] Change in the five-year average output from the average of the preceding five years expressed as an annual compound rate.

the early 1980s may enable most of these countries to strengthen the foundations for a sustainable acceleration in their growth in the latter half of the decade. It has become increasingly recognized that for an acceleration of growth not to exacerbate existing imbalances or to re-ignite those that led to the recent austerity policies depends critically on whether national and group-wide economic policies can be designed to reflect the prevailing development conditions.

The 1983 plans and related macroeconomic policy discussions had forecast a cautious expansion in most countries. The very severe external constraints encountered in the course of 1982 led policy makers to slate improvement in the current account as the central concern of overall output and distribution plans. All Eastern European countries envisaged a rapid promotion of exports with stagnant or only moderately increasing imports. The growth of domestic absorption, investments in particular, was to trail that of aggregate production. Against the backdrop of the 1982 achievements as reported in the plan fulfilment report,[34] the Soviet Union had envisaged for 1983 only a slight acceleration in its aggregate output. This was largely due to the unimpressive prospects for its main exports, particularly petroleum, lingering bottlenecks in transportation and capacity limitations in basic supplier sectors. China's 1983 plan forecast moderate but more balanced growth and a further extension of the managerial and incentive reforms that have been progressively introduced since the late 1970s.

Many countries were unable to abide by key features of these plans. While in Europe the intentions in the plans with respect to exports and personal incomes were adhered to rather rigorously, those relating to imports, investment activity and consumer markets in many cases were not. Major deviations from planned levels occurred also in China. Although imports did not accelerate to the high levels forecast, domestic investment expenditures far surpassed plan targets and imbalances between heavy and light industry and between consumption and accumulation were noticeable.

One of the major 1983 targets in Eastern Europe was for a very slow or even negative growth of investment activity in line with the experience of the two preceding years. Policy makers hoped, however, that this sluggishness would not inhibit the achievement of moderate output growth on the basis of productivity gains and the more efficient utilization of fuels and raw materials. China and the Soviet Union had also envisaged only modest increases in investment outlays. These policy goals were embraced in order to hold down imports and domestic absorption, at the same time as minimizing the impact of austerity measures on consumption levels and freeing up goods for exports.

The plans for Eastern Europe called for an average contraction of about 2 per cent in overall investments, but with a wide range from a 10 per cent decline in the German Democratic Republic and Hungary to a 2 per cent increase in Bulgaria and Poland. Because of excess spending, particularly in the German Democratic Republic, Hungary and Poland, the group in fact averaged 2 per cent growth. In spite of major restraints enacted in the second half of 1983, China also experienced an unplanned surge in investment.

The spurt in investment activity, although it provided a welcome impulse to construction and industrial activities, violated the explicit intentions of central policy makers. The leap forward occurred partly because investment decisions were often made by local administrative units and individual enterprises based on retained profits and banks loans. To control this surge thus provided a major challenge to planners during most of the year in a number of countries. However, the problem arose not only from the violation of plan targets. Some part of the excess investment activity stemmed from the gradual re-assessment of distribution priorities in the light of changing circumstances.[35] The difficulties encountered in controlling decentralized investment expenditures led to imbalances in domestic markets and to import pressures. In particular, planners' hopes to complete projects in progress and thereby accelerate the bringing on stream of new capacity met only with moderate success in some countries.

The combination of the above-plan expansion of investment and the strong emphasis on export promotion in 1983 permitted only moderate gains in levels of living. This manifested itself not only in rather low rates of increase for private welfare indicators such as money incomes, wage rates, social transfers and retail sales. The decision of policy makers to ease the impact of domestic adjustments on consumers to a lesser degree than in preceding years also brought about sharp, planned and *ad hoc*, price increases.

Maintaining price stability in consumer markets has been a major preoccupation of policy makers since the mid-1970s. However, there has been rising awareness in these economies of the need to overhaul price policies as an integral part of the redesigning of planning and management systems with a view to better coming to grips with the growing complexity of economic structures and to fostering efficiency. In addition to bringing current prices into line with internal and external cost relations, policy makers have become more and more inclined to decontrol prices. However, in order to forestall dislocations in markets and to minimize consumer resistance, the process of introducing greater price flexibility has had to proceed gradually. This is especially so in economies, such as Poland, that are characterized by sizeable imbalances; but it applies also to those that have adhered to a policy of adjusting wholesale prices only at five-year or even longer intervals.[36]

In 1983, there were several price changes in the majority of the European economies that were not necessarily in line with the annual plans. Though growth in wages and social transfers in real terms remained small as planned, in the course of the year balance-of-payments considerations prompted further measures to increase exports and curb imports. Some measures took the form of sharp revisions in consumer prices,[37] others simply of a reduction in supplies which gave rise to shortages, and a few even of an explicit rationing[38] of goods that the authorities decided to earmark for exports on a priority basis[39] or not to import in the required quantities.[40]

In view of the tight balance-of-payments situation, economic activity was geared to production for exports and import-substitution, of agricultural and energy products in particular. Throughout the European members of the group, industry had been growing rather slowly in 1981-1982. The moderate growth targets set for 1983, which averaged 3.5 per cent, were approximately reached in most countries. Romania was the most notable exception, owing to severe external payments problems, inflexible domestic fuel supplies and bottlenecks in food-processing sectors. On the other hand, the recovery in Poland was strong and rather satisfactory results with raw material and energy conservation,[41] and the export push to market economies helped to realize the targets set in other countries. In many cases, this could be achieved only by boosting exports, including those of goods that the plans had earmarked for supplying domestic markets, and by easing import restraints. However, difficulties with the procurement of basic industrial inputs from within the CMEA and the strict management of convertible currency reserves clearly limited the degree to which alternative import sources could be tapped.

Above-plan industrial activity was nowhere more pronounced than in China: heavy and light industry expanded by 12.1 and 8.4 per cent instead of the planned 3.9 and 4.1 per cent, respectively; this discrepancy caused planners serious concerns. In particular, the rapid expansion of heavy industry was responsible for placing demands on energy and raw material sectors that could only be met by diverting supplies from other sectors. Moreover, it severely stretched transportation capacities, and as output increases did not correspond to planned levels sizeable inventories built up. The sharp expansion further led to bottlenecks in supply sectors and disproportions within industry itself. It also induced above-plan investment expenditures,[42] an increase in purchasing power for which the available supply of consumer goods did not suffice, and upward pressure on commodity prices that had to be eased by fiat in mid-year.

In contrast to the comparatively good agricultural performance recorded in 1982 throughout the group, 1983 was an uneven year. Whereas food and industrial crops as well as livestock production in the Asian centrally planned economies fared very well, adverse weather conditions, including spring floods and a hot dry summer, played havoc with the crop season in many areas of Eastern Europe and, to a smaller extent, also in the Soviet Union. The summer wheat crop[43] was adversely affected, and coarse grains and some root and forage crops experienced particularly sharp losses.

The European countries had hoped to increase food self-sufficiency and, in particular, to curtail their dependence on imports. Crops were to expand faster than livestock output.[44] While the import restraint was closely adhered to, the set-backs incurred in grain, root and forage crops caused stagnation in overall agricultural production. The 1983 grain harvest in Eastern Europe was about 5 per cent below that of 1982, which was a record or near-record year for most countries.[45] Losses were substantial in Bulgaria, Hungary and Romania and are bound to affect not only the 1984 current accounts but even more importantly the state of domestic consumer markets. Livestock production levels were restrained by the combination of import limitations and below-plan forage crop levels. Herd sizes changed little in the course of the year, but the cut-backs enacted in late 1982 and early 1983 curtailed meat production later in the year. Given the emphasis in the plans on export promotion, inclusive of foodstuffs, there was little scope for markedly improving domestic market supplies.

The USSR also failed to reach its main targets for certain components of agriculture, but the overall growth of 5 per cent was substantial. Although this year's grain crop of about 200 million tons was significantly below the annual average target of 238-243 million tons for the 1981-1985 period that was embodied in the food programme for the decade,[46] it was none the less the best since 1978 and the fifth largest ever. Favourable weather during the harvesting season, coming after the summer's drought, was one crucial factor.

However, additional inputs of farm equipment and fertilizers, higher procurement prices, and experimental reforms in the planning and management of farms need also be credited. Of especial promise for the future are the results attributed to the experiment with the "brigade contracting system".[47] The improvement in grain supplies and forage crops in the USSR created room for a significant increase in herds and livestock production. Meat output in 1983 in fact appears to be an all-time high. The comparatively good agricultural situation should permit tangible improvements in market supplies well into 1984; it should also reduce the need for imports.

In 1983, agricultural production in the Asian centrally planned economies was generally very good. New incentives and regulations in Viet Nam as well as favourable weather throughout the group yielded record or near-record grain crops.[48] The 4 per cent target for agriculture in China was exceeded in part because of another record grain crop and record cotton production. Further institutional and incentive reforms in rural areas appear to have played a more important role than incremental commitments of machinery and other resources to the sector. Favourable weather conditions in both 1982 and 1983, in spite of severe set-backs in some regions, helped, of course, but cannot be relied upon to prevail at all times. Further improvements in farm management, in the supply of fertilizer and high-yielding seeds, and in the availability of suitable farm equipment may be required to sustain the increase in unit yields.

Growth prospects of the European centrally planned economies in 1984 will to some extent depend on the recovery in developed market economies. This is clearly the case with regard to how far export promotion can be pursued, provided the output of exportable commodities will rise sufficiently. The recovery in Western Europe is also crucial in improving the environment for external finance which could help to validate a more expansionary policy stance, especially in the most heavily indebted Eastern European countries. The spreading and strengthening of the recovery in the Western European market economies are, then, undoubtedly important in selecting the levels of economic activity that the European centrally planned economies can sustain without exacerbating their external payments problems. However, the major constraints on the latter's growth prospects for 1984 are of a domestic nature. Aside from the fact that the developed market economies are not Eastern Europe's major trade partners and that there is keen competition for their markets, growth in Eastern Europe and the Soviet Union is expected to remain constrained, if perhaps to a smaller degree than in the past, by those internal and external problems that have been pivotal determinants of the pace of economic development since about 1980.

As in 1983, the majority of the Eastern European countries are placing very high priority on rectifying external imbalances, especially with the market economies. The policy stances that enabled these countries to start amortizing their external debt in 1982-1983 without jeopardizing the state of approximate balance in intra-CMEA trade are slated to remain in place and, where possible, to be strengthened. In view of the desire to reduce debt levels as well as the likely shift in their intra-CMEA terms of trade, the objectives to be pursued are all-round export promotion, restraint on imports, efficiency in the use of industrial inputs and a limitation of the increase in total domestic absorption. The latter target is to be attained primarily, as in recent years, by slow growth in investment activity but increasingly also by making inroads into private consumption demand. Plans forecast a uniformly higher rate of expansion for overall output than for domestic uses.

The rate of growth of aggregate output planned for 1984 in Eastern Europe averages out at under 4 per cent - only slightly above the 1983 achievements. A sharp acceleration is envisaged only in Romania, where the target of 7.3 per cent for NMP is more than double the 3.4 per cent reported for 1983. Most countries are striving to minimize any adverse impact of this continued modest growth on already attained levels of living. But it is increasingly realized in policy discussions that continued slow growth of investments would seriously mortgage the growth potential in the medium run.

Reflecting the need to undertake further adjustments, investment in 1984 is to expand less rapidly than in 1983, but growth is planned to be positive in the majority of countries. On the other hand, aggregate consumption will increase only minimally and it will in fact decline in some countries. Planners are aiming at the stricter regulation of investment activity so that decentralized decisions will also be in line with overall policy stances. Priority will be given to fostering fuel production and making more efficient use of primary and intermediate inputs. Industrial development, which is planned to be more balanced in countries that failed to achieve that objective in 1983, will be export oriented or linked to import substitution and energy conservation. The expected spreading of the economic recovery in Western Europe may facilitate the achievement of these external objectives. In agriculture, crop targets are in line with 1982 levels, but livestock production is slated to increase only marginally, owing to import restraints and the crop set-backs incurred in 1983.

The USSR's 1984 plan has been built around a modest expansion of aggregate economic activity, a similar performance in industry (3.8 per cent) as in 1983, but with higher growth for light industry for the second consecutive year, and substantial growth (6.4 per cent) in agriculture. As is the case in Eastern Europe, the USSR is planning to increase aggregate output through marked productivity gains, especially in agriculture (8.5 per cent), but with only a modest expansion in capital outlays (3.9 per cent). Improvements in the structure of production, stricter norms for the specific material intensity of production, and sharp improvements in product quality are important policy goals. The growth in output is earmarked primarily for improving levels of living. The total real income of the population is slated to increase by 3.5 per cent. 1984 will also be the first year of experimental reforms in some selected industrial enterprises which together account for perhaps 5 per cent of gross industrial output. The goal is to improve economic performance by devolving greater planning and managerial responsibilities to enterprises.

For 1984, the Asian planned economies continue to emphasize quantitative as well as qualitative self-sufficiency in agriculture and the strengthening of their material base, with the planned magnitude depending on 1983 achievements. While growth in China is expected to remain strong, planners are bent on controlling investments, partly through more stringent government expenditure policies, on achieving a better balance in industry at lower overall growth rates, on expanding fuel and raw material output, and on further extending the reform and adjustment policies of the past few years. These policies will be supported by a sharply expansionary import programme for advanced technology. Further incentive reforms in agriculture may well offset the effect on output of less favourable weather conditions.

Notes

1 Aside from the pronounced acceleration in output growth in Tunisia and the more moderate improvement in Algeria and Egypt, the major factor behind the slight increase in the pace of growth in Africa was the much smaller contraction in the Libyan Arab Jamahiriya's overall output in 1983 than in 1982.

2 For a fuller analysis of current conditions in Latin America, see Economic Commission for Latin America, *Balance Preliminar de la Economía Latinoamericana durante 1983* (Santiago, 16 December 1983).

3 For a description of these policies see *World Economic Survey 1981-1982* (United Nations publication, Sales No. E.82.II.C.1), pp. 86-87.

4 Sharp devaluations also enhanced Latin American exports to the United States.

5 See Food and Agriculture Organization of the United Nations, *Food Emergencies in Africa: Situation and Outlook for 1983/84* (Rome, October 1983). The food situation of sub-Saharan Africa in a global context is analysed in greater detail in the annex.

6 In the United States, the growth for the first year of recovery from the trough in the fourth quarter of 1982 was 6.1 per cent. This figure compares to the following past percentage rates of real growth from trough during the first year of recovery: 7.4 in 1955, 8.4 in 1959, 7.0 in 1962, 4.7 in 1971, 6.7 in 1976 and 4.3 in 1981.

7 For example, capacity utilization in the United States increased from 69.4 per cent in December 1982 to more than 79 per cent at the end of 1983 - far below the nearly 90 per cent mark reached in the latter half of 1978.

8 The implementation of the final phase of cuts in income tax rates, rising consumer borrowing and the sizeable increase in total disposable income, largely because of over 3 million gain in employment, were the additional factors that favourably affected the strong increase in private consumption expenditures in the United States. Growth in private consumption accounted for more than 80 per cent of total growth in GNP in 1983.

9 Rising interest rates usually stimulate personal savings. However, the favourable real wealth effects stemming from lower inflation rates tend to work in the opposite direction. The latter appears to have outweighed the former in 1983, thus reducing the saving ratio. In the United States, for example, the ratio of personal saving to personal disposable income declined continuously from 6.6 per cent in 1981 to only 4.0 per cent by mid-1983; it increased somewhat to 4.5 per cent in the latter half of 1983. In countries that were still experiencing recession, the usual pro-cyclical effect, stemming from consumption expenditures weakening less than personal disposable income, may have led to a fall in the personal saving rate.

10 In 1981, for example, the percentage shares of the Federal Republic of Germany, France and Italy combined in total exports of selected countries were: Belgium-Luxembourg 44, Denmark 27, Greece 32, Ireland 20 and the Netherlands 46. The average ratio of exports of goods and services to the GDP for these small economies as a group exceeded 44 per cent.

11 See Commission of the European Communities, *Annual Economic Report 1982-1983* (October 1982), pp. 7.9-7.13; and *Annual Economic Report 1983-1984* (November 1983), pp. 94-96.

12 Small economies with little or no growth in 1983 were: Ireland, the Netherlands, New Zealand, Portugal and Switzerland. Australia, Belgium, Greece, New Zealand and South Africa experienced a decline in the level of real output. Output in Australia and New Zealand also contracted on account of the drought-related set-backs in farm output which exacerbated the weak impulse from the international environment.

13 For a broader analysis of anti-inflationary policies in the early 1980s, see *World Economic Survey 1983* (United Nations publication, Sales No. E.83.II.C.1), pp. 73-83.

14 Labour productivity in many developed countries grew in the course of 1983. It averaged 2 per cent for the major countries, but Italy experienced a further decline. In some, this gain was pro-cyclical as it resulted from strong output performance with modest increases in employment (especially North America and Japan). Particularly in the smaller European countries, productivity gains resulted primarily from the further shedding of labour.

15 In fact, in the European Communities the unemployment rate is forecast to inch up further to about 11 per cent (Commission of the European Communities, *Annual Economic Report 1983-1984* (October 1983), p. 41).

16 During the recovery of 1976, output growth for six of the seven major members exceeded the average rate for all developed market economies. In 1983, however, three countries (France, the Federal Republic of Germany and Italy) fell well below the average. In fact, the variation of output growth among the major economies, as measured by the standard deviation, was more than twice that observed in 1976. This disparity in economic performance reflects the unsynchronized nature of the recovery and its underlying macroeconomic policies. The present lop-sided upturn has been depending crucially on the significant growth (3.3 per cent) of the United States and its strong import demand since the latter half of 1983.

17 In 1982, the official target range for M1 remained at an annual 2.5-5.5 per cent, while in the second half of the year M1 grew at an annual rate of 11.2 per cent.

18 M1 grew at an annual 12.7 per cent during the first half of 1983.

19 The situation in France and Italy differed since these countries have been following restrictive demand-management policies to bring inflation in line with that of major trading partners. In France, the growth of the broad monetary aggregate (M2) slowed down considerably as a result of the weakening of private credit demand. In Italy, on the other hand, the growth of total domestic credit exceeded the preset target rate because of large borrowing requirements by the public sector.

20 Based on preliminary figures, seasonally adjusted M1 grew only at an annual rate of 3.7 per cent during the second half of 1983.

21 Currency depreciation against the United States dollar in 1983 added substantially more to the rise in consumer prices in the smaller than in the major developed market economies.

22 For example, the average budget deficit as a percentage of GDP in the European Communities in 1983 before and after deducting interest payments were estimated at -5.4 and -1.6, respectively (see Commission of the European Communities, *Annual Economic Report 1983-1984* (October 1983), pp. 16-18). This suggests that the size of the public debt and the rate of interest are key determinants of fiscal outlays in these economies.

23 The weak international trade situation has had particularly adverse effects on the European economies. A recent econometric simulation indicates that for every 2 percentage points slow-down in the growth of world trade the growth rate of real GDP of the European Communities as a group decelerates by 0.5 percentage point with a lag of one year. The loss may rise to as high as 1 percentage point if the weaker trade situation continues (see Commission of the European Communities, *European Economy*, No. 18 (November 1983), p. 53).

24 The ratio of the federal government budget deficit relative to GNP increased from 4.8 per cent in 1982 to nearly 5.5 per cent in 1983. Although the surplus of state and local governments increased, the general government budget deficit still rose marginally to 3.9 per cent of GNP.

25 Based on estimates prepared by the Council of Economic Advisors, by 1988 cyclical and structural deficits will be $16 billion and $187 billion in comparison to $95 billion and $101 billion in 1983, respectively (see CEA, *Economic Report of the President* (Washington, D.C., U.S. Government Printing Office, 1984), p.36).

26 Government outlays relative to GDP for the group rose from 29 per cent in 1961 to nearly 41 per cent in 1981; in the small European economies, that share nearly doubled, from 26 per cent to nearly 52 per cent in the same period. The possible repercussions of this surge on levels of economic activity are described in some detail in *Supplement to World Economic Survey 1983* (United Nations publication, Sales No. E.83.II.C.3), pp. 21-30.

27 In 1983, the cyclically adjusted general government deficit in the following countries showed movements towards fiscal tightening: Belgium, Denmark, Federal Republic of Germany, Ireland, Italy, Japan and Spain.

28 With a given level and pattern of expenditures and unchanged tax rates, as the economy approaches full employment the deficit relative to GNP will decline and so will its impact on aggregate demand.

29 See Organisation for Economic Co-operation and Development, *Positive Adjustment Policies - Managing Structural Change* (Paris, 1983) and *Job Losses in Major Industries - Manpower Strategy Responses* (Paris, 1983).

30 In 1983, the net inflow from abroad exceeded one half of the general government deficit. Since the corporate sector is likely to become again a net borrower in 1984, the brunt of financing the government deficit will have to be borne by the foreign sector.

31 Subsequent to the rise in the United States and then in German interest rates, Austria, Belgium and the Netherlands also raised their interest rates. This trend, however, was not followed by Denmark and Ireland, where the basic rates of interest have been allowed to come down moderately.

32 In some countries, however, import constraints stemming from weak export commodity prices for minerals and metals inhibited industrial activity.

33 The plan fulfilment report (*Pravda*, 29 January 1984) only gives the growth in the uses of net material product (NMP). However, it had earlier (*Pravda*, 29 December 1983) been disclosed that NMP produced per worker in 1983 grew by 3.5 per cent. Since there was probably some growth in the labour force in the material sphere, NMP produced expanded by about 3.5-4 per cent.

34 *Pravda*, 23 January 1983, reported 2.6 per cent growth in the domestic use of net material product. However, this was revised to about 3.6 per cent (*Narodnoe khoziaistvo SSSR v 1982 g.* (Moscow, Finansy i statistika, 1983), p. 36). The 1983 plan target was therefore an acceleration over the original but not over the revised 1982 growth rate.

35 For a strong statement on the importance of maintaining adequate investment activity, even at the cost of stagnation of consumption, by a top Hungarian policy maker, see J. Hoós in *Figyelő*, 13 October 1983.

36 Especially in Czechoslovakia, the German Democratic Republic and the Soviet Union.

37 Pronounced price adaptations were reported by Bulgaria, Czechoslovakia, Hungary and Romania.

38 For example, in order to cut down on fuel imports, Romania in late 1983 decreed the halving of fuel consumption in all activities other than material production, even though sharp raises in fuel prices had been introduced twice earlier in the year. Where necessary, the reduction in fuel consumption has been accomplished by simply cutting supplies.

39 In some Eastern European countries, including Poland and Romania, above-plan procurements of fuels and some basic foodstuffs, particularly meat and meat products, were reserved for exports, as sales of manufactures in convertible currency markets lagged well behind plan.

Notes (continued)

40 In addition to the export requirements, marketed quantities of fruits, vegetables, flour, bread and bakery products were inadequate in some countries because of import constraints or adverse weather conditions or both. The tight supply of flour, bread and bakery products was the indirect effect of substituting grain stocks for fodder that would otherwise have been imported.

41 Several of the European planned economies reported quite noticeable success with raw material and energy conservation measures, which had been allotted a key role in the 1983 plans and will remain of great importance in the next two years or so.

42 Largely because central planners have devolved a good deal of control over investment decision making in recent years. Thus the share of State to total investment outlays declined from 80 per cent in 1979 to an estimated 43 per cent in 1983 (*China Daily* (Beijing), 15 July 1983, p. 4).

43 In some countries, reseeding in mid-season helped to stave off even sharper output losses.

44 In the latter sector the recent shifts in herd composition were to be strengthened in order to save on imported feedstuff.

45 Thus, the 95-100 million ton harvest still slightly exceeds the average of 1976-1980.

46 See *Narodnoe khoziaistvo SSSR 1922-1982* (Moscow, Finansy i statistika, 1982), p. 53. The USSR has not disclosed annual plan targets for the last three years.

47 Brigades of kolkhoz members contract with farm management for delivery of an amount of produce in exchange for fixed quantities of inputs, with penalties for either side in case of non-compliance with the time- or size-dimension of the contract. The precise utilization of these primary and intermediate inputs, the mobilization of labour and the distribution of tasks among the brigade members are up to the brigade. Wage regulations are flexible and above-contract deliveries yield sharply incremental incentives to the brigades concerned.

48 For the first time since the Second World War, Viet Nam became a net rice exporter.

Annex

SELECTED SECTORAL TRENDS

The food crisis in Africa in the context of global production and trade

Despite the relatively good performance of agriculture in developing countries as a whole during 1983, the serious problems faced by this sector in many areas are far from being resolved. Only the Asian countries, mostly the countries east of Pakistan, experienced a substantial gain in food output. In all other developing regions, per capita production of food fell to its lowest level in four years. The situation continues to be very alarming in Africa, where the most severe drought in a decade reduced per capita food production for the fifth consecutive year. The greatest set-back occurred for coarse grains, which constitute the basic ingredient of the diet in the predominantly rural areas, and critical food shortages are being experienced by many countries.

Although agricultural output in Africa is small in the global context (less than 5 per cent), it is the dominant type of economic activity, often in the form of subsistence farming, for over 200 million people. The very modest growth in Africa's agricultural production, with stagnation in food output, had wide-ranging repercussions on overall economic activity in the continent. But it is not expected to have sizeable effects on world food markets in spite of the fact that some major net exporters of agricultural products experienced a sharp contraction in output.

While in 1982, the reasonably good performance of agriculture in the world as a whole lessened the severity of the world economic recession, in 1983, global net agricultural output, food as well as non-food,[a] fell slightly below the 1982 level. After having kept ahead of population growth for almost six years, the decline in per capita agricultural output in 1983 is likely to entail some adjustments in global demand and trade.

Adverse weather conditions in much of the the world contributed to the contraction in agricultural output. In addition to adverse weather, the programmes designed to regulate supplies in developed market economies, particularly the United States, were a key determinant of world agricultural performance. Agricultural production of the developing countries as a group expanded by almost 3 per cent - more than double the 1982 growth rate and roughly in line with the 1976-1980 trend. Because of propitious monsoon rains, output in most of Asia accelerated sharply. The combined level of production of all centrally planned economies rose modestly, largely in response to comparatively favourable weather conditions in combination with institutional and incentive changes in China and the USSR.

The contraction in the agriculture of developed market economies was particularly severe for food - about 8 per cent in 1983 (see table A-1). Owing largely to the 1983 acreage-restriction programmes of the United States and adverse weather conditions during the summer growing season, North America's food output fell by almost one fifth.

Table A-1. Indicators of net world food production,[a] 1971-1983

(1974-1976 = 100)

Country group	Total: Growth trend[b]	Total: 1980	Total: 1981	Total: 1982	Total: 1983	Per capita: Growth trend[b]	Per capita: 1980	Per capita: 1981	Per capita: 1982	Per capita: 1983
World	2.4	111	114	117	117	0.6	101	103	104	101
Developed market economies[c]	2.1	109	114	116	107	1.3	105	109	110	101
North America	2.8	112	125	125	102	1.8	106	117	117	94
Western Europe	1.8	111	110	114	112	1.3	109	107	111	109
Oceania	2.8	103	114	102	120	1.5	98	107	94	110
Developing countries[d]	3.2	116	120	122	126	0.8	103	104	103	104
Africa	1.8	109	111	115	115	-1.1	94	93	93	91
Latin America	3.7	118	123	127	126	1.2	104	106	107	104
Near East	3.4	114	117	119	121	0.6	99	99	98	97
Far East	3.5	117	125	124	132	1.3	105	110	107	111
Centrally planned economies	2.1	107	109	114	118	0.7	101	101	105	107
Asia	3.2	118	121	130	132	1.5	109	111	117	118
Europe	1.5	101	101	105	110	0.6	97	96	100	104

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on Food and Agriculture Organization of the United Nations, *Production Index Numbers*.

[a] All edible commodities that contain nutrients net of intermediate use, such as seed and animal feed.
[b] Average annual growth rate for 1971-1980, obtained as the slope of a regression line fitted to the data.
[c] Including Israel, Malta and Yugoslavia.
[d] Excluding Israel, Malta and Yugoslavia. The FAO regional grouping used in the table is as follows: "Africa" excludes South Africa, Egypt, the Libyan Arab Jamahiriya and Sudan; "Latin America" includes the Caribbean; "Near East" includes Afghanistan, Bahrain, Cyprus, Democratic Yemen, Egypt, Islamic Republic of Iran, Iraq, Jordan, Kuwait, Lebanon, the Libyan Arab Jamahiriya, Oman, Qatar, Saudi Arabia, Sudan, the Syrian Arab Republic, Turkey, the United Arab Emirates and Yemen; "Far East" includes Bangladesh, Bhutan, Brunei, Burma, Democratic Kampuchea, East Timor, India, Indonesia, the Lao People's Democratic Republic, Malaysia, Maldives, Nepal, Pakistan, the Philippines, the Republic of Korea, Singapore, Sri Lanka and Thailand, and also includes the territory of Hong Kong and the Chinese territory of Macao.

Such a sharp compression of output in one of the largest producing areas in the world would normally have had serious consequences for global food security. It did not for three reasons. First, the reduction in North America was virtually offset by the improved performance of other countries, especially Australia, China and the USSR, so that world food output declined by less than 1 per cent. Second, the substantial food inventories carried over from 1982 would, in any case, have sufficed to make up for the production losses in the short run. Third, the developing countries as a group increased their food output sufficiently to maintain per capita levels attained in the preceding two years or so. Their aggregate demand for imports from world markets therefore changed little from 1981-1982 levels.

Virtually all components of the food sector registered a decline in global production. The main exception was meat. A rise in feed prices led to an increase in the rate of herd liquidation despite continued sluggish world demand. World output of cereals declined by 6 per cent, mainly on account of the nearly 40 per cent reduction in the United States.[b] Cereal output of Western Europe also decreased, partly because budgetary restraints only allowed for a raise in grain prices guaranteed by the European Communities lower than the increase in costs. Among the developing countries, a very large gain was attained in the Asian countries, particularly India. However, adverse climatic conditions in many countries of Africa and Latin America reduced the cereal crop of these regions by 10 and 7 per cent, respectively.

The reduction of the cereal output stemmed especially from the sharp fall in the production of coarse grains for which global output is very dependent on the performance of Africa, Latin America and the United States - the regions that experienced the most serious shortfalls in output in 1983. Wheat was comparatively less affected by the prolonged drought in the United States since the bulk of the harvest was over by the time the drought reached its peak. As a result, world output of wheat remained virtually unchanged. Global rice production rose by 2 per cent, due to favourable weather conditions in Asia.

Despite the large stocks accumulated at the beginning of the 1983/84 season, the severe contraction - over 12 per cent - in world output of coarse grains in 1983 has already exerted upward pressures on the export prices of cereals. At the end of November, the price of maize stood 50 per cent above that of a year earlier. At that level, it became profitable to substitute wheat for maize in animal feed, especially in the United States and the European Communities. The decline in the output of coarse grains also resulted in a significant run-down in global stocks, which in the course of the present season are likely to be halved. This would be the steepest fall ever recorded in a single season and could bring world stocks of all cereals down from 323 million tons to 254 million tons during the 1983/84 season (see table A-2). The end-of-season stocks would amount to 16 per cent of expected utilization in 1984/85 - a coverage that falls slightly below the 17 per cent coverage that the FAO has stated as the minimum required for world food security.

However, since stocks are still sufficient to cover anticipated domestic and import needs during the present season, there is no immediate cause for alarm. Most of the decline will occur, as intended, in the United States, while the cereal stocks held by net food-importing countries will probably increase sharply. At the end of the 1983/84 season, cereal stocks will as a result be more evenly distributed among exporting and importing countries.

The decline in cereal output has had little effect on world supplies of cereals for direct human consumption since nearly all of the contraction was registered for coarse grains, which are mainly used for fodder. The weak recovery experienced so far in the world economy as well as continued balance-of-payments difficulties of many developing countries have limited the demand for food cereals, which is stagnating in 1983/84. Increased

Table A-2. World stocks and trade in cereals, 1979-1984

(Million tons)

Country or country group [a]	Stocks[b] 1979	1980	1981	1982	1983[c]	1984[d]
World	277	258	237	281	323	254
Developed market economies	148	141	121	165	203	123
North America	96	94	76	121	161	81
Western Europe	28	26	27	24	28	24
Australia	6	5	3	3	1	6
Other	18	17	16	17	12	12
Developing countries	51	47	54	57	56	57
Africa	5	5	6	7	7	6
Latin America	8	7	12	10	11	8
Near East	7	7	11	12	8	9
Far East	31	28	25	27	30	34
Centrally planned economies[e]	78	70	62	60	64	74

	Exports[f]			Imports[f]		
	1981	1982	1983[c]	1981	1982	1983[c]
World	215	195	197	215	195	197
Developed market economies	180	158	163	59	52	56
North America	139	123	124	1	1	1
Western Europe[g]	21	22	21	30	24	24
Australia	15	11	16	-	-	-
Japan	1	-	-	24	25	25
Other	4	2	2	4	2	6
Developing countries	30	31	32	84	82	88
Africa	1	1	1	24	23	28
Latin America	19	20	20	19	22	23
Near East	-	-	-	28	24	21
Far East	11	10	11	13	13	16
Centrally planned economies	5	5	4	73	61	54
USSR	1	1	1	45	33	29
China	1	1	1	14	20	17
Other	3	3	2	14	8	8

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on Food and Agriculture Organization of the United Nations, *Food Outlook*, 1983, No. 10 and 1984, Nos. 1 and 2; and *FAO Monthly Bulletin of Statistics*, 1983, No. 12.

[a] Coverage of regional groupings as in table A-1.
[b] Carry-over stocks for crop years ending in the year given.
[c] Preliminary.
[d] Forecast.
[e] USSR and China only.
[f] Export and import data refer to crop years starting in the year shown in column heading, except for rice on a milled basis, for which data refer to the calendar year of the year shown. Cereals include wheat, coarse grains and rice on a milled basis. The data include the wheat equivalent of wheat flour. Components may not add to totals because of rounding.
[g] Excludes intra-EEC trade.

imports of wheat in Africa and Latin America have been compensated by lower import requirements on the part of China, India and the USSR. The shift from maize to wheat in feed demand by developed market economies is placing some upward pressure on wheat export prices, but the large stocks at the beginning of the season have been cushioning its impact.[c] Rice export prices have also remained well below their 1981 peak.

Longer-term prospects for world cereal supplies are encouraging. The 1984 winter wheat acreage in the United States is expected to be sharply higher than in 1983. This reflects, in part the lower benefits available to wheat farmers under the 1984 acreage-reduction programme. The latter also excludes diversion and deficiency payments, as well as payments in kind, from the potential benefits granted to coarse grain farmers. Moreover, in the case of coarse grains, the loan rate for the 1984 crop is below that of 1983 and the minimum reduction of acreage required to qualify for the programme benefits has been halved. Under normal weather conditions, provided the programme is not modified,[d] cereal output in the United States in 1984 should significantly surpass the 1983 harvest.

The deterioration in food output has led to a critical situation especially in sub-Saharan Africa,[e] where a drought described by authoritative analysts as the worst in a decade, is presently afflicting more than 150 million people in 24 countries.[f] Two thirds of the affected countries belong to the least developed group. For many of them, 1983 was the second consecutive year of exceptionally dry weather. The drought spread throughout the region during 1983: most of the Sahel region, the Horn of Africa, and western and southern Africa experienced erratic and well below-average precipitation levels. The latter's deleterious effect on production was aggravated by widespread bush fires and a recurrence of rinderpest, which is a serious threat to the livestock sector.[g] Aggregate cereal import requirements of these 24 countries for 1982/83 were estimated at 4.6 million tons but actual commercial imports stagnated at some 2 million, owing to serious balance-of-payments difficulties. Domestic inventories, which surged in 1981 because of bumper crops, were mostly used up to bridge the shortfall in cereal production in 1982 and can therefore not provide any relief.

Short-term prospects for the drought-affected countries are even more alarming. Shortages of seeds and fertilizers required for multiple plantings in drought times will affect the 1983/84 crop, which is forecast to be lower than this year's. The ability to increase imports has declined on account of rising world prices for cereals, while export volume has stagnated and average real prices for the basic exports of these countries - cocoa, coffee, cotton and groundnuts - remain well below their pre-recession levels. Concessional aid remains sluggish and other sources of finance are unlikely to expand to any significant degree. Several of these countries were forced to reschedule their foreign debt over the past two years.[h] It is doubtful, then, that food shortages can be met by increased commercial imports. On the assumption that enough foreign exchange can be secured to maintain commercial imports at their 1982/83 level, food aid requirements will increase to about 3.8 million tons - about double the amount actually delivered in 1982/83. Of this total, only two thirds had been pledged by donor countries as of early February 1984.[i]

Although food crop conditions in other sub-Saharan countries are currently rated as normal, the group of low-income sub-Saharan countries will continue to need food aid at least at the same level as in recent years. Such aid has proved to be increasingly inadequate: as a share of total food imports it dropped from 36 per cent in the mid-1970s to less than 23 per cent in 1982/83. In the absence of remedial action, per capita food availability, which has already been below minimum nutritional requirements for more than a decade in these countries, will further decrease.

Given the current high global grain inventories, avoiding famine in Africa is primarily a matter of mobilizing foreign exchange reserves and food assistance. Funding minimum import demand from the historically low foreign exchange reserves in most of these food-deficit countries will be very difficult. Further, current export revenues do not appear to be improving markedly in spite of the rise in commodity prices for the exporters of tropical beverages (cocoa and some types of coffee) and industrial crops (cotton, rubber and sisal) since early 1983, because the recovery in developed countries has not yet led to a sustained strengthening of international demand for such commodities. The weak increases in export revenues in combination with the persisting low levels of international reserves inhibit many developing countries from covering domestic production shortfalls through commercial food imports.

Regardless of the level of commercial and other food imports, the incidence of the drought will be felt differently by various groups in the affected countries. Because of high domestic transportation costs and not well developed distribution systems, urban markets in sub-Saharan Africa are regularly supplied to a large extent through imports. Cereal provisions to these markets have therefore been less directly affected by the drought, although the import constraints, of course, have had some direct impact on urban provisions. By contrast, the basic diet of the predominantly rural areas, in which the larger proportion of the population lives, overwhelmingly consists of domestically grown sorghum, millet, maize and cassava. The output of all of these items was drastically reduced by the drought. Rural areas, especially in remote parts of the land-locked countries, will be particularly severely affected by the drought unless extra resources are appropriated to assure delivery of foreign assistance to where it is in greatest need. The foreign assistance necessary to finance the distribution costs involved in meeting the minimum food requirements, particularly of the rural population, through imports was estimated at some $6 million.[j]

World cereal markets are unlikely to be seriously affected by these import requirements of low-income sub-Saharan countries. The latter's cereal imports normally represent less than 2 per cent of the world total and any increase, which is rather unlikely given the scarcity of foreign exchange in these countries, would be offset by the lower import needs of China and India. Moreover, rice and wheat, for which world supplies are still relatively ample, account for almost 70 per cent of cereal imports of sub-Saharan Africa.[k] The impact on global supply will also be small since, even though output of sorghum and millet in the drought-affected countries represents about 10 per cent of world production, most of it is domestically consumed and only a small fraction is regularly exported.

Shipments of world food aid in cereals for developing countries as a whole are expected to decline marginally in 1983/84 and pledges to the World Food Programme for the current biennium 1983-1984 amount to only 80 per cent of the organization's original target. International assistance to agriculture has fared even worse than food aid. Multilateral institutions, which normally provide more than half of total aid to agriculture in developing countries, have been disproportionately affected by the curtailment of aid programmes of developed countries. Of particular concern are the problems encountered by the International Development Agency (IDA), which is the largest single donor to agriculture, in the seventh replenishment, at an adequate level, of its current funding. Total IDA resources might be reduced from $12 billion in the previous replenishment period to $9 billion over the 1984-1986 period. Also some bilateral programmes have hardened their loan terms, including the degree to which aid is tied to procurements in donor countries.

During the past several years, some modification in the regional pattern of global food trade flows has emerged (see table A-3). In the early 1980s, the developing countries as a group limited food imports and, in fact, encouraged food exports partly for foreign exchange reasons but also because of good agricultural performance. Dependence of these countries on net food imports from the developed economies therefore appears to be declining, in contrast to the 1970s, when food imports of developing countries grew three times faster than their food exports. A parallel change in the opposite direction is noticeable in food trade flows of developed market economies, whose export growth has recently been lagging behind that of imports.

It would be premature at this stage to assess the redirection of food trade as indicative of the future. Short-term factors are obviously involved: the above-mentioned revision of the supply-control programmes of the United States should increase food production and thus encourage exports. Moreover, the African developing regions particularly will remain dependent on food imports for years to come. But the recent shifts in the direction of trade and the greater share of importing countries in world cereal stocks forecast for 1984 point to a more balanced trade relationship at the global level. This could enhance world food security.

The situation in world energy markets

The effect of the economic upturn in a number of industrial countries on demand for energy in 1983 remained too weak to offset the decline in energy use that resulted from continued conservation efforts in reaction to the two rounds of oil price increases of the 1970s. This further contraction in the structural demand for energy in turn triggered once again a combination of supply and price responses. In some contrast to the uncertainties in global energy, particularly oil, markets in 1980-1982, a greater degree of stability emerged

Table A-3. Trade volume in food products,[a]
1971-1982 indices and trends
(1974-1976 = 100)

Country group[b]	Exports Growth trend[c]	Exports 1980	Exports 1981	Exports 1982	Imports Growth trend[c]	Imports 1980	Imports 1981	Imports 1982
Developed market economies	6.2	148	154	150	2.3	111	110	113
North America	7.4	156	161	156	0.1	96	103	94
Western Europe	6.0	143	153	151	2.4	113	110	116
Oceania	3.7	148	129	131	2.7	100	96	137
Developing countries	3.1	118	130	133	9.3	179	188	183
Africa	-3.2	86	85	86	9.6	193	207	217
Latin America	3.6	117	132	128	10.1	208	197	168
Near East	0.1	116	151	170	12.7	190	217	222
Far East	7.2	145	153	171	5.2	139	146	139
Centrally planned economies	-1.4	97	94	92	7.5	156	177	178
Asia	-1.3	99	85	82	7.5	185	197	217
Europe	-1.5	97	99	97	7.5	149	172	168

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on Food and Agriculture Organization of the United Nations, *FAO Trade Yearbook*, vol. 36 (1983).

[a] Food products excluding fish. The trade volume indices are of the Laspeyres type with 1974-1976 average unit value weights.
[b] Coverage of regional groupings as in table A-1.
[c] Average annual growth rate for 1971-1980 obtained as the slope of a regression line fitted to the data.

in the course of 1983 and it was expected that this change in the character of the market outlook would remain in place in the medium term. However, the flare-up in the lingering military confrontation between the Islamic Republic of Iran and Iraq and the more general insecurities in the Persian Gulf in early 1984 have increased the fears that markets may be destabilized again.

Total world primary energy output declined in 1983 by about 1.4 per cent - almost one half of the contraction in 1982. While weakness in aggregate energy production in the last three years reflected chiefly the fall in the output of oil and natural gas, the 1983 decline was about evenly distributed with production of oil, natural gas and coal contracting by 1.2, 1.5 and 1.6 per cent, respectively. World energy markets are currently characterized by large idle productive capacity and sizeable fuel stocks. In 1984, any increase in the energy demand on account of the strengthening recovery of the industrial countries is therefore more likely to elicit larger supplies than price pressures. Thereafter, barring political upheavals, world energy prices may grow in line with the overall rate of inflation in the industrial countries.

In 1983, the world coal industry experienced some of the problems that have been typical of the oil sector since 1981. Despite the 1.6 per cent decline in the level of output, the industry experienced record stock accumulation, flat export demand and intensified competition.[l] With the exception of China and Poland, where coal output advanced by 3-4 per cent, coal output in other major producers stagnated or declined. The drop was particularly large in the United States (about 6 per cent), owing to sluggish domestic and foreign demand. In the European Communities, total output declined by an estimated 5 per cent, while it remained virtually unchanged in the Soviet Union.

In 1983, world output of natural gas averaged 55 trillion cubic feet.[m] This contraction of about 1.5 per cent stemmed chiefly from the overall sluggishness of energy demand. But also government pricing policies, lagging investment and the oil-gas joint product association in many countries may have exerted a downward pull on production. Though the largest decline occurred in North America, particularly in the United States, output was also lowered in the Middle East. It rose, however, by 3.7 per cent in Western Europe and, buoyed by the 7 per cent output gain in the Soviet Union, by 6.3 per cent in the centrally planned economies.

Developments in the world oil market were marked by the sharp drop in world crude oil prices in the first quarter of 1983 and the price stability that has been prevailing since then. The fall in prices reflected the excess supply condition created by weak consumption demand and, most importantly, by a substantial reduction of oil inventories in the OECD. In the first quarter of 1983, oil inventories were run down at the abnormally high rate of 4 million barrels per day (mbd), which prompted OPEC members to scale down their aggregate oil output to 15.2 mbd - the lowest level since 1965. Despite this, the imbalance between demand and supply continued to exert pressure on oil prices and, in the end, OPEC felt compelled to lower the price of its marker crude (Saudi Arabian Light) by 15 per cent and to re-introduce an aggregate maximum production quota of 17.5 mbd. Though the recovery of demand in the United States in the second half of the year and the termination of speculative destocking, which followed the official price reductions announced in March, led to an increase in the level of world oil output in the latter part of the year, the industry continued to operate with substantial unutilized refining and production capacity. Furthermore, the uncertainty about the future course of international oil demand and world prices complicates the production picture for the oil industry.

Over the last four years, world oil consumption declined steadily, albeit at a slowing pace. At 57.6 mbd, consumption in 1983 was 1.7 per cent below the level of the previous year and 11.3 per cent below the 1979 peak of 65 mbd (see table A-4). While oil use in the centrally planned economies increased by 1.5 per cent, it declined by 2 per cent in the developed market economies and by 4.5 per cent in the developing countries. In contrast to the experience of the last three years during which the developed market economies accounted for the bulk of the contraction in the absolute volume of world oil use, in 1983 the decline was roughly evenly split between developed and developing market economies.

Table A-4. World oil production[a] and consumption, 1980-1983

(Million barrels per day)

	1980	1981	1982	1983[b]
Production				
Developed market economies	14.4	14.4	14.6	15.5
North America	11.6	11.5	11.4	11.6
Western Europe	2.5	2.6	2.8	3.3
Developing market economies	34.0	30.4	27.4	25.6
OPEC member countries	28.0	23.6	19.5	17.9
of which: crude oil	27.0	22.5	18.6	17.2
Mexico	1.9	2.4	2.7	2.7
Centrally planned economies	14.6	14.6	14.7	14.9
USSR	12.1	12.1	12.3	12.4
World total	63.0	60.2	56.7	56.0
of which: crude oil	60.0	55.9	53.2	52.6
Consumption				
Developed market economies	38.7	36.0	34.5	33.8
United States	17.0	16.0	15.3	15.1
Western Europe	13.8	12.8	12.4	12.0
Japan	4.7	4.4	4.2	4.1
Developing market economies	11.6	11.5	11.1	10.6
Centrally planned economies	13.3	12.9	13.0	13.2
Total	63.6	60.4	58.6	57.6

Source: Department of International Economic and Social Affairs of the United Nations Secretariat, based on *Oil and Gas Journal*; United States Department of Energy, *Monthly Energy Review*; and *Petroleum Intelligence Weekly*, various issues.

[a] Including natural gas liquids.
[b] Preliminary.

The relatively large drop in the level of oil consumption of the developing countries in 1983 is particularly noteworthy as it represents the second year of declining oil use. This drop in oil consumption reflects primarily the steady deterioration in the general economic situation of many developing countries but also the influence of enhanced conservation measures prompted by the substantial increase in oil prices. Since the early 1980s, a number of countries have enacted programmes to economize on the use of energy, particularly oil, by letting the real domestic price of petroleum products rise to reflect more appropriately the real cost of imports.[n] The steps taken have included the elimination of explicit government subsidies as well as letting domestic prices adjust fully and promptly to the impact of currency devaluations. This upward drift in real domestic oil prices had adverse consequences for demand.

The observed drop in the level of oil use of the developing countries in 1982-1983 is likely to be a temporary phenomenon, however. The growth of population, continued industrialization and urbanization, and increasing substitution of commercial fuels for rapidly depleting traditional fuels, such as wood and animal wastes, will inevitably increase the demand for commercial, particularly liquid, fuels. While the growth rate of energy consumption during the remainder of the 1980s is expected to be markedly lower than that of the preceding two decades, the incremental requirements are considerable and satisfaction of this demand may be a major challenge for these countries.

Increased volatility and unpredictability of market conditions have been important characteristics of world oil markets in the last couple of years. Despite prompt and large output adjustments by OPEC member countries, oil prices have been largely unpredictable. While real world oil prices increased on the average by about 140 per cent from 1978 to 1981, they declined by 19 per cent[o] over the last two years. Unfulfilled price expectations have, in turn, been partly responsible for the recent reversal in the intensity of exploration and development, both of which had been thriving on the expectation of rising prices.

One important source of instability in the world oil market in the last four years or so has been the sharp fluctuation in the demand for inventories.[p] In the last 10 years, changes in inventories in the OECD area have accounted for about 30 per cent of the variation in total demand of these countries.[q] While part of the fluctuation reflects seasonal changes in the level of oil use, in recent years changes in inventories for speculative reasons have played an increasingly important role in the overall balance of world oil demand and supply and hence in the determination of world oil prices. Thus, the fall in crude oil prices in the first quarter of 1983 was directly related to the substantial depletion of stocks; similarly, the two oil price increases of 1973-1974 and 1979-1980 occurred when large stock accumulation in anticipation of supply shortages led to panic buying and tight market conditions.

With world oil demand for consumption steadily declining throughout 1983, albeit with normal seasonal fluctuations, the fragile balance prevailing between aggregate world oil demand and supply reflected the offsetting movements of changes in the level of oil inventories and OPEC's aggregate output. After the sharp rundown of about 4 mbd in the first quarter of 1983, the level of world oil inventories remained virtually unchanged in the second quarter, but it increased at a rate of 1.5 mbd in the third quarter; in the final quarter of the year, stocks were once again being depleted at a rate of about 0.7 mbd. Movements in OPEC's aggregate output, from 15.2 mbd in the first quarter to 18.3 mbd in the third quarter, almost fully compensated for these fluctuations in demand.

Notes

[a] Only the component tropical beverages registered a significant output gain largely because of the cyclical peak of the coffee crop in Brazil.

[b] The programme to set aside acreage in exchange for payment-in-kind accounted for a substantial part of the decline in wheat output; the impact on coarse grains, such as maize and sorghum, was less since these summer crops were severely affected by the long drought. But the acreage allocated to coarse grains in 1983 was the lowest since the mid-1950s.

[c] In late 1983, prices were about 5 per cent below those of a year earlier.

[d] The United States Congress has approved a bill which provides greater benefits to wheat farmers. Although the Administration initially opposed this proposed legislation, it appears to have abandoned its opposition in early March 1984 (*New York Times*, 9 March 1984) The Senate is now likely to pass the bill soon.

[e] For a broader picture of the situation in that region, see World Bank, *Sub-Saharan Africa: Progress Report on Development Prospects and Programs* (Washington, D.C., September 1983).

[f] Angola, Benin, Botswana, Cape Verde, Central African Republic, Chad, Ethiopia, Gambia, Ghana, Guinea, Guinea-Bissau, Lesotho, Mali, Mauritania, Mozambique, Sao Tomé and Principe, Senegal, Somalia, Swaziland, Togo, United Republic of Tanzania, Upper Volta, Zambia and Zimbabwe.

[g] Rinderpest outbreaks have been reported in Benin, Chad, Ethiopia, Ghana, Mali, United Republic of Tanzania and Upper Volta, while livestock in the Central African Republic, Gambia, Guinea, Mauritania, Mozambique and Somalia is threatened by independent outbreaks in neighbouring countries.

[h] Central African Republic, Senegal and Togo.

[i] Food and Agriculture Organization of the United Nations, *Food Supply Situation in 24 African Countries Affected by Food and Agriculture Emergencies in 1984* (Rome, February 1984).

[j] Food and Agriculture Organization of the United Nations, *International Emergency Assistance Required in Food Supplies, Agriculture and Animal Husbandry for African Countries in 1984* (Rome, 9 January 1984).

[k] Economic Commission for Africa: *Survey of Economic and Social Conditions in Africa 1981-1982* (Addis Ababa, 1983).

[l] In 1983, exports of coal by the United States declined by 26 per cent (*Quarterly Coal Report*, July-September 1983).

[m] Based on data for the first nine months of the year (*Oil and Gas Journal* (Tulsa, Oklahoma), 5 December 1983).

[n] World Bank, *The Energy Transition in Developing Countries* (Washington, D.C., August 1983), p. 15.

[o] Average world crude prices deflated by the United Nations unit value index of manufactures exported by the developed market economies.

[p] Stocks of crude and products in OECD countries as a whole increased sharply from 67 days of oil consumption (doc) in early 1974 to a peak of 119 doc in the second quarter of 1982; they declined to about 109 doc in the first quarter of 1983.

[q] Based on quarterly data (1974:II-1983:I) of total OECD stocks of crude and products (Organisation for Economic Co-operation and Development, *Quarterly Oil Statistics*, various issues).

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