

D. J. DELIVANIS
PROFESSOR OF ECONOMICS, UNIVERSITY OF THESSALONIKI

**THE IMPORTANCE OF WAGE
AND PRICE DEVELOPMENTS SINCE 1948.
INTERNAL AND EXTERNAL EQUILIBRIA
OF INDIVIDUAL COUNTRIES**

(Σελίδες 193 – 206)

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The author has had the pleasure to be the colleague of Professor P. L. Perdikas in the Panteios School of Political Sciences in the years 1939-46 and has kept a very agreeable memory of this collaboration. His esteem for Professor P. L. Perdikas has continuously increased as the latter has been able in this long and successful career to combine teaching, research, publication and practical appliance of law, both as a lawyer and as the law consultant of one of the leading Greek banks. In the latter Professor Perdikas' opinion is very much considered as is natural in view of his ability, of his knowledge and of his morality. The author has had the opportunity in preparing last year a lecture delivered at the Summer School of the University of Vienna to investigate the repercussions of the wage and price development on both the internal and the external equilibria of individual countries. He considered when asked to participate in the present volume issued on the occasion of the attainment of Professor P. L. Perdikas by the age limit to review his 1971 lecture and to publish its text. The countries chosen for this purpose have been Switzerland, the United States, Western Germany and the United Kingdom. Developments were considered until the end of the 1970 and so Switzerland and the United States are representative of countries whose foreign exchange rates have not changed 1948-70 through their own initiative, with the difference however that foreign trade and capital transfers from abroad and abroad are much more important in the first case than in the second. Western Germany represents the countries whose currency has been revalued and the United Kingdom those whose currency has been devalued more than once since 1945.

The consumer price index and the wages of unskilled workers may

be considered as representative in our case. There were however practical difficulties to be considered. I mean that the first has been started more than once on a new basis and that the second is not available. As a matter of fact it proved necessary to recalculate on the basis of 100 for 1948 the consumer price index numbers and to rely on the average hour wages of male adults in local currency in manufacturing as wages of unskilled workers are not available. Both these steps cannot be considered as 100% satisfactory inasmuch as data for the years 1945, 1946, 1947 and 1949 have not been published by the International Labour office as reproduced in the monthly statistical bulletins of the United Nations.

Wage and price developments may affect the internal equilibrium of an individual country, provided they last long enough, they act continuously in one direction, they are strong enough and sufficiently diversified in order to prevent rational investment, rational employment, rational consumption and satisfactory forecasting. Wage and price developments affect the external equilibrium of an individual country if they are longer and stronger than abroad, or if they act in an opposite direction provided these repercussions are not neutralised through market forces or governmental steps taken in the appropriate direction.

In examining wage and price developments since 1948 we may notice that at least as a rule they were in the four countries concerned upwards, they did not reach excessive rates any year since 1948, they were usually parallel and usually the result of negotiations whose outcome has been influenced more than once in the United Kingdom and in the United States by strikes, by threats of strikes, by governmental interference and by the activity of pressure groups. Seen in retrospect the developments have been quiet but only in one direction which means that upwards developments were not neutralized later by developments in the opposite direction as was the rule before World War II.

Part I will deal with internal equilibrium, Part II will deal with external equilibrium, Part III with particulars affecting the four countries chosen. Conclusions will follow.

I

It has to be accepted that internal equilibrium is achieved in a country when

- 1) saving equals investment ex ante,
- 2) prices and wages are relatively stable,

3) unemployment is considered to be at a normal level, that means rather low but not leading to bottlenecks,

4) plants available are operated on a scale considered normal,

5) orders on the waiting list are not excessive,

6) hoarding and unhoarding do not become noticeable exactly as they were always considered to be before J. M. Keynes drew attention in this General Theory on the importance of the repercussions whenever big changes occur.

1. In examining developments in the world in general and in the four countries chosen during the years 1948-70 in particular we notice that investment always exceeded savings *ex ante*. The gap was and is covered first by inflation, in this case by recourse to credits of the central bank which are harmless as their granting is combined with increased production through the more intensive operation of the plants available and through the employment of those who until now were and are un and underemployed. The most frequent procedure is the addition of a second or even of a third shift provided the labour force available is willing to work on these shifts. It has been found out as a matter of fact that in many developing countries supplementary investment is carried out because those unemployed refuse to work on the second or on the third shift. This leads very often to the deterioration of the trade balance and of the balance of payments¹ whilst this refusal proves that the conditions of those unemployed are not so desperate as many believe them to be as otherwise they would have accepted to work even on shifts operating on inconvenient hours. The second possibility to bridge the gap between saving and investment is unhoarding. It is wellknown that every body, every agency and every firm is hoarding up to a certain degree and that under certain circumstances, e.g. a pessimistic outlook for the purchasing power of the monetary unit, the forecast of a particularly profitable investment, or the possibility to secure within a relatively short time a very substantial profit even if *ex post* these prospects do not materialize, hoarding is reduced. This reduction may contribute to increase the possibilities of investment either directly, I mean when the amounts unhoarded are invested at once, or indirectly when they first increase consumption and then through the acceleration principle lead to increased investment. The third possibility available is the import of

1. Ch. G.C. Winston, Capital utilisation in economic development, *The Economic Journal* 1971, pp. 36-60.

capital from abroad which implies that capital saved there is placed at the disposal of those planning investments at home. Of course the import of capital is possible only when certain conditions are fulfilled in the country importing capital from the political, economic and monetary point of view. As a matter of fact capital is not imported in a country facing political troubles or a revolution except if those concerned in this country are able to persuade those foreign banks, firms and persons intending to borrow or to invest there that their capital will be safe. It is also improbable that foreign corporations or private people living abroad will consider transfer to a country on the eve of devaluation, or of the imposition of foreign exchange control or of a general embargo on payments abroad. Capital transfer is also excluded with differences between the foreign exchange value and the purchasing power of the monetary unit to the latter's disadvantage as in that case the transfer will imply a loss of capital which may be or will be quite substantial. Last but not least even if capital is not imported from abroad but the balance of payments shows a surplus this may allow to bridge the gap between saving ex ante and investment as long as this surplus will be transformed into local purchasing power through the banking system.

We may accordingly conclude that despite the inequality of saving ex ante and investment the gap may be covered by means which are not creating troubles worth mentioning under more or less normal conditions as they have been in the four countries concerned in the years 1948-70.

2. The development of wages and prices has been 1948-70 continuously upwards but at least in the four countries their upwards surge has never been hectic and has never led to real disequilibrium which shows that within certain limits price and wage fluctuations even if onesided do not upset equilibrium. This has to be stressed particularly as the range of fluctuations has been rather sharp and for the first time has never been reversed. It follows that the internal equilibrium is not affected even under unfavourable circumstances on a scale worth mentioning by price and wage fluctuations provided of course that their increases are not paid by the proceeds of central bank loans or by the proceeds of capital imports which are not affected for the repayment of foreign loans, for the repatriation of foreign capital, for supplementary imports of foreign commodities and for supplementary recourse to foreign services. It may be noted in this connection that 1948-70 capital imported was nearly always affected in a way not leading to

internal disequilibrium as their proceeds were as a rule spent without endangering the equilibrium of the economy concerned. Certain doubts are permitted in this connection in the case of Switzerland where however the possibilities of affecting foreign funds for various investments were sharply reduced in order to curb inflation whenever considered to be dangerous. The success of these steps has been quite satisfactory independently of the fact that they were taken and carried out without the announcement of a complicated plan as long as the latter would have been eventually considered as unconstitutional or at least subject to popular referendum.

3. The classical economists and at least some of their successors strongly believed that internal equilibrium may be achieved only with full employment. We all know in our days that equilibrium is perfectly possible with any level of unemployment and that the economy may always adapt itself independently of course of the sufferings the people in general and those unemployed in particular have to undergo has been proved that full employment and overemployment are not quite similar but that whilst bottlenecks are characteristic of the latter their appearance cannot be excluded in the former. There is no doubt that some unemployment provided it is not too large makes internal equilibrium easier than overemployment. The latter shows more than anything that the internal equilibrium is out of reach. In the years 1948-70 overemployment has until now up to a certain degree been prevented in all countries facing same through overtime and even more through immigration. The latter's opposition by the local manpower has substantially weakened as long as its members do not face any immigrants as competitors as they used to do in the past but as welcome addition. Foreign workers are affected mainly to the more burdensome, exhausting and unhealthy jobs as long as they cannot be carried out by machinery.

4. Plants available are operated normally independently rather often of the impossibility to secure three shifts. This is excluded as long as those unemployed do not participate in the night shift. Another reason for the partial exploitation of plants, transportation, housing etc available is connected with overinvestment whenever future needs in function of purchasing power available had been overestimated, mainly because those planning expansion usually do not consider unforeseen changes and their own competitors' expansion plans. This has happened more than once with the expansion of the air companies and in many other sectors leading to a waste of savings, labour and land which could

have been used in a more rational way. Governments' advice to invest leads often to overinvestment upsetting internal equilibrium.

5. It is natural at least under rather normal conditions that producers should have in advance orders as only thus it will be possible for them to plan their production in advance and to secure the most advantageous use of their plants, of their transportation and of their staff in combination with maintenance and repair at appropriate times. From the producers' point of view the greater the orders' waiting list the better but excessive waiting lists are always a sign of disequilibrium. The latter may be neutralised through new investments when their output is to start, through increased imports or through reduced exports or inventories. Increased investments are needed when the output of those available cannot be further increased and when demand is expected to continue on the same scale. On the other hand increased imports presuppose the possibility of paying for same and of securing appropriate transportation. The problem of increased imports created at various times difficulties in Western Germany and in the United Kingdom and thus excessively long waiting lists could not always be avoided as easily as in the other two countries. As far as Western Germany is concerned there were no problems in this connection after 1954. The development of inventories has often been influenced by the prospects of strikes in the frame of the efforts of those concerned to avoid as far as possible unfavourable repercussions of the strikes of their suppliers' and transporters' staffs on their own business. This tendency is particularly strong in the United States where strikes may be foreseen and where when started last very long.

The conclusion if orders on the waiting list are excessive or not in any concrete case depends from various circumstances and we may say that in the sixties the waiting list was considered excessive and thus a sign of disequilibrium much later than would have been the case in the fifties and even more in the forties or in the interwar period. The orders not carried out have to be examined in function of the productive capacity and of the waiting time considered to be normal.

6. The fluctuations of hoarding and unhoarding have not been excessive in the four countries examined here except in Western Germany in the years preceding the monetary reform of 1948. Accordingly we cannot derive from same proof of internal disequilibrium existing before hoarding or unhoarding is carried out or created through same with the sole exception of Western Germany before the monetary reform of 1948. There is no doubt that in our age hoarding and up to

a certain degree unhoarding may be neutralised through the central bank's credit policy if well planned and if well carried out.

Let me conclude that a further proof that internal disequilibrium does not materialise is the continuation on a normal scale of growth or development and of the operation of plants, of transportation and of all those services which are indispensable for the satisfaction of needs according to the prevailing opinions of all those affected.

II

External equilibrium is secured when

a. $M = X$

where M = imports of commodities from abroad, use of services provided by foreigners, foreign firms and foreign agencies, payment of profits and interests abroad, repatriation of foreign capital, investment and borrowing abroad,

X = export of commodities abroad, supply of services to foreigners, to foreign firms and to foreign agencies, receipt of profits and interest from abroad, repatriation of capital from abroad, investment and borrowing from abroad, provided that deals desired or considered profitable by those concerned are not prevented for monetary reasons, namely the inadequacy of foreign balances or the dangers deriving from the excessive demand of foreign balances by those offering funds in local currency, through appropriate steps.

b. Capital is imported from abroad or exported there in unlimited amounts for investment diversification, increased income, capital appreciation but not out of fears connected with monetary devaluation, moratoria and embargo on payments abroad, provided conditions are normal².

c. Foreign exchange rates are stable which in reality means that fluctuations are within the margin fixed over and under parity, as it happened with the gold standard and with the Bretton Woods system in the case of the currency of the countries members.

d. The balance of payments is in equilibrium. In this connection there is no agreement³ if we have to consider the current balance of

2. In that case equilibrium cannot be preserved.

3. Cf. D.J. Delivanis, *Courses of economic and monetary policy*, 4th edition, Thessaloniki, 1971, pp 190-2 (in Greek).

payments excluding capital transfers, the aggregate balance of payments including capital transfers, the balance of payments without recourse to the gold stock and the foreign balances of the banking system. Many arguments may be advanced in favour and against each of these alternatives. It looks as if the equilibrium of the current balance of payments is the best as long as capital transfers are not to be considered as normal. This however is not right as first many imports and exports of both goods and services are carried out only provided the appropriate capital transfers secure the financing needed, as second capital transfers are under normal circumstances quite normal in both ways, as third in many cases the foreign balances and the gold stock of the banking system are considered to be abnormally high or abnormally low leading to corresponding arrangements which have to be noticed in the balance of payments upsetting same without proving however that there is external disequilibrium.

The repercussions of the price and wage developments are felt on the external equilibrium in a way worth mentioning when differences develop between the country concerned and those foreign countries with which intercourse is substantial

- in the rate of inflation,
- in the rate of growth or development,
- in monetary policy when the country concerned applies inflation whilst the others wage deflation or vice versa,
- in the bargaining power of the wage earners, of the employers and of the government.

These differences must be substantial in order to lead to external disequilibrium and it cannot be said in absolute numbers or in percentages when it is so in general. It is only possible to accept that the external equilibrium of the country concerned has been upset through differences in the wage and price developments there and in the countries with which intercourse is substantial when:

1. The gold stock and the foreign balances of the banking system of the country concerned have diminished or increased sharply creating problems for the smooth carrying out of payments either of this country in the first alternative or of the other countries in the second alternative. Let me add that the fluctuations of the gold stock and of the foreign balances may be either neutralised or sharpened by capital transfers independently of the reasons inducing those concerned to proceed. A great deficit in the current balance of payments may be transformed into a substantial surplus if capital transfers occur on a great scale,

either in order to participate in the boom developing in the country concerned through excessive investments connected with the discovery of petrol, or gold, or uranium or any other commodity securing substantial profits to those producing or handling same or in order to avoid losses in the country from which capital is exported. On the other hand a substantial surplus may be wiped out by huge capital transfers if suddenly new taxes are to be levied or if devaluation rumours spread or if investments abroad are considered to be more profitable.

2. It becomes unavoidable in the country concerned to modify monetary, credit or foreign trade policy and eventually the foreign exchange rate.

In both cases we have to consider that the influence of wage and price developments cannot be separated from the influence of other factors which have not to be economic or monetary. It is wellknown that economic developments are very often connected with non economic factors in view of the connection and reciprocal influence of economic, political, social and natural developments. Let me add that capital transfers have to be cleared between themselves but if substantial balances remain commodities have to be dispatched or services have to be offered, in both cases on a greater scale than before or loans ad hoc have to be granted or at least consolidated.

III

In view of the opinions expressed in part II, I will try in part III to find out a) if the devaluation of sterling in 1967, b) the revaluation of the West German mark in 1969, c) the stability of the Swiss franc and of the United States dollar (until the end of 1970) can be interpreted by differences in the price and wage developments in the countries concerned as shown in table I.

a. On the basis of the data available in Table I we may note that the consumer price index number (all items) increased in the United Kingdom 1948-66 by 67% whilst in the other three countries the increase was only 19-29% independently of the fact that the starting point in Western Germany has been particularly low. In the same period the average earnings per hour in manufacturing of male adults increased in the United Kingdom by 258% whilst the rise amounted to 89% in Switzerland, to 375% in Western Germany (the very low departure point has to be stressed particularly here) and to 100% in

Table I

Consumer price index number (all items)

Year	1948	1950	1951	1952	1953	1954	1955	1956	1957	1958	1958	1960
Germany F.R.	100	100	108	110	108	108	110	113	106	108	109	110
Switzerland	100	98	102	105	104	105	106	107	102	104	103	105
United Kingdom	100	106	116	126	130	132	136	142	123	126	127	132
United States	100	100	100	100	110	110	110	112	108	110	108	110

Average male earnings in manufacture per hour in local currency

Germany	1.65	1.27	1.45	1.56	1.63	1.67	1.73	1.94	2.34	2.49	2.62	2.88
F.R. (D.M.)												
Switzerland												
(S.F.)	2.80	2.90	3.-	3.11	3.11	3.11	3.11	3.20	3.38	3.53	3.62	3.75
United Kingdom												
(old pennies)	31.2	33.5	36.8	39.6	41.7	44.6	48.—	56.9	65.3	67.3	70.—	76.8
United States (\$)	1.35	1.47	1.59	1.67	1.77	1.81	1.35	1.88	1.98	2.11	2.19	2.26

Consumer price index number (all items)

	1961	1962	1963	1964	1965	1966	1967	1968	1969	1970
Germany F.R.	113	117	119	122	125	129	132	134	137	143
Switzerland	107	111	115	118	121	126	131	134	140	145
United Kingdom	132	148	151	154	162	167	172	178	189	205
United States	111	112	113	114	116	119	122	126	132	141

Average male earnings in manufacture per hour in local currency

Germany F.R. (D.M.)	3.08	3.53	3.77	4.10	4.49	4.80	4.99	5.19	5.72	6.38
Switzerland (S.F.)	3.90	4.21	4.39	4.93	5.29	5.29	5.76	6.11	6.44	—
United Kingdom (old pennies)	81.5	84.9	88.7	95—105	111.8	116—123.8	134—154.5			
United States (\$)	2.32	2.39	2.46	2.53	2.61	2.72	2.83	3.01	3.19	3.36

Source: International Labour Office as reproduced in the monthly bulletins of the United Nations.

the United States. Under these circumstances it seems that the devaluation of sterling 1967⁴ was justified by both the development of the prices and of the earnings inasmuch as the productivity rise was not substantial in the United Kingdom. It has to be added in this connection that during the years 1964-7 the balance of payments of the United Kingdom was showing substantial deficits, the welfare expenses

4. I will not deal with the 1949 devaluation of sterling as the latter was the result of the action of many factors connected with the financial repercussions of World War II on the United Kingdom economy.

increased substantially and strikes were reducing the output of the United Kingdom' economy and the latter's reliability as far as the carrying out of accepted orders was concerned.

b. When looking to the revaluation of the Denmark in October 1969 the latter may be justified only in connection with developments in the United Kingdom but not with those in Switzerland and in the United States except if accepting that the price and wage rise in Germany started in 1948 from very low levels, was combined with substantial productivity rises and did not prevent the appearance of substantial and growing surpluses of the balance of payments. Another argument against the 1969 revaluation of the Denmark is that it did not stop price and wage increases in Western Germany but it has to be stressed that developments within one year are not enough to conclude.

c) The stability of both the Swiss franc until 1970 and of the United States dollar may be perfectly justified by data available as long as price and wage rises were not higher than those prevailing in other countries and as both were able to increase substantially their productivity. Whilst the connections both commercial and financial of these two countries with foreign countries are very important, they affect substantially the various aggregates only in the case of Switzerland. Developments however in both countries have shown that both may disregard developments in their respective overall balances of payments as long as the United States may always and indefinitely pay their creditors in dollars in New York and as long as the note issue of the National Bank of Switzerland was covered by more than 100% in gold until May 5, 1971.

Conclusions

It seems appropriate to conclude that price and wage developments even if strong are not catastrophic for the external or for the internal equilibria of the country concerned provided in the case of the external equilibrium a) she is not a single walker and b) differences with other countries are not excessive, in the case of the internal equilibrium fluctuations are not excessive.

The internal and the external equilibria are more upset by deficits than by surpluses of the balance of payments and the latter more than the former. It is easier for the authorities of the country concerned to cope with surpluses than with deficits. The sterilisation of foreign capital, the combination of capital inflow with the restriction of the credits granted by the central bank and with the repayment of Treasury

bills and Treasury loans to the central bank, the issue of loans through public subscription and the use of the proceeds for the repayment of central bank loans, tax increases whose proceeds are affected in the same way, last but not least the reduction of public investments are available. Of course each of these steps is connected with difficulties or with public expenses reducing the possibilities of welfare. Only the sterilisation of foreign funds, as shown by the experience of Switzerland, does not create difficulties provided the commercial banks cooperate sincerely. The restriction of central bank loans particularly in developing countries is so difficult that the interruption of the increase is already, if carried out, considered satisfactory. Increased taxes are certainly not easily enforced particularly when the proceeds will not help anybody. The limitation of public investments may be considered; that of public consumption is not possible as long as nobody is disposed to accept a cut in disposable income in order to contribute to the realisation or preservation of equilibria whose importance from the microeconomic point of view will be felt only after a relatively long time.