

# **ECONOMIC PROSPECTS FOR THE THIRD WORLD**

The 1984 Forecasts  
Trade and Recovery

Sheila Page



00010196



Overseas Development Institute

**ECONOMIC PROSPECTS FOR THE THIRD WORLD**

**The 1984 forecasts**

**Trade and recovery**

**Sheila Page**

**OVERSEAS DEVELOPMENT INSTITUTE**

**Report prepared for discussion at an ODI Conference, 2 October  
1984. Not to be quoted without permission.**

**Overseas Development Institute**

**10-11 Percy Street  
LONDON W1P 0JB  
Tel: 01-580 7683**



## CONTENTS

PATTERN OF THE RECOVERY	1
THE FORECASTS	3
Output and trade	
Prices and Balances	11
Financing	13
Medium Term Scenarios	18
Special features of the 1984 publications	21
POLICY ISSUES	22
The effects of the recession within developing countries	
International financial issues	23
The role of trade	25
CHANGES IN TRADE RELATIONSHIPS	27
Empirical evidence	
The characteristics of the 1983-5 recovery	31
Long-term changes in industrial structure	34
Protection and other institutional changes	36
Conclusions	45
APPENDIX: FORECASTS DISCUSSED AND DEFINITIONS	47



### THE PATTERN OF THE RECOVERY

The consensus of the forecasters is that the recovery of the industrial countries from the recession of 1980-82 is coming to an end. After the 'rapid'<sup>1</sup> growth of last year and the first half of 1984, they are slowing down and by 1985 they will have returned to the rates observed in the years following the first oil price rise. There will thus not be a complete recovery from the recession in the sense of a reduction of unemployment to pre-recession levels. These levels themselves reflected the similar lack of a full recovery from the 1974-5 recession. There is still no resumption of the rate of productivity rise seen before 1973. The developing countries will not enjoy even this partial recovery. They are recovering to their 1970s rates of growth, but without the year of faster growth achieved by the industrial countries. They also reach the rates of growth now seen as normal during next year and, under present policy forecasts, maintain them during the medium term.

The ratio of import growth to output growth for the industrial countries also reaches a peak this year (of over 2 on the most recent forecasts), and then falls back. Inflation which has fallen during the recovery does not (on most forecasts) change further in either direction as the industrial countries return to steady growth, and the relative rise in commodity prices comes to an end, but is not reversed.

In contrast to the industrial countries which grew more than expected last year, and are continuing to do so this year, the developing countries' output rose less than forecasters expected in 1983, and forecasts for this year have been lowered. The only exception has been some of the low income countries (especially south Asia). Thus the return to normal growth next year for most developing countries will be from a substantially lower base than was anticipated in the 1983 forecasts, and, with views of what is normal also lowered, the long term prospects for their output are significantly worse.

---

1. Although it is difficult to avoid falling into 1984 terminology, it is essential to remain aware that the OECD growth expected this year by the highest forecaster in table 1 is less than the average for 1963-73, while the 7% growth in world trade is about equal to the average.

Their low growth last year and the unexpectedly large rise in their terms of trade have, however, given them a large improvement in their trade balances. Although some of this was offset by the unexpected rise in interest rates, there was also a greater than expected improvement in their current balances. But with little further change expected in their terms of trade or real trade balances, these also are merely carried forward as a step-change from the past.

The results for 1983-4 and their implications for the future have contributed to increased interest in the relationships among output in the industrial countries, their trade, prices of traded goods, and the trade and output of developing countries. Both the actual performance in the last two years and the different forecasting errors suggest that the impact of the industrial countries' recovery on the volume of developing countries' exports has been much less than in the past; the effect through prices (which benefits the countries which are still mainly exporters of primary commodities more) may also be relatively lower, but this change seems less important than was thought. All the forecasters this year discuss possible explanations for these observations, and most consider this an important area of uncertainty for the future. The final section of this paper will describe the types of explanation that have been offered, in the 1984 reports and in other recent studies of trade. It is clear that the distribution among the industrial countries of the current recovery must be part of the explanation, in particular the unusually wide gap between rates of growth in the United States and in Europe. But this may not be a sufficient explanation because this should have been taken into account in the forecasts. There is a wide variety of possible explanations for a change in the 'transmission mechanisms' between the developed and the developing countries, some of which seem to be directly linked to either the nature of the recession or the type of recovery, while others are more structural. The work that is being done is leading to greater awareness of possible effects, and therefore to more useful discussions in the reports of the nature and size of the uncertainties attached to their forecasts, but there are no firm conclusions.



## THE FORECASTS

### Output and trade

For 1983, most forecasters had initially (in 1982) expected the industrial countries to grow at 3% or over, but by last summer forecasts had been reduced to around 2%. United States growth, however, was even stronger than expected in the second half of the year raising the average to about 2½%. Its growth has continued to be stronger than expected, and forecasts for 1984 have risen from 3-3½% last year to 4-4½% for the most recently published (table 1). There have been roughly 1% increases in the forecasts for Japan, and Western Europe is still expected to grow about 2%. The slowing in output has been postponed from original expectations for the end of 1983 to summer 1984. By 1985 (table 2) forecasts are all back to around 3%. The United States and Japan slow down, and Western Europe remains around 2-2½%.

The cycle is thus effectively confined to North America and Japan, which move very closely together, with Europe's growth remaining virtually flat. Under the present policies, medium-term forecasts (IMF base; World Bank Low; IDB and NIESR), average growth then remains between 2½ and 3% (table 3) which is viewed as approximately in line with the present growth in productivity (slightly higher for the IMF's 3¼%), although not necessarily the limit of what could be achieved. (This is discussed further in the section on the medium-term scenarios). These forecasts, which are generally similar to those made last year, are realistic in the sense that they are in line with recent experience and the apparent present intentions of the industrial countries' governments. But keeping the assumption about a return to normal, and merely pushing it forward as actual changes fail to conform with it, is disturbingly like the failure of forecasters in 1980-1 to perceive the onset and duration of the 1981-82 recession.

The 1982 forecasts for 1983 imports by industrial countries were too high because of too high output forecasts (UNCTAD) or too high elasticities (OECD and NIESR). By mid-1983, all were much too low (by at least 2 points) because of both too low output and too low elasticity forecasts). They appear to have grown by about 4% in volume, about 1.6 times the rate of output growth. This double failure

to get the elasticities right (except by UNCTAD in 1982) has prompted much of the current interest in whether there have been changes in the relationship between imports and output. The most rapid growth, and increase in apparent elasticity, was by North America, but Germany and the UK were also quite high. For 1984, the forecasts made last year were generally around the recent trend 5% (except for the UN which assumed only 3½% with a growth of output of 3%), but they are now unusually divergent (from 3%, and less than output, for IDB, to 9.4%, more than twice as fast as output, for NIESR). Except for the most recent (UNCTAD), the forecasts have risen as the strong performance by the US in the first half of this year became obvious. OECD and NIESR put the US rate at about 20%, and even higher numbers would be consistent with the most recent evidence. A rapid growth in imports at this stage of recovery, and in particular a very large rise by the United States (1976: 22%; 1977: 10%) is not unusual, although the difference between the US and the European countries' performance is, for trade and for output. Once again, the rate is expected to come back down to around 5% in 1985.

Industrial countries' export volumes grew about two points less than imports last year, and are generally expected to have a similar differential this year, but to return to about the same or even a higher rate next year and in the medium term. This means that the main opportunity for non-industrial countries to benefit either from rapid growth in industrial countries' demand or from large net demand from them is nearly past.

Import demand by the major oil producers fell 10% last year, at the most pessimistic end of forecasts. There is again a wide range in forecasts: some forecasters now expect a further fall this year. Most expect a recovery next year: although the real oil price forecasts suggest a continued fall, demand for oil may be recovering.

The higher demand by industrial countries resulted in a faster than expected growth in world trade volume last year (2% compared with forecasts of around 0-1%), and this will probably be repeated this year; the highest forecasts (of around 7%) are still low even by the standards of recoveries in the 1970s. This rate is not expected to continue. Two forecasters with relatively low rates for 1984

Table 1

Forecasts for 1984 (Percentage growth rates)

	UNCTAD	IMF	OECD	UN	IDB	EIU	NIESR
<u>Developed countries</u>							
Output	3.9	3.6	4½	3.8	3½	< 3.5	4.6
US	5.6	5.0	6	5.5	5.0	4.5	7.2
Japan	4.5	3.9	4½	4.5	4.0	3.9	5.0
W. Europe	2.1	1.9	2½	2.1	1.0	1.6	2.2
Consumer prices	5.5	4.9	5½	4.8			5.3
GDP deflator		4.5	5	5.4			
Import volume	5.8	6.5	9	5	3	4½	9.4
Oil exporters' import volume	-1.3	1.0	-5	3		-2	
World trade	5	5.5	7	4		3.5	7½
Trade in manufactures			8			> 3.5	8½
Oil price, US\$	0	-1.5	-2	0		< 0	-3
real	< 0	-2	-2	-6			-3
Price of manufactured exports	> primary	1	0	6	4	3	0
Price of primary products	> 0; < 6	7	8	6	2		5
Food		8.6	} 9	1			} 9
Tropical beverages		6.1		11			
Vegetable oil seeds & oils			21	10			
Agricultural raw materials		8.6	5	6			1
Minerals, ores, metals		4, 4	1	2			-2
<u>Non-oil developing countries</u>							
Output	3.2-3.5	3.5		3.5			
Export volume	6.7	7.0	7	4-5		4	
Import volume	4.9	5.5	6	2		2	
Export prices	1.3	2.9	5	4.5			
Import prices	0	1.5	3	4			
Terms of Trade	1.3	1.4	2	0.5		> 0	
<u>Output by group</u>							
Secondary oil exporters	3.5	2.4					
Major exporters of manufactures	2.3	2.5					
Low income	3.9	5.8					
<u>Output by area</u>							
Western hemisphere	6.9	1.3		3.0 <sup>a</sup>	-0.5(-0.2) <sup>b</sup>		
Africa	2.7	3.5		2.5 <sup>a</sup>			
Asia	5.2-5.6	6.1		5.5 <sup>a</sup>			
<u>Exports by group</u>							
Secondary oil exporters	7.2	6.8	6	4		> 4	
Major exporters of manufactures	7.8	8.4	8				
Other	5.2	7.5	5				
<u>Exports by area</u>							
Western hemisphere	4.7	6.9			5		
Africa	5.3	6.6					
Asia	6-6.9	8.6					

GATT , World Trade 5-6

Notes: a - 1984-5

b - See text for explanation.

(the UN and UNCTAD) do expect faster growth in 1985. This may reflect differences in views over the speed with which trade would respond to the revival in output rather than more fundamental differences, but they are a useful reminder that changes in trade do tend to lag behind those in output, so that a deceleration in output from now into 1985 might not be accompanied immediately by a corresponding movement in trade. Trade in manufactures rose substantially faster last year (4%) and is expected to continue to rise at its traditional 1 point differential above the total. The general 'external environment' for the developing countries that emerges from the output and trade forecasts for the other areas is thus a growth in demand of around 5%, with little further addition to be expected from changes in their own export performance.

In sharp contrast to the results for the industrial countries, output growth in the developing countries was lower in 1983 than was expected even a year ago, and much lower than the earliest forecasts, made in 1982. Most estimates now put it between 1 and 2%. Forecasters still expect an improvement this year, but only to 3-3½%, not to 4%. A further improvement is expected for 1985, except apparently by the UN (although its 3½% may be intended to be a view for the average of the 2 years), but only to around 4½%. The exception is the World Bank, whose forecasts for 1980-85 imply an average of 4½% for the two years 1984-5. For the medium term, growth remains around 4½%, slightly higher than the IMF's forecast last year, but well below the World Bank's 1983 central forecast of 5½%. Thus no period of rapid recovery is expected in these countries as a consequence of that in the industrial countries. This result appears quite realistic in the light of the developments so far, but it is unusual historically and therefore provides further reason for concern over possible changes in the linkages between industrial and developing countries. It could be interpreted as evidence for a more long term linkage: the developing countries reduced their growth during the second half of the 1970s by less than they 'should' have done when industrial country growth fell, and therefore have less to recover from.

The lower growth than expected in 1983 was accounted for mainly by Latin America (whose output probably fell 2½%), although Africa also did less well than forecast (at about 0). Asia, especially the low

Forecasts for 1985

	UNCTAD	IMF	OECD	UN	IDB	NIESR	World Bank 1984-85 <sup>c</sup>
<u>Developed countries</u>							
Output	2.9	3	2½	3	3	3.2	3.5
US	3.1	4	2½	3.5	3.1	3.5	
Japan	3.5		3½	4.0	3.5	4.5	
W. Europe	2.3		2½	2.4	1.4	2.5	
Consumer prices	6.0	4½	5½			5.3	
GDP deflator		4.5	5	5.1			
Import volume	5		5½	5.5	5	4.6	
Oil exporters' import volume	-6.1		4	5			
World trade	5.5		5½	5		5½	
Trade in manufactures			6½			5½-6	
Oil price, US\$	0	0	0	5	9	0	
real	< 0	-4	-3	-1	2	-(4½-5)	
Price of manufactured exports	0<M<6	4	3	6	7	4½-5	
Price of primary products	0<P<6	3	6	1	3	1	
Food			6	0		-1	
Tropical beverages				-3			
Vegetable oilseeds			2	-12			
Agricultural raw materials			4	6		1	
Minerals, ores, metals			7	8		3	
<u>Non-oil developing countries</u>							
Output	4.4-4.9	4½		3.5			4.5
Export volume	6.2	>7	5	5-6			9.4
Import volume	2.6	6	6	4			9.7
Export prices	-0.4	<3	4	4			
Import prices	0		4	5.5			
Terms of trade	-0.4	0	0	-1.5			
<u>Output by group</u>							
Secondary oil exporters	4.9	> 3.5					7.8
Major exporters of manufactures	4.4	> 3.5					2.4
Low income	3.9	5.8					5.9
<u>Output by area</u>							
Western hemisphere	3.0	> 1.3		3.0 <sup>a</sup>	3(5.3) <sup>b</sup>		
Africa	3.3			2.5 <sup>a</sup>			3.7
Asia	5.2-6.2	6		5.5 <sup>a</sup>			6.3
<u>Exports by group</u>							
Secondary oil exports	7.1		5	5			
Major exporters of manufactures	7.4		6				
Other	2.1		4				
<u>Exports by area</u>							
Western hemisphere	4.2				6		
Africa	3.0						
Asia	5.5-7.7						

Notes: a - 1984-5

b - See text

c - Derived from 1980-5 forecasts and 1980-3 actual.



income countries of South Asia, but also the East Asia industrialising countries, did better than most forecasters expected. The revisions downwards in the 1984 forecasts follow the same pattern so that the forecasts now all expect a very wide spread this year, with Latin America again the lowest. Both it and Africa are, however, expected to do slightly better than last year, while the Asian countries maintain their relatively good performance of 5-6%. The further improvement in 1985 again comes from Africa and Latin America. The divisions by group, which are not completely comparable among the forecasters, again show the unexpectedly good performance by the lowest income groups (although not published separately the IMF's implied forecasts for China and India are clearly very high) and poorer performance by at least some of the exporters of manufactures. The medium term forecasts in general do not expect either the good performance by the poorest countries or the wide spread among the different groups to continue.

The growth of developing countries' exports in 1983 was faster than was expected a year ago, and about in line with the normal rates of 5-6% found in many of the 1982 forecasts for 1983, but their performance relative to industrial countries' total imports or to world trade was not as good as expected by UNCTAD, the IMF, or OECD; although the errors were larger for the UN and EIU, the relationships may have been nearer. Although data are still very incomplete, it appears that Asia did best, followed by Africa, and then Latin America. At an aggregate level, the first two gained in market share, and this probably is true if the composition of the increase in developed countries' imports into individual countries' imports of manufactures is calculated, but the increase in share must be considerably smaller than at first sight because of the importance of the rapidly growing US market for the developing countries.

OECD (p 134) have published a table comparing export growth of the individual OECD countries and of the non-OECD groups to the weighted average of growth in demand for manufactured imports in each country or area's markets. According to this, the rapid growth in US imports meant that developing countries' markets grew even faster than their exports in 1983 so that on this stricter measure they lost share.

The same calculations give a growth of  $14\frac{1}{2}\%$  for their markets this year so that even the OECD's high expectation of  $9\frac{1}{2}\%$  for their manufactures would imply a further fall. There appear to be some problems in this calculation (perhaps arising out of averaging the very large changes and relative changes), as it shows both OECD and total non-OECD exporters losing market share in both 1983 and 1984, which seems inconsistent, but they confirm that the real gain in share, after discounting the extra growth because the area's markets are growing relatively rapidly, is at best quite small. This distinction is clearly important for the future when the differentials among industrial countries' growth, and US growth in particular, are assumed to fall, and therefore the potential gains from composition effects will be reduced or eliminated. Only the IMF and the World Bank appear to expect significant gains in market share in 1985, and even these appear not to continue into the medium term, although the forecasts are not explicit. This is a change for both forecasters from their 1983 views.

In 1984 and 1985 Asian exporters are again expected to do best, but exporters of manufactures are expected to do better than the low income countries in the medium term, increasing their share of aggregate markets while the poorer countries' share continues to fall.

The forecasters have generally regarded exports of manufactures to be more sensitive to changes in the rate of growth in the industrial countries than those of primary products for the usual reasons of little opportunity for market share increases for basic commodities and higher income elasticities for newer or more differentiated products. Therefore, other things being equal, the errors in the forecasts for 1983 and the revisions for 1984 for the industrial and developing countries appear to go in inconsistent directions.

Estimates for import volume in 1983 still vary widely, and are likely to remain uncertain because of the large movements in relative prices and exchange rates, but it seems probable that low income countries in Africa and Asia and Latin American countries suffered falls, while the East Asian countries probably rose. Aggregate growth must have been very low. This would be in line with the estimates for output

growth, and also with the lowest forecasts made last year. In all areas and probably all the groupings, the net effect of export and import changes was an improvement in the volume balance of trade. In 1984, most forecasters expect much larger rises in imports but these are still smaller than the changes in exports so that balances continue to improve. This is also true by area; although Western Hemisphere imports may grow more rapidly than exports, the improvement last year was sufficiently greater than the other areas for the performance over the two years to be comparable. By 1985, these improvements come to an end (except for the UNCTAD forecast which gives all parts of the world an improvement, by substantially cutting the observed 'world deficit') and with industrial countries' imports and exports growing at the same rate, developing countries' trade does the same. In the medium term, both the World Bank and the IMF allow some deterioration (through increased financing). The period of high stimulus from net foreign demand has effectively come to an end.

As expected, export volumes grew much faster than output in 1983 and are expected to continue to do so this year and next, but the differential is either greatly reduced (IMF) or eliminated (World Bank) in the medium term. This is a significant change from the 1983 medium term when both expected export volume to grow significantly faster. On the import side, the medium term forecasts now imply lower elasticities than in last year's forecasts; the forecasts for output have been reduced by less than those for imports. Both are now well below the figures usually assumed for industrial countries with the World Bank the lower. Although the ratios are not out of line with the period 1967-76, used as the long-term trend in the IMF tables, or with the years since 1981, periods including the first oil price rise and consequent oil saving or a deep recession with financing crisis may not be typical, and for other periods including the late 1970s higher elasticities are observed. If the imports are treated as the constraint (given by exports and financing limits), this suggests that the output forecasts may be inconsistently high.



### Prices and balances

Inflation in 1983 in the industrial countries proved to be much lower than expected (except by NIESR); differences in definitions and in treatment of exchange rate changes explain part, but not all of the errors. Consumer prices probably rose about 5½%. Forecasts for 1984 have been lowered to this level, but no longer imply a decline between the two years. This change in pattern can be regarded as consistent with the greater pressure from rising demand now expected. No change or very small rises are expected in 1985, with some forecasters treating rises as part of the cause of the slowing (inflation effects on consumers' asset holding decisions), while for others they must be viewed as 'in spite of' the fall in growth. This difference emerges more starkly in the medium term forecasts with the World Bank having a high rate in its basic low forecast (and a lower one in its more optimistic scenario), while the IMF and NIESR have lower inflation rates than in recent years in their basic forecasts.

The lower inflation is one explanation for lower prices of manufactured exports in 1983-84 than were expected last year, but the rise of the dollar, in which these are expressed, is more important. These fell last year by 4%, the third successive year of decline, and it should be noted that as late as summer 1983 none of the forecasters expected a fall, although OECD had no rise. Forecasters last year expected manufactured export prices in 1984 to rise by slightly less than domestic inflation in the industrial countries, and this remains true (except for the UN), but the further rise in the dollar has meant that some forecasters again expect little or no change. Most forecasters continue to expect this traditional relationship in 1985 (the UN and IDB are exceptions), and with no further changes in the dollar (by forecast or conventional assumption), the rate rises, but the spread among forecasts is remarkably large, from 3% for the OECD to 7% for the IDB. In the medium term, the World Bank expects a more rapid rise, while the IDB reduces the differential, but both organisations' expectations of a general rate of inflation of around 7% give them very high forecasts. The IMF expects no difference,

and NIESR the more usual negative difference; both have lower general inflation forecasts giving figures of 4-4½%. This spread for the medium term is unusual, and is particularly important at present because of the effect of high or low inflation on the burden of debt.

The oil price did not change in the second half of last year, so most forecasts were quite close to the dollar change, although the unexpected fall in manufactures' prices meant that the real fall was only 9-10%, rather less than expected. In 1984, the dollar price is probably slightly lower on average for the year than in 1983, although the UN and UNCTAD assume no change in the nominal price, so the small rise in manufactures' prices give a small real fall (or a large one on the UN forecast). In 1985, most forecasters expect the dollar price again to remain unchanged, giving a larger real fall if manufactures' prices do rise. The UN has a smaller fall, and the IDB expects a resumption of the real rise. The 1984 and 1985 forecasts are clearly subject to some uncertainty given the further rise in the dollar since they were made which would reduce the manufactures' price rises (because non-US exports' prices would rise less in dollars) and therefore the real fall in the oil price (if this does not adjust). In the medium term, the IMF and NIESR continue to expect no change in the real price, while the IDB has a small rise.

The prices of other primary products rose even more strongly than the highest forecasts expected in 1983, at about 6%; combined with the lower than expected manufactures' prices, this gave a real rise of 10%. A further relative rise is still expected in 1984 (except by UNCTAD and the IDB, although both only give indications in the text of the direction and probable magnitudes of the changes), of at least 6-7%. These are smaller taken together than the real rises in 1976 and 1977 (about 10% and 16%, Table 4) but the recovery is weaker. In both 1983 and 1984 the rise appears to be confined to food and other agricultural products, with only modest changes observed or expected for minerals and metals. In 1985 most forecasts expect the rises to be less than in 1984 and less than manufactures (except the OECD). In the medium term there is no agreement on whether they will grow faster, more slowly or at the same rate.

The rise last year contributed to an improvement in developing countries' terms of trade as most had expected, although it was relatively small (probably 1-2% although again there is still substantial variation in estimates). It seems probable that it mainly benefited the exporters of primary products, but even this is not clear from the estimates. All forecasters expect a further improvement in terms of trade this year, although as usual the rise in market prices is only partially carried through onto export prices, and further reduced by the shares of manufactures (40%) and oil (20%) in total exports. In 1985 and the medium term little change is expected. Thus the contribution of relative prices to developing countries' balances is coming to an end at the same time as that of real changes in exports and imports.

Arithmetically, these results give us the path of the trade balances forecast for the developing countries, although almost all the forecasters now emphasise that in terms of causation the line runs from available financing: export growth, terms of trade, and transfers and capital flows, to imports (IMF, p 160, states this particularly clearly). The IDB forecasts are not based on available financing, but rather derive the need for this from the implied balances. Under them, borrowing, presumably from banks, would need to rise (under either scenario) in order to pay the interest on existing borrowing, although the area would be in trade surplus. In 1983 the largest improvement was in Latin America, but it applied to all developing areas (helped by a reduction in the world discrepancy on payments, so that the estimates must still be regarded as particularly uncertain). A further, but smaller improvement should come in 1984, with little change after that. The current balance changes are smaller than those in the trade balances particularly this year because of the rise in interest payments.

#### Financing

The large changes in private financing are now assumed to be in the past, and the 1984-5 and the medium term forecasts are generally built around stable flows for the future. Official grants have remained approximately constant, and IMF and UNCTAD expect them to remain so in real terms. The World Bank assumes they will rise at 2½%, in line with

the growth in industrial countries' GDP, a rather better performance than in recent years, but less than it expected in the 1983 forecast. This implicitly also assumes a resumption in growth of OPEC aid. Direct investment fell sharply in 1983, from \$11 billion to \$8 billion according to IMF figures, and by a similar amount on UN estimates, but the UNCTAD estimates disagree, and it is difficult to reproduce the IMF figures from data for individual countries. Whatever the base figure, the forecasters do not expect major changes in the future. The IMF assumes it will grow 5% in real terms, 9½% in nominal. The World Bank does not state its assumption.

IMF credits, which rose from \$7 to \$10 billion in 1983 are expected to fall to \$7 billion this year and back almost to their pre-crisis level in 1985, about \$2½ billion. This reflects both the policy of treating the increased role for the IMF as a temporary response to crisis, not the beginning of a permanently increased participation, and the reality of the failure to increase its resources. Any new crisis lending must therefore assume repayment by existing borrowers. The IMF assumes that trade credits will grow in line with imports. The UNCTAD report points out that the reductions in the subsidy element in these has reduced their absolute attractiveness to borrowers, but possibly not their relative use because of the reduction in availability and increase in costs of other sources of funds.

The developing countries do appear to have increased their reserves in 1983 as was forecast (and the decline in the value of their imports implies a larger increase in the import coverage): and a further increase is expected this year, so that the growth of imports has been slightly less than implied by export growth plus available financing. These two years' increases may be sufficient to restore (on average) their position to an almost acceptable level, so that further drains on their ability to import may be rather smaller. The IMF assumes a small further rise in the medium term.

The UNCTAD report (pp. 53-54) attempts to divide the bank lending in 1983 and early 1984 between 'managed' (reschedulings; loans associated with IMF packages) and 'spontaneous' lending by banks as an indication of real ability to borrow. It estimates 'spontaneous' gross borrowing in 1983 at \$9.7 billion compared to \$21.9 billion in 1982. In the first quarter of 1984, the annual rate is estimated to have contracted

slightly further (\$6 billion). For its short term forecast, it assumes both managed and spontaneous lending remain at these levels, but this disaggregation provides a clear warning of potential changes if the managed component declines. It also points out that the relatively unchanged average terms and conditions of developing countries' borrowing is the result of more favourable terms on the managed offsetting less favourable on the rest. The IMF assumes (p 70) that the level of net bank loans will remain unchanged in real terms or (p 158) that it will rise 3% a year which with its low inflation forecasts gives a very small possible inflow, consistent with the indications in the UNCTAD discussion.

The short-term forecasters avoid attempting to forecast interest rates, although they emphasise the large effects which changes can have on the current balances and prospects for debt repayment. Effectively most appear to assume something like unchanged rates from the time of the forecast, which probably implies falls from present rates. In the medium term, particularly when the forecasts are based on maximum available funding for deficits or target debt-service ratios, forecasts are difficult to avoid. The IDB says it uses independent forecasts, but does not specify them precisely (cf pp 66-7). The World Bank forecasts the real rate at 3½% because of the large US budget deficits: added to its inflation forecast for industrial countries in own currencies of 6% this gives a nominal rate of 9½% for eurodollars. The rate paid by developing countries could presumably be higher because of the differentials charged to them. The IMF assumed an unchanged rate on bank credits to developing countries from the end of 1983 through 1984 and 1985, falling through 1986 and 1987 (to give an average for the two years 2 points lower) and then more slowly in 1988-90, to give an average for those years a further 1 point lower. As part of this is considered to be a reduction in spreads for developing countries, and inflation in the industrial countries falls by around a point, the implied fall in real rates is quite small. This is assumed to be explained by some reduction in the US and other budget deficits. Both these forecasts obviously imply considerably larger falls from present (early September 1984) real and nominal rates.



Table 3

Medium Term Forecasts (Percentage growth rates)

	World Bank 1985-95			
	High	Low	Low I	Low II
<u>Developed countries</u>				
Output	4.3	2.5	2.5	2.5
Deflator	4.3	6.8	6.8	6.8
Import volume				
World Trade	7			
Trade in manufactures				
Oil price, US \$ real				
Price of manufactures		9	9	9
Price of primary products		7	7	7
Aid plus bank credit expansion/year	2.5	-1	-1	-1
<u>Non-oil developing countries</u>				
Output	5.5	4.7	4.3	5.1
Export volume	6.4	4.7	4.0	5.1
Import volume	7.2	5.1	4.3	5.4
Terms of trade		-1	-1	-1
Debt service at end/exports	12.7	13.7		
Exports of manufactures	9.7	7.5	6.1	8.0
Exports of primary products	3.4	2.1	2.2	2.4
<u>Output by group</u>				
Secondary oil exporters	5.4	4.7	4.6	5.0
Major exporters of manufactures	6.3	5.2	4.4	5.7
Low income countries	5.1	4.4	4.0	4.8
<u>Output by area</u>				
Western hemisphere				
Asia, low income	5.3	4.6	4.2	4.9
Africa, low income	3.2	2.8	2.6	3
<u>Exports by group</u>				
Secondary oil exporters	4.1	2.4	2.2	2.7
Major exporters of manufactures	8.2	6.3	5.2	6.8
Low income countries	6.8	5.2	4.3	5.6
<u>Exports by area</u>				
Western hemisphere				
Asia, low income	7.5	5.7	4.7	6.1
Africa, low income	3.3	2.2	2.1	2.5

For explanations of alternative projections see text.

IMF Base			IMF Alternatives			IDB	NIESR
1985-7	1988-90	1985-90	Pessimistic	Crisis	Weak policies	1986-90	Nov 83 1985-8
		3½ 4	2½	2½	3½	2.5	2½ 5
						3.5	4½ 5
		4 0	4 0	4 0	4 0	9 2	5 ½
		4	4	4	4	7	4½
		4				7	6
		0					
4.6	4.6	4.6	3.5	3.7	4.8		
5.4	5.3	5.4	3.4	3.4	4.4		
6.2	6.1	6.2	4.2	4.5	7.2		
0.1	0.0	0	0	0	0	0	0.5
		22.7	22.7	22.7	23.3	21(27.3)	
4.5	4.5	4.5					
4.3	4.3	4.3					
3.5	3.5	3.5					
						2.7(5.4)	
2.6	3.0	2.8					
6.9	6.5	6.7					
4.7	4.0	4.4					
						4.5	

### Medium term scenarios

The IMF, World Bank and IDB present more than one medium term forecast based on different assumptions about behaviour in the industrial or the developing countries. The IMF presents both simple sensitivity analyses to particular changes in the base case assumptions and three alternative forecasts (given in table 3) based on particular sets of changed assumptions. For each it calculated the results on the basis of either no change in imports and output in the developing countries, giving financing consequences, or no change in financing, deriving the consequences of this for imports and output. Its scenarios and all but one of its sensitivity analyses were chosen to show less favourable results than the base case, suggesting that it sees most of the uncertainties in this direction.

A 1% p.a. lower growth in industrial country GDP reduces developing country exports by 2% which would require imports to grow at a rate lower by  $1\frac{1}{4}\%$  and developing country output by 1%, effectively a 1 for 1 reduction in output. 1% higher commercial interest rates (with no change in official rates) in each year would give a once for all cut of  $1\frac{1}{4}\%$  in imports and  $\frac{1}{2}\%$  in GDP. 10% higher oil prices would give once for all falls of 1% for imports and  $\frac{1}{4}\%$  for GDP. If a reduction in protection permitted exports to grow 2% faster, imports would grow 1.8% faster and GDP 1% faster.

The pessimistic scenario combines the assumption of lower industrial growth with higher interest rates, and, as shown in table 3, no change in financing, reducing developing country output by more than 1% p.a. It is pointed out that further effects could come if low growth led to higher protection, and lower exports by the developing countries to a decline in confidence and a reduction in financing. The crisis scenario combines slower growth with a cut in lending (and is elaborated in the form of a cyclical recession centring on 1987). The 'weak policies' scenario does not specify what the developing countries do, but the result is lower exports and higher imports and, although this is not pointed out, higher growth; as in the oil price sensitivity analysis, the first 1% change in imports produces only a  $\frac{1}{4}\%$  change in GDP. The implied non-linear elasticities of the other sensitivity analyses suggest that only slightly weaker policies are necessary to get a



worthwhile increase in growth.

The World Bank offers a High case which assumes policies in the industrial countries to remove the obstacles to 1960s rates of growth; the World Bank identifies these as high budget deficits, and consequent high interest rates and inflationary expectations; rigidities in the economies, such as subsidies or protection of obsolescent industries; and high wages. The implied model is not elaborated. If growth in the industrial countries were raised to 4.3% with an inflation rate of only 4.3%, world trade would grow at 7% a year, compared with only 5% in the 1983 World Bank central forecast of 3.7% for industrial countries' output. This would improve developing countries' prospects in real terms, by raising demand for their exports; in relative price terms (although the amount of the increase in real prices for their exports is not specified); and in financing terms, by being associated with lower real (2½%) and nominal (6%) interest rates. Capital flows would also increase, because aid would rise in line with the GDP forecast and direct investment with the lower interest rates. (The latter would apparently not be adversely affected by the decline in the differential between developing and industrial country growth rates). Protection would also be reduced and the assumption is apparently that it would even fall at a faster rate than in the 1960s, explaining the faster rate of growth of trade relative to output than was observed then (p 37). Although developing countries' exports would not be able to achieve the rate of growth, in absolute terms or relative to world trade, assumed in the 1983 central forecast, their growth of 6½% would still permit the same import growth of 7.2% and output growth of 5.5%. The debt service ratio would be lower than in the base or low case. The greatest benefits would of course go to the exporters of manufactures, but all areas would benefit significantly because of the widespread nature of the changes.

If the low growth of the base scenario leads to higher protection and therefore lower exports, scenario Low I suggests that imports reduced by 0.8% would reduce output by 0.4%. Further consequences of this change are not worked out in the detail of the High forecast, for example possible consequences for terms of trade or creditworthiness. It is not clear from the various mentions (p 34 particularly) of the effects of protection in the developed countries whether its expected growth, under all the Low cases, is or is not a barrier to increasing exports. It 'threatens' the exports, but apparently does not 'limit'

them (p 43). Low II assumes 'improved performance' in the developing countries, with an unchanged forecast for the industrial countries. (At least, it is unchanged net: they would presumably have an increased turnover of trade to match that of developing countries, unless this was entirely South-South trade) The greater elaboration (p 41) by the World Bank than the IMF of what it means by better policies in the developing countries does not really make it clear what happens. They permit a 0.3% rise in imports and no change in the real or nominal external balance to be associated with a 0.4% rise in output; exports of primary goods are increased by 0.3% apparently without any change in prices or in demand in the industrial countries.

It may be unfair to point out that both the IMF weak policies and the World Bank improved policies lead to higher growth in the developing countries, but it is noteworthy that in both reports' discussions of the relative effects of various circumstances on different countries, creditworthiness is associated with faster growth, with the causation clearly going from growth. This suggests that the procedure at the aggregate level of assuming a credit constraint and deriving permitted growth may be a very uncertain method of proceeding, and, if it were put on a more formal basis than either organisation uses (both effectively build up checks on their aggregate forecasts from individual country or area specialists), it might produce extreme instability in the solutions.

The IDB medium-term scenarios are both based much more explicitly on government intervention in the economies, in particular to control imports and encourage exports than would be regarded as respectable by the IMF or World Bank. This explains the low import elasticities used and the assumption that Latin America can achieve a ratio of its export growth to income growth in the industrial countries of 1.5 (as in the 1970s). (It is also of course permissible for a forecast for one area to make assumptions about increases in share which would not be permissible for developing countries as a whole). The lower scenario assumes 'growth rates in government and private consumption that maintain consumption per capita at the levels which prevailed in 1983. In the high growth scenario the assumed growth rates in final consumption are those necessary to provide productive employment to a growing labor force.' (p 63). The fall in total output between 1981 and 1983 of 4% makes these both rather modest targets. Real imports fell about 40% in those years, so the assumed growth rates of 5.1% and

and 8.4% with output of 2.7% or 5.4% are intended to permit some recovery in the average propensity to import, but assume continued tight control. Given the initial trade surplus and the 4½% growth rate of exports, trade remains in surplus throughout the period. If interest rates fall, interest payments on the high scenario would be \$44 to \$60 billion a year, 27 to 29% of export revenues. On the low growth scenario, the ratio reaches 21% by the end of the decade. This was the level in 1980; in 1983 it was estimated as 38%.

#### Special features of the 1984 publications

One major change from the 1983 forecasts which is apparent from the preceding section is that both the World Bank and the IMF devote serious discussion to the possibility and consequences of worse outcomes than their base cases. They also both include discussions of the possible consequences of alternative domestic policies in the developing countries even if these still seem incomplete in comparison with their more familiar work on external relationships. The IMF sensitivity analyses in particular make the publications much more useful to an outside user, who wished to question some, but not all of the assumptions or relationships. The World Bank's decision to devote its major development and presentation to its present-policies scenario, rather than to its possible High case makes its forecast more immediately usable for the rather less professional and 'forecast-it-yourself' audience at which it is aimed. Both thus present a much clearer range of possible outcomes, with their assumptions and consequences than before, and both include among them more pessimistic scenarios than in previous documents, meeting a strongly expressed criticism of previous forecasts.

The other forecasters, notably OECD, have also gone much further in stating the uncertainties and risks underlying each part of their forecasts. As so few price forecasts are available, it must be regretted that UNCTAD no longer includes explicit forecasts for commodity prices. Several of the publications have special sections related to trade and protection this year, including the IMF (which summarises a fuller working paper), the IDB, UNCTAD, and NIESR. The IDB also reported particularly on debt; the UN, on economic cooperation; and the World Bank, on population.

## POLICY ISSUES

### The effects of the recession within the developing countries

The methods and types of question appropriate to short-term forecasting do not encourage forecasters to look at the more long-term effects of the type of recession and recovery they are observing and forecasting. Even the 'medium term' when it is confined to 5 to 10 years and forecast under substantially the same methods does not require these to be considered, but several of the forecasters do try to identify the long-term effects, both economic and non-economic, of the scenarios they present. The World Bank takes the most limited view among the organisations with particular interests in the developing countries. It merely notes that the recession 'increased unemployment, reduced investment and undermined social programs' in the same paragraph in which it finds that 'it provided many valuable lessons for economic policy' (p 1); it does later translate many of its output forecasts into per capita terms which show their consequences more clearly. The whole emphasis of its discussion of adjustment, however, is on the subordination of domestic consequences to external requirements: 'the service of debt is a matter of political will, and strength of will depends on the cost of exercising it' (p 43). UNCTAD on the other hand devotes a section to social conditions (pp60-63) in which it not only notes the direct effects on welfare (it suggests drops in spending tend to be more than proportional to output falls) including effects on employment, education and training, and health, but points out that these in turn will have direct economic effects: on productivity and on the future vulnerability and flexibility of the economy under shocks.

The IMF notes that the post-recession growth of productivity may be affected by the nature and duration of the recession (p 34), in particular it is possible that many gains from better labour use, which usually are observed after a recession, have already been made, while low investment may further limit medium-term growth. The UN considers similar questions, but suggests that they could help the recovery, by requiring investment relatively early in the recovery cycle, and therefore providing an additional stimulus. All of these productivity effects, which could apply to both the industrial and developing countries, not only must be carefully considered in taking a view on the most likely among the various sets of assumptions



and forecasts presented here and also in judging the desirability of the different scenarios. They suggest that the consequences of the slow growth choices may be more damaging (or less favourable) than may appear from the identifiable trade, price, and output effects shown in tables like table 3. They also suggest, and this is indirectly confirmed by the World Bank's emphasis on 'will', and the IMF's terminology of 'weak policies', that some of the economically possible scenarios may not be socially or politically possible, and even that certain combinations of particularly unfavourable industrial country performance and policy may leave no feasible path within the normal bounds of this type of forecast.

#### International financial issues

Several of the forecasters question the extent to which the United States can continue to draw on world saving to finance its own gap between saving and investment. UNCTAD suggest that it is not merely an unfortunate consequence of independent US policies which other countries must accept. US tax treatment of corporations and individuals has been changed to make the required high level of real interest rates tolerable for the US borrowers while attractive to foreign lenders. The further changes in the withholding tax treatment of holders of US bonds presumably came too late to be included, but would strengthen the argument that the policy of securing foreign financing must be regarded as deliberate, and therefore that it is a legitimate question for foreign and international agency concern and comment. The World Bank notes several times that its forecasts, particularly of real interest rates are affected by the level of the US deficit, and that the external environment for developing countries could be improved by changes in US policy. The IMF states the problem (pp95-96) of a growing demand for a constant supply of international saving, and calls the high interest rates 'a potential threat to smooth and sustained global economic growth'. Assessing the importance of the threat and the possibilities open to other countries, or groups of countries, to protect themselves against it depends in part on views of how interest rates and other forces interact in influencing investment and growth, and on what types of capital, exchange rate, and trade policies are legitimate tools. The belief that there is a need for international control of the effects on the supply of savings

in other countries and on the balance within them between investment and consumption is contributing to the spreading conviction that there are too many new types of international relationship and influence for the piecemeal reform of international institutions that has been going on since 1971 to be a sufficient answer.

The other financial issue is the one that lies behind all the short and medium term forecasts, but is only rarely brought to the surface: whether the debt crisis has reached a stable solution and whether the present structure of international obligations can be regarded as secure. All the forecasts, and all the alternative scenarios, assume this, although the possibility of major difficulties in particular cases is recognised and discussed. The IMF includes a useful section on the timing of amortisation payments, and points out that the large number of renegotiations in 1982-1983, many of which provided grace periods of 2-3 years, will produce a corresponding hump in amortisation starting in 1985 (pp 69-70). It assumes that this can in turn be refinanced, and probably more easily than in the first renegotiation because of the improved export prospects. It is however clear that it believes that strains on the international system and the banks could be reduced if some of this could be refinanced in advance. Other than this implication of the risks of putting strains on the international system and a suggestion that a return to a higher proportion of spontaneous rather than 'involuntary' lending (its term for UNCTAD's 'managed') would be good for general confidence, it does not discuss either whether an international system which has become dominated by 'involuntary' lending and IMF conditions is really a preservation of the pre-1982 market or whether even the new system can survive, especially under its more pessimistic scenarios. The World Bank suggests that some of the worst hit debtors would, under its low forecasts be 'in and out of financial difficulties for the rest of the 1980s and possibly beyond' and they 'might effectively impose their own schedule for debt repayment' (p 47; this seems one of the more imaginative euphemisms for default). It also includes a comparison of the recessions of the 1930s and the 1980s (pp20-21) which, although it concludes that the dangers of the present are less than those that led to the defaults of the 1930s, does show that it recognises the similarities, and it points out where the risks lie, in slow growth of exports, protection, high real interest

rates, and a reversal of the normal direction of flow of resources to the developing countries.

IDB notes that Latin America has achieved a trade surplus, which will grow under its forecasts (p 68), 'However, interest payments have made this the single most important component of the deficit on the current account.' 'If the debt continues growing under the terms it has in the recent past, the balance of payments deficit will tend to increase without there being a commensurate increase in the region's productive capacity. The above changes relative to the nature of the external deficit have, in turn, important policy implications given the limitations posed by the inelasticity of interest payments'. It does not draw policy conclusions.

#### The role of trade

The IMF and the World Bank both this year include scenarios that attempt to show what they believe could be achieved (or lost) by changes in domestic policies in the developing countries, within an unchanged external environment, and they and the other forecasters consider the relative positions of countries with different degrees of exposure to external events. The IMF notes that the major exporters of manufactures group was particularly badly affected by the recession because of such exposure, and UNCTAD cites India as an example of good performance partly because of the relative unimportance of external demand. In analysing present possibilities, however, as opposed to considering what countries could have done to have avoided finding themselves exposed, the scenarios show clearly, and the World Bank points out repeatedly in the text, the relative importance of external conditions and therefore of policy in the industrial countries: 'the onus on the industrial countries is greatest, because growth prospects throughout the world would be transformed if they overcame the rigidities and inflationary fears that slowed them down in the past ten years'. Although it is not disputable (in spite of the IMF's unfortunate weak policies scenario) that for any set of industrial country policies, it is better for the developing countries to follow 'good' policies than 'bad', given the difference of opinions even at the international organisation level over what good or acceptable policies are, for example, on trade policy, and the difficulty that the World Bank and IMF both found in formulating a clear statement of what they

meant by them at the very aggregate level required for these reports, it is sensible that the reports have this year shifted more towards emphasis on policies in the industrial countries and, in the case of the World Bank, also policies at the international level on such issues as protection in the industrial countries. This agreement on the importance of the 'international environment', however, means even greater emphasis on the questions raised of exactly how well the 'transmission mechanism' is now working.



## CHANGES IN TRADE RELATIONSHIPS

### Empirical evidence

The relationship between recovery in the industrial countries and in the developing could have been weakened either by characteristics of this recovery, or temporary factors affecting one or both groups, or by long-term changes that will continue to affect the links in the medium term. This section will summarise the evidence that there have indeed been changes, and the following ones will describe some of the explanations that have been offered for expecting changes. The evidence is not yet sufficient to reach firm conclusions on either point. This note is intended rather to focus on where the disagreements lie, and what type of evidence is relevant to the different points of view.

The obvious first point to make is that trade has grown more rapidly than output for the world and for all the major areas and individual countries for more than thirty years and is continuing to do so on all these forecasts, so that the potential size of any effect must have increased and be increasing. The effects, however, may be less easy to identify or to attribute definitely to trade than in the past because other international links have also increased sharply, particularly in the last ten years, through capital markets, floating exchange rates, and labour migration.

The IDB, UNCTAD, and the IMF all compare the recession or recovery of the mid-1970s with the current period. The IDB points out (p 127) that the volume of imports by the industrial countries fell much more in 1975 (8%) than in 1982; even if one takes a longer period than does the IDB, from 1980 to 1982, the fall this time is only about 4% (table 4). World trade also had twice the absolute fall: 4% in 1975, 2% in 1982. It is true that the period of slow growth plus recession was longer so these direct comparisons cannot be conclusive, but they suggest that it is not unreasonable to expect less from the recovery in the 1980s. The other organisations concentrate on comparing the recoveries.

This comparison is obviously impossible to make yet because the figures in table 4 are averages of forecasts which themselves embody opinions about how the recoveries may differ. Up to 1984, taking account

of the different timings of the beginnings of the recoveries within the calendar years, the recovery in trade seems slower than in the 1970s, as was the recession, and smaller, but if it were to go on, not stop now as forecast, it could catch up the full decline of the 1980-81 period. It could be argued that 7% in 1984 relative to the -2% in 1982 is not significantly different from 11% in 1976 relative to the -4% in 1975. Taking industrial countries' imports alone, the same argument holds, again up to the present. Only if the recovery, as expected by all forecasters, ends more quickly than did the recession, and therefore remains only partial will it be different from the past. The patterns for exports by the non-oil developing countries, on the other hand, are extremely different, with the fall coming much later relative to that in total world trade, but the recovery perhaps rather sooner.

The IMF notes that the recovery in current dollars of primary product prices is much smaller in 1982-85 than 1975-77, and that on its forecast the developing countries' terms of trade would still be 10% below those of 1976-78 (pp 143-144). Table 4 confirms this, but indicates the dangers of this type of comparison. The changes in terms of trade in the 1975-1977 and 1982-1985 periods in each case net to 0. The latter change still leaves the developing countries with the loss from the second oil price rise, but this seems better treated as a separate problem. What is clear from the table is that (as was pointed out in the section on forecasts) the recovery in the price of primary commodities relative to a manufactures is less strong, but on the other hand it is not expected, on these forecasts, to be lost over the next year as it was in 1978.

If the volume figures are combined with those for the terms of trade of the developing countries to show what UNCTAD calls their purchasing power of exports, this is rising much less rapidly than during 1976-7, but again it had fallen less and the rate of rise had declined only slowly before 1982. The same interim conclusion holds that on these forecasts for 1985-90 there is a lack of complete recovery from the recession to be explained, but that on figures up to 1984 it could equally be true that the recovery is merely as prolonged as the recession.

The IDB reports on studies on the income elasticities of industrial countries' demand for imports from Latin America and compares them with

Table 4: Comparison of Trade in the 1970s and 1980s  
Recessions and Recoveries (percentage change)

	volume			prices (dollars)				purchasing power (a)
	ic imports	world trade	non-oil dc exports	primary commodities excl.oil	manufactured exports	relative price of commodities	terms of trade of non-oil dcs	
1973	12	12.5	10	48	17.5	26	6.5	17
1974	0.5	5	1.5	33.5	22	9.5	-7	-5.5
1975	-8	-4	0.5	-11.5	12.5	-21.5	-9	-8.5
1976	14	11	14	10.5	0	10.5	2	16.5
1977	4.5	5	4	25.5	8	16	7	11.5
1978	5	5.5	10	-6.5	14.5	-18.5	-4.5	5
1979	8.5	7	8	15.5	14	1.5	1	9
1980	-1.5	1.5	9	15	11	3.5	-4.5	4
1981	-2	1	8	-15.5	-6	-10	-5	2.5
1982	-0.5	-2	1.5	-16	-1	-15	-3.5	-2
1983	4	2	5.5	6	-4	10.5	1.5	7
1984	9	7	7	6	0	6	2	9
1985	5	5.5	6	5	3	2	0	6
1985-90	4	5	5	5	5	0	0	5

Note: (a) change in export volume and terms of trade

Source: IMF, World Economic Outlook, various issues  
 UN, Monthly Bulletin of Statistics  
 ODI estimates using Tables 1-3, and noting change in \$ since spring 1984.

other estimates for overall elasticities (pp 134-137), but does not explicitly address the question of whether these have changed. It uses about 1.5 for all exports and 2 for non-fuel exports, which are within the traditional ranges. These are also roughly the elasticities that can be inferred from most of the forecasts for 1985 and the medium term although higher numbers are suggested for 1984 in recent forecasts. The IMF discusses its assumed elasticities for the developing countries for the medium term (p 160) and suggests that those estimated over the period 1963-81 are suitable. As was discussed earlier, these prove to be quite low, between 0.75 and 1.5 and there are problems in the choice of period. The World Bank alternative scenarios suggest that it is also using rather low numbers for developing countries.

Two types of change in industrial countries' elasticities could be of interest in the context of this paper: changes in their demand for all goods and in their demand for the exports of the developing countries. Little has been published on these questions sufficiently recently to be relevant to these forecasts, although some members of the trade panel may be able to report on such work. The problems of taking into account the severe recession, the changes in composition of trade (especially the fall in the share of oil) and relative price and exchange rate changes are very serious, and the period in which changes for the types of structural and institutional reasons discussed in the next sections would be evident is very short to reach significant conclusions. What does emerge from the work that is available and from work in previous periods examining this type of question is the importance of first separating out compositional changes when looking at broad aggregates such as 'trade', 'output', industrial countries, and developing countries. These are usable only when it can be assumed that major structural changes are not taking place. In view of the types of explanation and change which are examined below, the minimum distinctions would be among the industrial countries: the US, Europe and Japan; and among products: oil, manufactures, and other primary products.

The EEC has published a report by Rollet<sup>1</sup> which tries to discern

---

1. Ph. Rollet. 'The external constraint and the operation of the price and income elasticities of external trade in the Community countries, the United States of America and Japan', European Economy, 16, July 1983.

whether there was a break in 1973. He found for EC trade with the rest of the world that although the overall elasticity had fallen slightly, for products other than oil it had risen (comparing 1964-73 with 1973-81): for manufactures it rose from 1.7 to 2.7. For the United States there was no change for manufactures (2.5) with the only category with a significant change being 'basic consumer items'. For Japan, there were very small declines for categories other than fuels. Manufactures changed from 1.2 to 0.9. If only the overall elasticities were examined, they would show sharp falls for the US (2.6 to 1.1) and Japan (1.3 to 0.5) and virtually no change for the EC (1.5 to 1.4). These data thus indicate the differences among areas and commodities, but give little evidence of any general shift, except for oil. They are, however, estimated over too long a 'recent' period to take account of some of the types of changes, particularly the changes in protection after the 1975 recession, that are suggested as influences on trade performance.

UNCTAD (pp 85-86, p 33) compares the growth of imports into the United States during the present recovery with that in 1976. It finds that the 'decline in net exports . . . was more than double that observed in the 1975 recovery'. It suggests that this was for reasons tied to present circumstances, such as the high value of the dollar rather than the more permanent structural ones.

These studies do not offer very much evidence for any permanent change in import-output relationships in the industrial countries, but because they do not actually look at the most recent period, abstracting from special circumstances surrounding the recession and recovery, they cannot answer the arguments about present 'normal' behaviour of imports which are relevant to making the medium term forecasts. And it is precisely identifying indications that relationships will change before they do that must be the justification of attempting to make such forecasts.

#### The characteristics of the 1983-85 recovery

There are three major differences between the distribution of the current recovery and that of 1976-7. Among the industrial countries, the United States recovery in 1983-4 has been at least as strong, while the European countries have not even grown at their recent trend rates, and even Japan's growth has been comparatively modest. In 1976 all major industrial countries except the UK grew more than 5%. The non-oil



developing countries continued to grow at around 5%, with little sign of a cycle through the mid-1970s. Finally, although they had slowed from 1974-75 rates, imports by the oil exporting countries were still rising at 15-20% a year.

The sharply contrasting performances of different markets in the present recovery make it difficult to judge from aggregate data whether either imports or market shares of exporters, in particular of the developing countries, have been behaving normally. The individual country and area elasticities of imports against output for the industrial countries that are implied in the forecasts for 1984 are not out of line with previous recoveries; they are slightly more than 2 for Japan and Europe and 3 or more for the United States. The last is rather below that for the US in 1976, but the rise did begin in 1983 so that the overall rise may not be much lower.

UNCTAD (pp 31-40) examines in some detail the impact of the US growth in 1983 on developing countries, especially on their exports of manufactures. Although it is a less important market than Europe in total and for the major categories of primary products, and less important than Japan for primary products other than food, it is the major market for their manufactures, taking 28%. In 1982-83, developing country exports of manufactures achieved increases in their share of total US consumption in almost all categories of manufactures, but only significantly increased their share of total imports in those categories in which the share was still relatively small. The fastest rises were where it was under 1% with some strong rises where it was between 1 and 2%. In textiles and clothing, however, where it was about 6%, the rise was only marginally greater than the increase in total imports (19% compared to 17%). Nevertheless, the aggregate increase in the value of US imports of manufactures from developing countries at 24% was greatly superior to its rate of total increase in manufactures, 13%. The OECD table (p 134) which attempts to allow for the US preponderance in computing growth of market shares has already been mentioned; it shows that the market growth for the developing countries exports of manufactures was 0 in 1982, 10% in 1983 and it is forecast at 14½% for this year. It believes that their actual exports of manufactures have grown less than this and although, as was noted above, there are apparently statistical problems, it certainly suggests that there could not have been any large gains.

As the United States returns (on these forecasts) to growth rates nearer to other industrial countries, these compositional gains in share will become less important. The UNCTAD report also notes that the developing countries themselves (here including oil exporters) are a more important market for developing country exports of manufactures than is the US (at 37%). This suggests that any constraints on their own growth of imports will affect markets for their manufactures particularly severely, another reason for expecting the present aggregate ratio of developing country export growth to world trade in manufactures to fall for compositional reasons.

The IDB gives a similar table for Latin American exports (p 122). This shows that the share of Latin American exports of manufactures going to the US is much lower than for all developing countries (at 21%) and it has fallen sharply since 1960; its share to developing countries is 45% and within that to Latin American countries, 37%. It thus is more seriously affected than the average by the slow growth in other developing countries by its higher share and concentration in the slowest growing group within them, and it has received less direct benefit from the rapid growth in the US (although it may have increased its share of that market). Other things being equal, therefore, it 'should' show a worse market share performance at the aggregate level than other developing countries.

For primary commodities, the pattern of the present recovery has had very different implications. These go mainly to Europe (from all developing countries and from Latin America), where output and import growth have been worst. For these, it is prices rather than volume that normally responds most strongly to changes in demand. As Europe does not, according to these forecasts, actually have a recovery this time, this may help to explain the rather sluggish performance of their prices relative to total output growth. This pattern may also justify the fact that reports do not forecast the normal fall back of commodity prices after a recovery, in 1985 or later.

The removal of the stimulus to world trade from the rapid growth of OPEC imports that was present from 1974 to 1982 will obviously mean a lowering in net stimulus to exports from both industrial and developing countries. The effect is likely to be felt particularly by the Asian developing countries.

### Long-term changes in industrial structure

The only report that (briefly) raises this type of point is the World Bank (p 39) and this is in connection with changes in output and productivity, not trade-output relationships. The type of arguments that will be listed in this section lie outside the normal fields of trade analysts or forecasters, but are clearly crucial for taking a view on the possibilities of major changes in trade-output relationships in the medium term. They would, however, require conferences of their own to examine properly.

The industrial countries and the developing countries are growing more slowly than they have done during substantial periods in the past, and on these medium-term forecasts (even the World Bank's High) they will continue to do so, and to operate at high levels of unemployment of labour and, in most cases, capital (table 5). This could reduce two of the traditional roles of trade, as a means of providing a flexible addition to supply when demand rises rapidly, most notably in recoveries from recessions, and as a means of meeting a more permanent excess of demand over potential supply in a country operating at a high level of capacity utilisation. These arguments would suggest that imports should have fallen more than proportionately to output and, as long as it is below some capacity or full employment level, imports might grow more slowly than in an economy growing at normal rate and at full capacity utilisation. Without any attempt to quantify any of these terms, this type of argument would suggest lower than normal elasticities in both industrial and developing countries at present (except possibly in the US and Japan) and in the future as forecast here. It is also arguable that slow growth could be associated with a lower average level of imports at any income level if it is easier for investors to keep in step with changes in demand, and therefore the average length of the periods in which new investment is made to meet new demands temporarily met by imports is reduced. This could mean that falls in imports during periods of recession would not be fully made up in a slow recovery.

Shifts in the composition of demand could affect either traded goods in general or particular goods which are likely to be traded. An example of the first would be a change in the share of government purchases in total consumption as it is normal for official purchasers



Table 5: Indicators of possible structural change (percentages)

	1970	1973	1975	1976	1979	1982	1983
<hr/>							
<u>Unemployment rates</u> <sup>(a)</sup>							
OECD	3.1	3.3	5.2	5.3	5.1	8.2	
US	4.8	4.8	8.3	7.6	5.8	9.5	9.5
Japan	1.1	1.3	1.9	2.0	2.1	2.4	2.6
EEC	2.7	3.0	4.5	5.2	5.6	9.1	10.1
<u>Government consumption</u> <sup>(b)</sup>							
OECD	16.4	15.7	17.3	17.0	16.5	17.7	
US	19.2	17.8	19.1	18.7	17.6	19.0	
Japan	7.4	8.3	10.1	9.9	9.8	10.2	
EEC	15.2	16.2	18.2	17.9	18.0	19.4	
<u>Machinery and equipment</u> <sup>(b)</sup>							
OECD	8.9	9.1	8.4	8.4	9.0	8.1	
US	7.3	7.7	7.4	7.4	8.8	7.4	
Japan	15.4	13.7	11.0	10.4	10.8	10.2	
EEC	9.3	8.9	8.3	8.4	8.7	8.0	

Notes: (a) standardised by OECD  
(b) as percentage of GDP

Source: OECD, Historical Statistics  
Economic Outlook

to operate formal or de facto preference against imports, or merely to be less likely to look for new suppliers, which might be importers. In both Japan and Europe the share of government consumption has risen since 1970, with little change in the US. This type of change can be closely associated with an increase in the share of services in total demand. This is less easy to document and the likely direction of its impact on total imports would be less easy to deduce, but it would seem likely at the least to reduce relative growth of imports of goods. Investment, particularly in machinery and equipment, which can be imported, has tended to decline, again with the exception of the US.

The successive increases in the price of oil obviously raised the relative price of all imports, to all countries, and thus could explain a decline in the average ratio of imports to output, but this is better treated as a reason for appropriate disaggregation. If, however, total figures are being used the fact that the lags in response of energy demand to price change are particularly long would suggest that there may still be some depressing effect on simple import-output ratios, even if no further relative price changes are being forecast.

The possibility of a long-term shift away from natural commodities to synthetics or to processes using smaller quantities, or merely of a less than proportional increase in demand for primary products would not necessarily suggest any change in elasticities. If such effects are related to changes in industrial structure or if exports grow at some low trend rate then it is possible that slow growth rates could lead to higher apparent elasticities.

One reason that has been suggested for the rapid growth of trade relative to output in the 1960s was the increased possibility of international specialisation, and therefore the potential for intra-industry trade. This could be attributed to greater standardisation of production or of tastes: to the growth in the gap between wages in the industrial and in the developing countries, and among industrial countries; to lowering of transport costs and improvements in its speed and reliability; to the importance of industries with important economies of scale.<sup>1</sup> There is considerable discussion now of whether

---

1. Martin Wolf. 'Fortress Europe' and 'Collective self-reliance', lecture, Deutsches Übersee-Institut, Hamburg, 1983

these changes are continuing, at the same or different rates, or even being reversed, especially in the case of the last two. It is also unclear what effect the types of technological change that are believed to be characteristic of the next decade will have.

#### Protection and other institutional changes

The most important institutional change is the growth of protection, particularly of non-tariff barriers against manufactured exports from the developing countries. The UN (pp 38-9) suggests that this increased in 1983 and early 1984, and cites examples by industrial countries against developing and among industrial countries. The IMF's Annual Report on Exchange Arrangements and Exchange Restrictions also found that protection continued to increase during this period in spite of the beginning of recovery in the industrial countries, although it suggests that the rise in 1983 was less than in 1982, and explicitly attributes the low growth of trade relative to output in 1983 to protection. The OECD's introductory assessment refers to 'a panoply of discretionary measures to affect trade flows' (p 12) and believes that they have become 'more widely used and more firmly established in recent years' and cover 'whole sectors of Member country economies'. The NIESR also notes recent increases. UNCTAD summarises the recent growth of non-tariff barriers in its forecast section (p 8) as well as having a more extensive discussion in its special report on the trade and payments system. Both it and the IDB attribute part of the poor performance of developing countries' exports in recent years to protectionism. As was discussed in the section of the forecasts, both the IMF and the World Bank consider it sufficiently important to include among the variants of their medium term scenarios, and to devote special sections of their reports to it, and the World Bank puts it first among issues requiring international action (p 48).

The IMF and the World Bank analyses of its effects, however, and the other forecasts, which assume either a flat level or constant rate of increase of protection, do not actually try to measure the impact of existing measures or to specify what measures would be necessary to produce the arbitrary changes in developing country exports which they impose in their scenarios. They merely show the results of a given percentage change in exports, without indicating how much of what type of protection would achieve it, or alternatively how much higher

exports would now be in the absence of the new barriers to trade. The scenarios do not, therefore, measure the effect of protection. The reasons for this gap are partly the same as for the failure to measure changes in trade output relationships in general: the difficulty of knowing what is 'normal' with sufficient certainty to identify deviations from it, and apportion such deviations among the various possible explanations, and partly the difficulty of measuring the quantity of protection sufficiently satisfactorily to be able to compare it to the size of such deviations from the trend if they could be found.

Resort to non-tariff barriers by the industrial countries has been of increasing importance since 1974, although there were examples in agriculture, textiles and steel well before then. These sectors, joined later by cars, standardised consumer electronics, shipbuilding and footwear, remain the most important subjects for protection, although examples can be found in a wide range of other products. The types of product thus give a bias against developing country exporters; many of the protecting countries have agreements with other industrial countries that automatically restrict their application to them (notably members of the EC and EFTA among themselves); many measures have been explicitly taken against some or all developing countries.

The most extensive protection is probably found in food products.<sup>1</sup> The IMF uses the share of trade in total production to indicate the extent of protection in this sector, and also summarises many of the policies that restrict trade. Although there have been some increases recently, notably in US and Canadian meat import controls and in various controls by both the EC and US against fruit and vegetables from developing countries, this sector was so extensively controlled even before the 1970s recession that it is unlikely that further increases in the controls can have significantly reduced the already low elasticities. It has also been controlled for so long that it would be difficult to find a period in any way comparable to the present in which it was not controlled that would permit measurement of what trade would be in the absence of control, and therefore measure the potential increase

---

1. S.J. Anjaria, Z. Iqbal, N. Kirmani. I.L. Perez. Developments in International Trade Policy, IMF Occasional Paper 16, 1982. Summarised in IMF, 1984; Commonwealth Secretariat, Protectionism: Threat to International Order, London 1982.

in levels and elasticities if protection were removed. Although the IMF report on restrictions notes possibilities of reform in the CAP, it seems unlikely that any major changes there or in other industrial or developing country policies would require a major reassessment of trade elasticities during the term of these forecasts.

It is in manufactured goods that the principal changes have taken place and that further changes are feared. Various attempts have been made to monitor them and measure their extent. Among official agencies, GATT, UNCTAD and the office of the US Special Trade Representative are now attempting to keep inventories. Similar files have been kept by various researchers and by individual countries for their own measures (perhaps surprisingly this last is not automatic or universal). The efforts are all handicapped by the lack of any clear definition of what is a control, and by the absence in most cases of any obligation on the controlling government or those affected to report the actions to anyone. The actions that may be included include anything from officially announced quotas such as those under the Multi-Fibre Arrangement, through 'voluntary export restraints', which may be arranged between governments, between the industries involved, or various mixtures of the two: administrative measures which effectively discriminate against imports directly (government purchasing) or indirectly (technical or other standards) to a variety of measures on the border between tariff and non-tariff measures, with the whole range of anti-dumping actions becoming increasingly popular.

The most comprehensive recent survey of the measures that have been taken is the IMF Working Paper cited above. Although it includes some measures of the total incidence of barriers by importing country (pp 114-119; p 123), these are classified also by type of measure and as some imports are subject to more than one type of measure, these do not give an overall measure. It was the first source to list the measures against particular countries (because of the difficulties of compiling the data almost all work has been from the import side), listing measures against exports by India, Malaysia, the Philippines, Pakistan, South Korea and New Zealand; although these appear to be incomplete they are the best available guide to the types of measure faced by developing countries and the sectors in which they are most important.



UNCTAD has used its inventory of restrictions to measure literally the number of import categories covered by controls, by importing country, but because of the wide variation in the quantities that can fall into a category, this does not seem a helpful approach. The World Bank (p 18) has used the UNCTAD data to find the share of imports by value controlled by industrial countries, classifying them into imports from developed and developing countries. GATT has set up a Group on Quantitative Restrictions and Other Non-Tariff Measures which is to report later this year, and is improving the inventory. It has published estimates from time to time of the amount of trade covered by restrictions, most recently that 30% to 40% of exports from developing countries are subject to constraints by the industrial countries. For these estimates, it has identified the commodities most commonly controlled, and calculated their shares in the exports of individual countries.

Table 6 shows the World Bank results and also an early attempt to use data on individual restrictions by country to measure the share of imports that were controlled before and after the major increase in controls in the second half of the 1970s as a first step in measuring the possible effect on changes in trade elasticities. Table 7 is an attempt to use the data collected for table 6 reweighted by the shares of imports of the controlled goods by the controlling countries in the exports of some developing countries. The countries shown account for about two thirds of all exports by non-oil developing countries and about 85% of their manufactured exports. Although the data needed on the composition of exports by country and commodity simultaneously were frequently completely lacking or seriously over-aggregated for the purpose, the results are encouragingly close to an earlier experiment in using the data in the same way as the GATT method, ie. identifying major categories; although they are higher than the GATT results (between 40% and 50% instead of 30-40%) it appears that the GATT data, which were intended to cover major debtors, included some oil producers: this sharply lowered the average for the group as neither table 7 nor GATT includes oil as a managed good.<sup>1</sup>

---

1. Table 6 and the last column of table 7 do on the grounds that it is difficult to treat a commodity as highly cartelised and regulated as oil, as freely traded.



Table 6: Extent of managed trade (percentages)

	<u>Share of imports controlled<sup>(a)</sup></u>				<u>World Bank/UNCTAD</u>	
	<u>(1974 weights)</u>				<u>(1980 weights)</u>	
	<u>1974 restrictions</u>		<u>1980 restrictions</u>		<u>from</u>	<u>from</u>
	<u>Total<sup>(b)</sup></u>	<u>manu- factures</u>	<u>Total<sup>(b)</sup></u>	<u>manu- factures</u>	<u>developed countries</u>	<u>developing countries</u>
US	36	6	46	21	13	6
Japan	56	0	59	4	19	5
EEC	36	0	48	16	15	12
OECD	36	4	44	17		
Oil exporters	54	46	65	60		
Non-oil developing	50	25	47	23		
World	40	13	48	24		

Notes: (a) for definition see source

(b) including oil

Source: S.A.B. Page, 'Protectionism and its Consequences for Europe',  
Journal of Common Market Studies, XX,1, September 1981.

Table 7: Impact of managed trade on developing countries (percentages)

	<u>Share of manufactures in total exports</u>	<u>1974 restrictions</u>		<u>1980 restrictions</u>		<u>1980 including fuels total</u>
		<u>Total</u>	<u>manu- factures</u>	<u>Total</u>	<u>manu- factures</u>	
Hong Kong	92	22	17	32	28	32
South Korea	90	30	22	47	37	47
Taiwan	79	31	29	58	63	58
Singapore	50	27	31	29	37	57
Brazil	40	63	44	71	66	76
India	58	47	37	68	74	68
Malaysia	30	34	19	35	23	63
Mexico	18	11	17	13	19	80
Thailand	35	71	20	74	29	74
Argentina	22	74	47	85	97	88
Peru	43	17	25	19	29	40
Colombia	20	77	51	78	54	86
Egypt	12	12	82	13	89	77
<u>Total</u>	55	36	27	46	44	62

Source: see text

The exact numbers should clearly not be taken too seriously, and all the qualifications are given at length in the original publication. But table 6 provides some evidence of the order of magnitude of the increase in controls, particularly in manufactures, from an insignificant proportion of industrial country imports to a level at which they clearly could affect elasticities. (The relative shares of different countries do not necessarily indicate relative protectiveness as there is no distinction within categories by 'tightness' of control, for example the actual size of a quota the marked discrepancy between the EC and the US on the World Bank figures, however, seems surprising). From the developing countries' point of view, table 7 also shows a sharp increase in the proportion of exports which are controlled.<sup>1</sup>

The effect to be expected on the elasticity of demand for developing countries' exports of manufactures depends on what can be assumed about the elasticities of the controlled and uncontrolled exports: as indicated above this is unknown. If one takes the simplest view, that no increase is allowed in controlled exports and that the elasticity for the remaining uncontrolled exports is the same as for uncontrolled exports before 1974 (highly unlikely because the composition is certainly different, and controls may have been imposed precisely on those with a high elasticity), the ratio of export growth to demand growth in the developed countries will be reduced by 0.17 (0.44-0.27) times the elasticity for every percentage point growth in output. If controlled exports are permitted a constant market share, the reduction would be .17 times the elasticity minus 1. For elasticities around 2 or 3, these give a range of possible effects from .2 to .5 on the ratio: significant especially over a medium-term period, but difficult to observe when even the data on total growth in manufactured exports are inadequate. It may be more useful to note that, for these developing countries, which were chosen because they were major exporters of manufactures: 55% of their exports are manufactures of which about 55% are not (apparently) controlled. so that about 30% of their exports could be responsive to growth in demand.

---

1. The weights applied to the restrictions are the same, so any increase in the share of trade going to other developing countries, which, as indicated in table 6, were and remain more restrictive, would make this increase larger.

For all developing countries, with only just over 40% of their exports manufactures, the corresponding figure is about a quarter. Although obviously growth in the developed countries has some effect on primary goods, including fuels, and on the managed exports, the main impact of any recovery has to be transmitted through these small proportions of exports.

There have been various attempts to use changes in import penetration by the developing countries in developed country markets as an indication of the effect of protection. The basic difficulty is the same, of knowing what the normal increase in penetration, in the absence of protective measures, would be. These studies usually show that import penetration is increasing or at least not diminishing (eg. World Bank p 43) although the most recent data on market shares in 1982-83 discussed above do not. But this is not sufficient evidence that the new protection is not having an effect as it is most often imposed where penetration is increasing; it would be plausible to assume a model in which import penetration increases in one product, which is then controlled, and penetration is then increased in another. Unless the disaggregation is very fine, this would appear in the data as a simultaneous increase in import penetration and protection. In principle, comparisons could be made between penetration in non-protecting and protecting countries, but even if the former existed, there would be other differences in demand or market structure. It seems difficult to justify as strong a statement as the IMF's about 1983, that protection accounts for the low growth of trade, but on the other hand it seems unlikely that measures affecting almost half of developing countries' exports, which at least those pressure groups who secured their imposition believe are effective, have no influence on the growth of trade.

Trade that takes place within firms, like that subject to protection, may respond differently from 'normal' trade to growth in trading partners. This would be important, if the share has changed recently, or is likely to do so, and if the elasticities are significantly different from those in trade between unrelated companies. There is considerable evidence that the share of such trade, in total and in manufactured exports from developing countries to industrial countries is important,

with estimates tending to fall in the range of 20 to 30%<sup>1</sup>, but most data for developing countries are gathered only for occasional years by individual researchers, usually with different methods or definitions, and the principal source for the United States has recently been discontinued. The evidence appears to be that, although there are differences in the short-term variability between intra-multinational and arms-length trade and possibly in the price elasticities, there is no difference in income elasticities.

It is impossible not to mention the growth of interest in 'counter trade' which appears to be becoming the recognised term for all forms of barter, compensated trade, forward commitments to take any type of good in exchange for services or investments, etc. It is too recent a phenomenon (except in particular markets, for example within the oil or chemical industries or between the centrally planned economies and the rest of the world) to have been measured, and it is very difficult to obtain evidence about it and particularly to confirm the estimates of its share. For the purposes of the analysis here, it is worth noting apparent reasons for its apparent growth, to indicate its potential impact. One explanation is the shortage of export credits, either between particular types of trading partner, such as in trade among developing countries, or for particularly risky debtors. As such shortages or market imperfections are not normally allowed for in the forecasts, it may permit countries to avoid a decline in trade that would otherwise adversely affect a forecast. It would also reduce the impact of high interest rates on the cost of working capital and therefore on trade. If these have had an effect in the recent past, this could increase trade ratio in the future, but again the effect is more likely to be avoidance of an unforecast fall. If it actually produces the effect which some developing countries have as a target, increasing exports effectively through introducing a better marketing procedure than whatever was available before, and if this is not merely a diversion of exports from one developing country to another, through either better marketing or an effective devaluation, then the effect would be as in the World Bank's improved policies

---

1. The UN Centre for Transnational Corporations is the most important source for recent data on this topic. See also David J. Goldsbrough 'International trade of multinational corporations', IMF Staff Papers 28,3, September 1981,

scenario (although it is unlikely that the Bank would consider it an improved policy). Both exports and imports from the developing countries increase through supply rather than demand factors, effectively altering the import elasticities but not the balances of the industrial countries and the developing. This could then be a stimulus to increased trade, possibly attributable to increased exchange of information about the available products and about the requirements of industrial country markets because of brokerage services from the company required to organise the countertrading. It would thus be comparable to transportation improvements in the 1960s. Until there are examples of this, the credit replacement function seems the most important, and it is probably not necessary to allow for any effect on the forecasts.

It is perhaps wrong still to treat the possible impact of floating exchange rates on the volume of trade as sufficiently new not to be already incorporated in any reasonable up-to-date elasticity measurements, but it may be useful to recommend two recent studies of the question.<sup>1</sup> The IMF paper finds 'no evidence that exchange rate volatility plays a major - or even significant - role in reducing trade volume'. The Akhtar and Hilton study concluded that their estimates 'lend considerable support to the hypothesis that exchange rate uncertainty tends to reduce the volume of international trade'. Both stress the uncertainties in the results and in choosing the specifications of the relationships to be tested.

### Conclusions

With the possible (even probable) exception of protection the evidence for any strong effect on trade from the influences examined in this section is not strong. The potential effects of some of the changes, notably in structural pressure of demand and protection, are sufficiently serious to require further study, in the context of particular industries, countries, and trade flows. It can be noted that almost every

---

1. IMF, Exchange Rate Volatility and World Trade, Occasional Paper 28, 1984. M. A. Akhtar, R. Spence Hilton, Exchange Rate Uncertainty and International Trade: Some Conceptual Issues and New Estimates for Germany and the United States, Federal Reserve Bank of New York, Research Paper, 1984. The latter includes a summary of previous research results (pp 70-71),

influence suggested, if it has any effect, would tend to reduce the ratio of trade to output, especially in the industrial countries and for their imports from developing countries more than the total.

The evidence that such a reduction has occurred, permanently or in the current cycle of recession and recovery, is also not strong, but there is certainly no indication of an increase in elasticities.

What this discussion does suggest is therefore that the uncertainties are almost entirely in a downward direction; the forecasts and their alternative scenarios must be assessed and used with this in mind.



## APPENDIX: FORECASTS DISCUSSED AND DEFINITIONS

### Forecasts

Economist Intelligence Unit, World Outlook.

General Agreement on Tariffs and Trade, International Trade.  
For 1984, press release, 18 May 1984

Inter-American Development Bank, External Debt and Economic Development in Latin America.

International Monetary Fund, World Economic Outlook.

National Institute of Economic and Social Research, National Institute Economic Review (August 1984).

Organisation for Economic Cooperation and Development, OECD Economic Outlook (July issues).

UN, World Economic Survey.

UNCTAD, Trade and Development Report.

World Bank, World Development Report.

### Definitions

For full definitions see individual reports.

Developed countries: differences among forecasters not significant in relation to developing country.

Oil price: average OPEC official export price; 'real' deflated by price of manufactured exports.

Price of manufactured exports: UN index for developed countries.

Price of primary exports: UNCTAD index market prices of developing country exports.

Major oil exporters: Algeria, Indonesia, Iran, Iraq, Kuwait, Libya, Nigeria, Oman, Qatar, Saudi Arabia, United Arab Emirates, Venezuela.

Non-oil developing countries (and area sub-totals): as defined by IMF but excluding South Africa, with minor differences for some reports:

Secondary oil exporters: Angola, Bahrain, Bolivia, Brunei, Congo, Ecuador, Egypt, Gabon, Malaysia, Mexico, Peru, Syria, Trinidad and Tobago and Tunisia.

Exporters of manufactures: Argentina, Brazil, Hong Kong, South Korea, Singapore, Taiwan.

Least developed countries: all others.





