5 The Major Seven

This chapter discusses the evidence of the policy mix in the seven largest OECD economies, the United States, Japan, Germany, France, Britain, Italy and Canada, and of its relationship to their relative macroeconomic success during the period from the later 1960s to the early 1980s.

The approach of the two preceding chapters, involving the aggregation of data from a number of countries, may suffer from the limitation that conclusions drawn from this aggregate data might have been a chance result of the aggregation: for the countries with less macroeconomic success within a particular group might not be the same as those that had a macroeconomic policy setting that could have been expected to produce the relative lack of macroeconomic success.

On the other hand, the case of every individual country is obviously likely to be greatly influenced by considerations quite distinct from the policy mix; indeed, the tendency for every country to believe that its own circumstances are distinctive (or even unique) has probably done much to cause inadequate attention to be paid to those deficiencies in the macroeconomic mix which have been of significance in virtually all of them – but which tend to be dominated by other factors when the experience of any individual country is being considered.

INFLATION AND UNEMPLOYMENT IN THE MAJOR SEVEN

The policies of the countries for much of the period from the late 1960s to the early 1980s was apparently based on the implicit assumption that high unemployment helped to restrain inflation and that there was no available means to achieve the same effect that did not involve the creation or continuation of the high unemployment. But if this assumption were valid one would expect there to be some
association between high or rising levels of unemployment and low rates of inflation. This section considers whether there is any clear tendency for those major OECD countries that permitted high levels of unemployment also to have relatively low rates of inflation.

There is obviously no such relationship between inflation and unemployment for Japan and Germany, the two countries that were most successful in maintaining a relatively high degree of macroeconomic achievement during the 1970s. For, as Table 5.1 shows, these two countries had by far the lowest average rate of unemployment over the whole period, whereas Germany also had the lowest average rate of inflation; and Japan’s rate of inflation was below the OECD average for the period since 1973 (though well above it up to the early 1970s). Moreover, for the second half of the 1970s (taken alone), during which Japan and Germany had clearly the lowest average unemployment rates of the seven, they had also a lower inflation rate than the other major OECD countries. So far from being consistent with the hypothesis that high rates of unemployment help to keep down the rate of inflation, this evidence would suggest the exact contrary.

At the other extreme, the two highest rates of inflation for the period 1971–82 were shown by Italy and Britain. Over the whole period these two countries had also the two highest registered unemployment rates among the European major countries. Again, this evidence would be consistent with the view that high rates of unemployment and high rates of inflation tend to go together – rather than providing any justification for the reverse proposition (which would be necessary to provide a basis for the view that inflation can be checked only by permitting high unemployment).

On the other hand, it might perhaps be said of the three remaining countries, the United States, France and Canada, that relatively high unemployment rates and relatively low inflation rates tended to some extent to go together (within the group in question). For, of these three, France had both the highest rate of inflation and the lowest level of registered unemployed, whilst the United States and Canada had approximately the same rate of both inflation and registered unemployed as one another – though the US had a slightly lower rate of both inflation and unemployment. Again, this would be highly questionable evidence on which to base policies of tolerating high unemployment in the hope of thereby restraining inflation; and, taking the evidence from the experience of these countries, it might with more justice be invoked to support the opposite view that low unemployment may tend to keep inflation down.