

NATIONAL ECONOMIC AND SOCIAL COUNCIL

Report on the economy in 1973 and the prospects for 1974.

REPORT No. 1

NATIONAL ECONOMIC AND SOCIAL COUNCIL

CONSTITUTION AND TERMS OF REFERENCE

1. The main task of the National Economic and Social Council shall be to provide a forum for discussion of the principles relating to the efficient development of the national economy and the achievement of social justice, and to advise the Government, through the Minister for Finance on their application. The Council shall have regard, *inter alia*, to:

- (i) the realisation of the highest possible levels of employment at adequate reward,
- (ii) the attainment of the highest sustainable rate of economic growth,
- (iii) the fair and equitable distribution of the income and wealth of the nation,
- (iv) reasonable price stability and long-term equilibrium in the balance of payments,
- (v) the balanced development of all regions in the country, and
- (vi) the social implications of economic growth, including the need to protect the environment.

2. The Council may consider such matters either on its own initiative or at the request of the Government.

3. Members of the Government shall be entitled to attend the Council's meetings. The Council may at any time present its views to the Government, on matters within its terms of reference. Any reports which the Council may produce shall be submitted to the Government and, together with any comments which the Government may then make thereon, shall be laid before each House of the Oireachtas and published.

4. The membership of the Council shall comprise a Chairman appointed by the Government in consultation with the interests represented on the Council
Ten persons nominated by agricultural organisations,
Ten persons nominated by the Confederation of Irish Industry and the Irish Employers' Confederation,
Ten persons nominated by the Irish Congress of Trade Unions,
Ten other persons appointed by the Government, and
Six persons representing Government Departments, comprising one representative each from the Departments of Finance, Agriculture and Fisheries, Industry and Commerce, Labour and Local Government and one person representing the Departments of Health and Social Welfare.

Any other Government Department shall have the right of audience at Council meetings if warranted by the Council's agenda, subject to the right of the Chairman to regulate the numbers attending.

5. The term of office of members shall be for three years renewable. Casual vacancies shall be filled by the Government or by the nominating body as appropriate. Members filling casual vacancies may hold office until the expiry of the other members' current term of office and their membership shall then be renewable on the same basis as that of other members.

6. The Council shall have its own Secretariat, subject to the approval of the Minister for Finance in regard to numbers, remuneration and conditions of service.

7. The Council shall regulate its own procedure.

NATIONAL ECONOMIC AND SOCIAL COUNCIL

Report on the economy in 1973 and the prospects for 1974.

DUBLIN:
PUBLISHED BY THE STATIONERY OFFICE

To be purchased from
GOVERNMENT PUBLICATIONS SALE OFFICE, G.P.O. ARCADE, DUBLIN 1,
or through any Bookseller.

Price: 7½ p.

(Prl. 3775)

NATIONAL ECONOMIC AND SOCIAL COUNCIL
MEMBERS

Chairman: Prof. W. J. L. Ryan

Nominated by the Government:

Mrs. H. Burke	Mr. A. N. O'Brien	Mr. M. B. Lawless
Prof. N. J. Gibson	Mr. P. Rock	Mr. C. H. Murray
Prof. D. Hannan	Mr. J. Walsh	Mr. T. O' Cearbhaill
Dr. K. Kennedy	Dr. T. K. Whitaker	Mr. P. O'Slatarra
Prof. P. Lynch	Mr. M. J. Barry	
Mr. C. Mac Gabhann	Dr. B. Hensey	

Nominated by the Confederation of Irish Industry:

Mr. F. A. Casey	Mr. P. J. Keehan	Mr. J. H. D. Ryan
Mr. L. Connellan	Mr. R. I. Morrison	

Nominated by the Irish Agricultural Organisation Society:

Mr. J. Buttimer	Mr. P. Kelly	Mr. P. Raftery
-----------------	--------------	----------------

Nominated by the Irish Congress of Trade Unions:

Mr. A. Barr	Mr. B. G. Harkin	Mr. D. Nevin
Mr. J. Carroll	Mr. D. Larkin	Mr. R. Roberts
Mr. J. Fitzpatrick	Mr. D. Murphy	
Senator F. Kennedy	Mr. P. Murphy	

Nominated by the Irish Creamery Milk Suppliers' Association:

Mr. P. Hourigan	Mr. D. Murphy	Mr. T. J. O'Callaghan.
-----------------	---------------	------------------------

Nominated by the Irish Employers Confederation:

Mr. J. Jennings	Mr. D. S. McAleese	Mr. J. J. O'Reilly
Mr. D. J. McAuley	Mr. P. Murphy	

Nominated by the Irish Farmers' Association:

Mr. D. Cashman	Mr. P. Lane	
Mr. S. Healy	Mr. J. Richards-Orpen	

NATIONAL ECONOMIC AND SOCIAL COUNCIL

THE ECONOMY IN 1973 AND THE PROSPECTS FOR 1974

I. INTRODUCTION

1. In this report we comment on the current economic situation and the outlook for the year ahead. Our comments and analysis refer to the conditions and prospects as seen in the light of the information available on 22 March 1974.

2. In Section II below, the main features of the economy in 1973 are summarised. In Section III we discuss the outlook for 1974 on the assumption that present policies are maintained. Finally, in Section IV, the implications of the forecasts for 1974 are discussed.

II. THE ECONOMY IN 1973

3. The latest estimates suggest that the main developments in the economy in 1973 were as follows:

- (i) In volume terms, GNP rose by about 7%. Much of the impetus came from the industrial sector, which grew by some 9½%. However, the volume of agricultural output declined marginally.
- (ii) In volume terms, exports of goods and services rose by 10½% while imports of goods and services rose by 13½%.
- (iii) There was a further deterioration in the balance of payments: the current deficit rose from £56 million in 1972 to £86 million in 1973.

(iv) There were significant increases in the main price indices: export and import prices are both estimated to have risen by around 19%. The consumer price index rose on average by 11.4%, with food prices rising on average by 16.5% and non-food prices by 8.9%; it is broadly estimated that about half the overall price rise in 1973 was accounted for by external factors.

(v) In 1972 the excess of imports of goods and services over exports of goods and services and net factor income from abroad was £98 million. This was financed by net transfers from abroad of £42 million and a net capital inflow of £107 million, with reserves rising by £51 million between December 1971 and December 1972. In 1973, the current trading deficit after allowing for net factor income from abroad was £161 million. This was financed by net transfers from abroad of £75 million (£44 million from emigrants' remittances, etc., and £31 million from EEC transfers), a net capital inflow of £89 million and an increase in external reserves of £3 million.

(vi) In volume terms, personal consumption rose by 6½%, public current consumption by 7½% and investment by 13¼%.

(vii) Employment in industry and services is estimated to have increased by 12,000 between April 1972 and April 1973. Taking into account an estimated fall of 6,000 in the number at work in agriculture, there was a rise of about 6,000 in total employment. Further evidence is provided by the increase in employment of 5,900 or 2.8% in transportable goods industries between September 1972 and September 1973. As regards unemployment, in terms of Live Register data, the figures for 1973 were on average 5,400 (or 7.5%) lower than the figures for 1972.

(viii) While the *volume* of net agricultural output fell by 0.5% in 1973, there was a significant increase in agricultural incomes (which include the value of changes in the numbers of livestock).

4. The estimates for the out-turn in 1973 differ significantly from the successive forecasts for 1973, as given in the *Quarterly Economic*

Commentary, published by the Economic and Social Research Institute, which contained the only forecasts published for 1973. Table 1 shows the successive changes in the forecasts for GNP in the five issues of the *Quarterly Economic Commentary* which discussed 1973.

TABLE 1

Percentage change expected in GNP for 1973 as compared with 1972

	Q.E.C. Oct. 1972	Q.E.C. Jan. 1973	Q.E.C. Apr. 1973	Q.E.C. Aug. 1973	Q.E.C. Dec. 1973
GNP at current market prices	% 13¼	% 14	% 15	% 18	% 20¼
GNP at constant prices (Volume)	5¼	5¼	5	5¼	7
GNP Deflator (Prices)	7½	8½	9½	11½	12¼

Source: Quarterly Economic Commentary: E.S.R.I.

There are a number of reasons why the earlier forecasts for 1973 differed so widely from the latest estimates of what happened in that year:

(a) When the earlier forecasts were being made, very little firm statistical data were available for the second half of 1972. It is now clear that there was a definite up-turn in the middle of 1972 and rapid expansion in the second half of the year. There was at the least only a glimmering of this even in the winter of 1972. Lack of information about the direction and rate of change of the economy inevitably meant that the earlier forecasts were very much on the low side.

(b) The five forecasts for the increase in personal consumer expenditure in the successive issues of the *Commentary* between October 1972 and December 1973 were 10½%, 11½%, 13%, 15¼% and 18¼%. The earlier forecasts were based on the assumption that there could be only very small increases over and above the basic terms of the 1972 National Agreement.

When the quarterly industrial inquiry figures for the second quarter of 1973 became available in November 1973, it became clear that the basic terms of the Agreement were being used as a basis for further negotiation and earnings rose more rapidly than could have been expected. The rise in retail sales in the first few months of 1973, both in value and volume, was seen as a temporary phenomenon, given the then expectation that earnings would rise about 11%. If the movement in earnings had been forecast correctly, the growth in retail sales would have been seen in a different light. By the summer of 1973, the forecasters were having severe difficulties in allocating industrial production between exports and home sales. With hindsight, it would now seem that manufacturing production was growing at about 13%, that manufactured exports were increasing in volume terms at a slower rate than had been forecast in earlier issues of the *Commentary*, and that personal consumption (as a result of the rapid growth in money incomes) was growing much faster than had been forecast. Consumer prices were underestimated in the earlier forecasts, because the expectation that food prices would rise more slowly in 1973 was not fulfilled, and the prices of non-food items rose faster because of the more rapid growth in money incomes and in import prices.

- (c) Data for export and import prices only became available for the first six months of 1973 early in February 1974. The increase in unit values, particularly for exports, for the first six months of 1973 was unexpectedly large. The increase in export prices for manufactured goods was under estimated in the forecasts for 1973, probably because not enough weight had been attached to the effects of the devaluation of the Irish pound in line with sterling. The degree of diversification in exports towards markets other than the UK may perhaps have been underestimated. The increase in the prices of imported materials and the high import content of industrial exports pushed up the prices of the latter. In the countries in which industrial exports were sold there was both relatively high inflation and real growth in output. Consequently the higher costs of Irish

exporters could be passed on in higher prices. As a result of these developments, the August 1973 and December 1973 editions of the *Commentary* reflect a relatively faster percentage growth in the forecasts for export *price* increases than for export *volume* increases. In the case of exports of cattle and beef, substantial increases had been expected in earlier forecasts, in fact the volume fell by about 12%.

5. At this stage the estimates for 1973 must still be regarded as provisional because some important statistics relating to that year are not yet available. For example, export and import unit values are available only for the first half of 1973, and the quarterly index of industrial production is not available for the fourth quarter. Experience suggests that when the first official estimates are produced they will subsequently be revised. In the years in which real growth rates of 4% or more were actually achieved, namely 1967, 1968 and 1969, the estimate made in the spring of the following year underestimated the true rate. For these three years the estimated price deflator for GNP was generally fairly close to the figure which ultimately emerged. There were, however, significant revisions in the first estimates for the price deflators for public net current expenditure and gross domestic fixed capital formation. The difficulty of estimation is compounded by the absence of published data for monthly or quarterly estimates for national income and expenditure. The available information—for example, the seasonally corrected figures for electricity consumption, cement sales, industrial production and retail sales—suggest that there was little or no growth in the economy during the first half of 1972, very rapid growth from the middle of that year to the first quarter of 1973, and a flattening-out thereafter, with the level of activity in the second half of 1973 being no higher than that in the first half of 1973. As more data become available, it must be expected that the estimates for 1973 will be revised.

6. The estimated growth in GNP in 1973 was surpassed only by the rate achieved in 1968 and was significantly greater than the 4.7% reached in 1972. The expansion was due mainly to the significant expansion in personal consumer expenditure, together with increases in industrial output to which exports contributed a large part. Certain

sheltered, non-exporting sectors such as building and construction also made significant contributions. The high growth rate was achieved in the context of rapid expansion in the main industrial economies and in international trade.

7. The growth in the volume of national production was led by the industrial sector, whose output is estimated to have increased by around 9½% in 1973. In the case of the services sector, it is estimated that a volume increase of over 6% occurred. In the agricultural sector, output is estimated to have declined marginally.

III. PROSPECT FOR 1974

8. At this stage the Council is not equipped to make its own forecasts for 1974. However, we would hope to be in a position to do so for 1975, because we believe that independent attempts to forecast the direction of the economy are necessary and desirable. Our secretariat has had discussions with the staff engaged in forecasting in the Central Bank, the Department of Finance and the Economic and Social Research Institute. The purpose of these discussions was to agree the assumptions on which a forecast for 1974 might at this stage be based. Given the uncertainty inherent in any forecasting exercise, different forecasts can, of course, rest on the same set of assumptions. In addition, the Department of Finance has given us its views on likely trends in 1974. In doing so, the Department stressed that predictions regarding the likely course of events in 1974 must be considered as even more tentative than usual at this time of the year because of the many uncertainties surrounding the short-term outlook and the dependence of the predictions on the validity of a number of key assumptions.

9. The Department's views were based on the following assumptions:

(a) *The Oil Situation*

Supplies of oil in 1974 are expected to be around the same level as in 1973, but through economies, this will be adequate to allow growth of around 4% in national production. The average rise in the price of crude oil in 1974 is assumed to be around 150%.

(b) Increases in wages and salaries will be in line with the terms of the 1974 National Agreement.

(c) *External Situation*

It is assumed that while economic growth in our trading partners, other than the UK will slacken in 1974, there will be a positive rate of growth. With regard to the UK, little increase in the volume of national production on 1974 as a whole can be expected.

(d) *Budgetary Assumptions*

For the purposes of this exercise the simplifying assumption is made that no greater current budgetary stimulus will be given in 1974/75 than was given by the final out-turn in the year 1973/74. A further substantial rise in the public capital programme at current prices is assumed.

10. On the basis of the terms of the 1974 National Agreement the Department estimates that non-agricultural employee incomes will rise by between 17% to 18%. It is likely that increases in profits, etc., will be markedly less. Agricultural cash incomes are also likely to increase at about the same rate as non-agricultural employee incomes. Agricultural stocks are expected to rise less rapidly than in 1973.

11. The Department expects industrial output, which expanded at a very rapid rate during 1973, to increase more slowly during 1974, partly because of the more unsettled conditions in international markets and partly as a result of the smaller degree of spare capacity available. For the industrial sector as a whole, including construction, public utilities, etc., an increase of around 5% in volume is forecast. The volume of sectoral output in agriculture is also likely to show an increase, following a marginal fall in 1973. The increase in the volume of output in the services sector is normally the most difficult to predict and this again is likely to show a smaller increase in 1974 than in 1973 in conjunction with the expected slackening in the rate of increase in economic activity. In general, prospects at present are for an overall growth rate for the economy during 1974 of the order of 3½% to 4%.

12. The discussions with those engaged in forecasting in the Central Bank, the ESRI, together with the Department of Finance's views on likely trends, suggest that the economy might develop as follows in 1974:

- (a) On the assumptions listed in paragraph 9 above, increases ranging from 2% to 3% in volume of personal consumption; from 5½% to 6¼% in public current consumption; from 2½% to 3½% in gross domestic fixed capital formation; from over 8% to 9¾% in the volume of exports and around 5% in the volume of imports, could occur in 1974.
- (b) The volume of imports is expected to grow at a significantly lower rate than in 1973. This is mainly explained by their high level in 1973 (mainly because of imports of ships and aircraft) and the slower growth forecast in national output in 1974.
- (c) In volume terms, the forecasts suggest that GNP would rise at a rate between 3% and 4%.
- (d) Significant increases are expected in the main price indices. Average import prices are almost certain to rise faster than last year and while average export prices should also be appreciably higher, some worsening in the terms of trade can be expected. Consumer prices could, on average, be about 14% greater than the average for 1973. This would reflect the further increases expected in import prices and the significant growth that is forecast for money incomes.
- (e) The forecasts for the balance of payments deficit on current account range from £124 million to £145 million, after account is taken of estimated net receipts of about £60 million from EEC transfers. The estimates for the net capital inflow range from £100 million to £115 million. If the former figure were realised, the external reserves could fall by between £24 million and £45 million.
- (f) The forecasts of a general slackening in the rate of economic activity have implications for the different sectors of production. The increase in industrial production is likely to recede from the high rate of growth experienced in 1973. A slowdown in the

growth rate for the services sector is also likely to occur. In the case of the agricultural sector, a small percentage increase is forecast in the volume of output, following the large build-up in agricultural stocks in 1973.

- (g) Since the forecast growth in GNP ranges between 3% and 4%, little change is forecast for total employment in 1974. The rise in industrial employment may therefore be relatively modest, and at best the increase in non-agricultural employment might only be sufficient to offset the expected decline in the numbers engaged in the agricultural sector.

13. We wish to comment on three issues. First, the forecasts for the increases in agricultural incomes in 1974: there was a substantial increase in agricultural incomes at current values (including the value of changes in livestock numbers) in 1973. During 1974 there is the likelihood of a rundown in the stocks accumulated last year. As farmers' incomes (in the national income sense) include changes in the value of livestock, any increase in agricultural incomes is dependent on the level of stock changes in 1974 as compared with 1973. In addition, agricultural incomes will be affected by decisions yet to be taken by the Council of Ministers in Brussels. Until these decisions are taken, considerable uncertainty must remain as to what increases (if any) might occur in agricultural incomes in 1974.

14. Second, the forecast rise in non-agricultural money incomes could be on the low side. The basic terms of the 1974 National Agreement, in conjunction with the carryover effect of the 1972 National Agreement, give an increase of almost 15% in the calendar year 1974 as compared with 1973, without taking account of wage "drift" or increases in numbers employed. Assuming very little change in employment in 1974, this would leave about 3% as an allowance for "drift"—that is, increases over and above those contained in the 1972 and 1974 National Agreements. Past experience suggests that this could be on the low side.

15. Third, it is particularly difficult to forecast by how much prices will rise in 1974. If consumer prices remained throughout 1974 at their level in December 1973, then the consumer price index would on average be 6½% higher in 1974 than in 1973. This leaves 7%–8% of the forecast

increase in consumer prices in 1974 to be explained by increases in import and export prices and the effects on the prices of home-produced goods of the increase in money incomes. If money incomes or import prices rose faster than forecast or if the growth in the economy were less than 3%–4%, the rise in consumer prices would be correspondingly greater.

IV. POLICY IMPLICATIONS

16. Any forecasts for 1974 must be based on what is known about the direction and rate of change of the economy at the time the forecasts are being made, as well as on assumptions about major factors that will influence developments in 1974, such as budgetary policy, changes in money incomes or the growth in the economies with which Ireland trades. At present, some essential statistics (e.g., export and import unit values) are not even available for the third quarter of 1973 and many key statistics are unavailable for the fourth quarter. The foundation for any forecast that is now made for 1974 is, therefore, less than adequate, because of the uncertainty surrounding what actually happened in the recent past. To this must be added the inescapable uncertainty about future developments both within and outside the Irish economy.

17. Any forecasts made at this stage must therefore be tentative. Forecasts made in the spring can seldom be firm enough to be taken as the basis for policies aimed at "fine-tuning" the economy. The inescapable margin of error in the best forecasts is probably greater than the difference that any feasible changes in policy could make to the outcome. However, these problems associated with forecasts relating to the year ahead do not mean that forecasting is not necessary. The forecasts help to focus attention on the main things that determine the direction in which the economy is likely to move. They also provide essential information to those who have to make economic decisions, whether in the public or private sectors.

18. We consider the assumptions on which the forecasts for 1974 are based to be reasonably situated within the framework of possibilities.

The most optimistic forecasts for 1974 suggest that the growth in national output will at 4% be about equal to the average growth rate achieved in the 1960s, that the prospects for any increase in employment are poor, and that the anticipated rise in prices and in the external deficit will both be much greater than the increases experienced hitherto.

19. In our view, the forecasts for 1974 do not warrant the application of restrictive monetary and fiscal policies aimed at dampening the development of the economy. If applied, such policies could have little effect before next autumn, and their effect on the growth in output and employment would only be felt thereafter. Moreover, they would not have any significant effect on the growth in wage—and salary—rates (which must be taken as a datum following the 1974 National Agreement), or on oil prices and the other external factors which will influence the rise in prices in this country. By curbing the growth in domestic output, they could raise rather than lower unit costs and in the short-run increase the effect of the rise in money incomes on prices and perhaps make it more difficult to maintain industrial exports. Indeed, the very considerable increase in import prices could by itself exercise a deflationary effect through its effects on reserves, unless offset by an appropriate monetary policy.

20. There remains the issue of whether or not expansionary policies should be applied in 1974 over and above those implicit in the budgetary assumptions, in paragraph 9 above, on which the Department's forecasts are in part based. The patterns of the growth in investment and output in recent years do not suggest that productive capacity would not be available to permit a growth rate somewhat higher than 4%, though capacity constraints could occur in a few sectors. Nor is a higher growth rate likely to be constrained by a general shortage of labour. Policies that were modestly more expansionary would be unlikely to cause a larger increase in wage—and salary—rates. Nor would they be likely to cause a faster growth in prices (than the very high rate already forecast), given the extent to which prices are affected by external influences and the terms of the 1974 National Agreement. Some expansionary stimulus would help to maintain or even increase the numbers at work. It would, however, also make for a higher external deficit.

21. The decision on the aims of short-term economic policies must also be influenced by how the relative competitiveness of Irish products is likely to change in 1974. The forecast increase in aggregate money incomes is much greater than the forecast growth in national output, so that domestic costs (and therefore prices) must rise. This relationship between the increases in incomes and national output will not be materially changed by whether policy is restrictive or expansive—indeed, expansive policies might improve it. Moreover, whether or not Irish products become more or less competitive during 1974 will depend on the relationship between the growth in money incomes and the growth in output in the countries to which Ireland exports, or from which it imports, goods and services. If competitiveness deteriorated, the growth in exports would be curbed and imports would be substituted for home-produced goods. However, we do not have any firm data about what is likely to happen to the relationship between the growth in incomes and output in other countries in 1974. We cannot, therefore, reach any firm conclusion about how the relative competitiveness of Irish products is likely to change during this year.

22. Having considered the range of forecasts for 1974, and the assumptions on which they were based, we have concluded that the aim of budgetary and monetary policies in 1974 should be to add about 1% to the growth in output. The specific measures which are used should as far as possible encourage productive investment and efficiency. At the same time, the necessary measures should be taken, within the context of policies which give this modest further stimulus to the economy, to ensure that special attention is paid to those with low living standards.

23. Without the modest expansionary stimulus we envisage, the growth in employment is not likely to reduce underemployment to any significant extent, or to reduce appreciably the numbers on the Live Register. Without the additional stimulus over-all employment is therefore unlikely to rise. We have noted that other countries have made special use of programmes for industrial training and retraining as a part of the range of policies for dealing with this kind of situation.

24. By the spring, many of the influences that will shape the development of the economy during the remainder of the year are already determined, and the scope for influencing the evolution of the economy is correspondingly limited. Moreover, there are obvious disadvantages in looking at one year in isolation; what may happen during it is influenced by what happened in the past; what happens during it will help determine what will happen in the future. We have in mind here, such factors as the Balance of Payments deficit (which may continue at historically high levels in 1975) and the increase in aggregate money incomes, which is likely to be substantially higher in 1975 than in 1974. The main lesson that emerges from the issues discussed above is that more than forecasting is needed if the objectives set out in our terms of reference are to be met. There is an urgent need for a programme or plan for economic growth and development extending over the three to four years ahead. The longer period provides the scope for the orderly evolution and development of economic and social policies. Moreover, an economic plan would provide a framework to which short-term forecasts and policies could be related.