

**THE INTERNATIONAL ECONOMIC OUTLOOK FOR 1992**

**Remarks by Robert P. Forrestal  
President and Chief Executive Officer  
Federal Reserve Bank of Atlanta**

**To the German American Chamber of Commerce  
Atlanta, Georgia  
January 8, 1992**

It is always gratifying to be invited to speak before this group, particularly since I have long been interested in international trade and finance. This year is an especially significant time to contemplate worldwide economic interchange, because, in December, we will mark the beginning of the single European market. EC 1992 dramatically symbolizes the watershed we have reached in the world with the closer integration of countries--not only in trade, but also in other dimensions, such as defense and the environment. We need only think about what happened in Maastricht, The Netherlands, last month to realize the great strides that are being made in global integration. At that historic gathering, EC members agreed in principle on a number of profound changes, including eventual monetary union.

Signs of this sea change are also apparent in Germany. With its efforts in East Germany, Germany is providing a model of how the world can integrate the rest of the formerly communist-based countries. More generally, we have begun to see in an astonishing variety of ways examples of integration. The Mideast peace talks, the Allied response to the Iraqi invasion of Kuwait, and the U.S./Canada acid rain agreement all testify to a new spirit of cooperation to achieve goals that transcend narrowly national interests.

In my remarks this evening I would like to explore this theme of integration, including

the challenges and difficulties that threaten to reverse this momentum. First, however, let me supply a foundation for what follows by giving you my outlook for the international economy in 1992, beginning with the G-7 countries.

### **International Overview**

Overall, growth will continue to be slow during 1992 for the group of seven industrialized nations, with the U.S. rate being lower than most of the others. Average GNP growth should come in between 2 1/2 and 2 3/4 percent for the industrialized nations, excluding the United States. This rate would be up slightly from the somewhat-less-than-2-percent average growth the foreign industrialized countries were projected to have in 1991. The U.S. economy should also pick up, but to a slower pace of about 2 percent, after shrinking slightly in 1991. The final figures will probably show that GNP contracted about 1/2 a percent or perhaps somewhat more, on an annual average basis last year.

Inflation in all of the G-7 countries seems to be under control and should slow to an average rate of about 3 3/4 percent in 1992. Price pressures look more moderate than they have in some time in the United States, and the consumer price index (CPI) should turn out to be 3 percent or a bit higher as an annual average, in line with the other industrialized nations.

### **U.S. Economic Outlook**

To expand further on the U.S. economy, since employment lags behind GNP and many businesses are consolidating, I think the jobless rate will remain pretty much unchanged from its

6.8 percent rate during the year. Although the recovery was slow in coming, the pace of business activity should accelerate gradually this year as current problems are worked through and more household and corporate income becomes available for spending. Of course, progress will not be even across the economy, with the construction industry--especially commercial--still being the slowest to recuperate. The industry suffers from excess supplies due to past overbuilding as well as the resultant appropriate hesitancy among many lenders to finance new projects. In addition, demographics are contributing to the sluggish housing market. There are not as many first-time home buyers as there were when the United States came out of the last recession in 1982. Besides the lingering weaknesses in construction, consumer demand for durable goods remains poor. Fewer new households translate into fewer purchases of new household appliances.

Not all the news is bad, however. The forces supporting growth should be exports and consumer spending, particularly on services. Net exports should continue to be a source of some support, but the pace of expansion will be slower than in the last few years. While personal income growth has been slow, it has also been steady, lending support to consumer spending, especially for services. It is true that consumers continue to be cautious with their purchases, but even under these circumstances the economy can still grow slowly.

### **Outlook for other Industrialized and Developing Countries**

Among other G-7 countries, the outlook for average GNP growth is strongest for Canada, which should come in with more than 3 percent growth in 1992, up from a contraction of about

1 percent last year. The United Kingdom seems to be recovering from its cyclical problems slowly. Japan will likely see a large decline in its rate of growth from about 3.7 percent on average in 1991 to less than 2.5 percent in 1992. In addition, Japan may create a source of friction among the countries with which it trades, because its trade and balance of payments surpluses are expected to rise after many years of decline. West Germany has increased taxes to pay for unification with East Germany and raised interest rates. These policy moves should result in slower growth in the near term. One other possible problem facing the German economy this coming year has to do with bank loans made to the U.S.S.R. The Soviet Bank for Foreign Economic Affairs announced in December that it would withhold principal payments on its debt from commercial banks as well as from the G-7. This action may affect German banks in 1992, since they hold much of the Soviet debt.

Inflation rates in Germany, Japan, and Canada should be even lower than the average annual rate for the G-7 countries, coming in at about 3 percent in 1992. Inflation in western Germany, however, is expected to rise in the coming months, mainly because of the tax increases and the possibility of liberal wage settlements. Steelworkers and banking unions are demanding pay hikes of more than 10 percent, far from the latest offer by employers. Unlike Germany, Japan's economic slowdown appears to be dampening inflation, and it should moderate further as the economy decelerates.

In contrast to the slower growth in the advanced economies, the newly industrializing countries of the Pacific Rim may post growth rates of between 5 percent and 6 percent on

average. As I pointed out last year at this meeting, Latin America has become a bright spot in the economic landscape. After years of no growth and astronomical inflation, many of these countries have taken major steps toward strengthening their economies by stabilizing their currencies and privatizing what were once government-run businesses. Leaders have asked their people to be patient and to wait for the economic payoff. Naturally, taking such a long-term stance takes its toll on both political leaders and citizens. However, some of these efforts are beginning to yield returns: the average 1992 growth rates may range from 5 percent in Argentina to as high as 10 percent in Venezuela. More generally, Latin American countries as well as former eastern bloc nations, such as Poland, seem to have reached the conclusion that a market economy represents a better way to cope for the long term. India, too, is beginning to deregulate its economy with help from the International Monetary Fund.

Unfortunately, Africa continues to be the exception to the rule of faster growth or even its prerequisite--a transition to market-based economic systems. Structural problems in the various economies prevent any purposeful movement toward stability. Of course, the recent problem in Kenya depressed the hopes of those who had held it up as an example of progress.

To sum up the world economic outlook for 1992, the United States and the other industrial countries can expect faster growth on average than last year, but slower growth overall compared with recent years. In contrast, many developing countries, except for those in Africa, can expect somewhat faster growth. Undergirding this improvement in the developing countries is the move toward market economies, which is heartening to all of us who have long hoped for



a more integrated global economy.

### **Integration: A Longer-Term Trend Taking Hold in 1992**

As I remarked earlier, we can see integration being played out in many dimensions in the world. One country that is taking a straight path toward integration is Germany. For instance, in October, it announced a shift in its policy toward reforming the EC's Common Agricultural Policy (CAP), which pertains to agricultural subsidies. This shift managed to give the GATT talks a breath of fresh air, at least momentarily, until other EC members delayed attempts to reform CAP until after the Uruguay Round. Germany has also taken on the important task of bringing the East German economy up to the West German level. A long-term, strategic perspective makes the people of former West Germany willing to put up with slower growth in the short term while integrating East Germany.

At the level of regional integration, the most notable effort is going on in the European Community. While I daresay many of us in this room probably believed that the EC agenda of 1992 would happen, I doubt that we believed Europeans would move so boldly beyond these goals toward an agreement on monetary union. Now that EC members have signed off on the proposal, a single currency that would most likely be based on the Deutschemark should go into effect in 1999. In addition, would any of us have believed the EC would be talking of one central bank? This idea was beyond our expectations two years ago. Of course, not everything is picture perfect. Great Britain remains reluctant to go along with many of the ideas being proposed. Also, the EC has not resolved how it will handle developing countries of Eastern

Europe that wish to join the community. All in all, however, it is a remarkable period of achievement in planning for the future of the EC.

In the same vein, steps toward greater international cooperation, if not outright integration, are being taken in many areas, perhaps without our full recognition of their significance. We are witnessing tremendous changes in financial markets, which are forging ahead at a rapid pace to become truly worldwide in their linkage. These changes have profound and generally positive implications for all countries, both large and small. In order to keep pace with the increased volume and scope of financial transactions, the financial industry has turned to automated trading systems. The globalization of financial markets, together with their automation, is giving far wider access to credit to all would-be borrowers.

The other hopeful aspect of these moves toward global integration is that they are working in dimensions beyond trade. For instance, integration is spilling over into politics in a positive way with the Mideast talks. The Arabs and Israelis may not have decided much, but we cannot lose sight of the fact that this is the first time they have even talked with each other. We also saw a unified response to Saddam Hussein. The many countries that supported the Persian Gulf War with soldiers, materiel, and financing recognized that the invasion of Kuwait by Iraq posed a threat not only to the political stability of the region, but ultimately to the economic security of the whole world. The resulting coordinated defense involved the kind of integration that we have just begun to see in trade--the area that we traditionally expect to be the focal point for global integration.

## Major Issues

However, as good as the atmosphere toward global integration was in 1991, some challenges loom large. In the first place, a major logjam revolves around multilateral trade issues. The GATT talks have been stalled by almost intractable disagreements over topics such as intellectual property and agricultural subsidies. Meanwhile, regional trading blocs have perhaps begun to seem more achievable than worldwide trade. I lament the growing wave of sentiment for trading blocs, because I strongly believe that the only way to achieve a true global economy is through broad multilateral trade agreements, such as the GATT. However, I do hold out the hope that the nations of the world will not stop at trading blocs alone. Rather, I believe these blocs could serve a useful purpose if they become pilot projects for worldwide trade.

Nationalism in various areas of the world is another roadblock to integration. Centrifugal forces among the provinces of Canada seem to be growing stronger. In Yugoslavia, we are seeing the worst form of nationalism leading to a war between peoples of the same country. This civil war is causing the deaths of thousands of people, the bombing of historic cities, and the destruction of property throughout Croatia. If countries remain more concerned with promoting their own identities than with understanding their relationship to other countries and the world, integration will be harder to achieve.

The former Soviet Union is presenting us with an even greater cause for concern about nationalism. Although Boris Yeltsin and other leaders have forged a new Commonwealth of Independent States, the disagreements among the many people of different nationalities who made



up the old union still remain. This fact is a particular concern because many of these new nations have nuclear arms on their soil, and control over these armaments has not been completely resolved to the satisfaction of the rest of the world. In addition, it is difficult to make economic progress in the face of social disorder like that taking place in former Soviet Georgia. The consequences of moving toward market prices, for example, are that much harder to accept when ethnic tensions have already fanned the flames of social unrest. Unfortunately, there is little that we in the rest of the world can do; it is the leaders of these former communist countries who must squarely address this troublesome issue.

In addition to the divisive nationalistic forces and, in the USSR, related problems like arms control, the slow growth that the industrialized countries will see in 1992 could also be a drag on the impetus toward global integration. In the United States, for instance, our economy is going through a period of adjustment, working through the consequences of past decisions that engendered short-term, unsustainable growth through borrowing. Now we are beginning to service that debt, much of which is owed to other nations, since we lacked the savings domestically to meet our demand for financing. In the past, growth in output was generally translated into growth in domestic consumption, but that is not true now because of the debt service burden. This burden is also limiting our capacity to grow.

Finally, pollution in the newly industrializing countries and the eastern bloc has become a major issue. It may cause the world to redefine how it measures growth by taking into account the effects on the environment. The sad fact is that while the powerful countries in the world

today were industrializing, they burned coal and built nuclear reactors and cut down forests, among other things. While all of these practices may have contributed to pollution, the environment was more capable of absorbing the effects. Now if countries like China and India were to do the same things other countries did as they modernized, the cumulative affect on the environment could be devastating. It seems persuasive to me that if we are to preserve the quality of our environment, we must begin to think of the harm we cause it through growth. One way to address this problem is through pricing that more accurately reflects environmental consequences. Another approach is through new programs that allow developing countries to swap debt for environmental conservation projects. Through the beginning of last year, such swaps retired nearly \$100 million of Latin American debt, according to one estimate. This sort of program gets to the heart of our concerns for the environment and demonstrates how global integration functions now to improve living standards the world over.

## **Conclusion**

In conclusion, this is an exciting time in world history, as we move toward global integration--not just in trade, but in other dimensions as well, such as defense and the environment. The world is moving closer on many levels, as I have outlined. We cannot let our concerns about slower growth divert us from our primary long-term goal--that all nations of the world will be able to raise their standards of living through enhanced international exchange and cooperation.