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GROWTH, INCOME DISTRIBUTION AND HOUSEHOLD WELFARE IN THE INDUSTRIALIZED COUNTRIES SINCE THE FIRST OIL SHOCK

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EXECUTIVE SUMMARY

During the first two decades of the post-World War II period, an era often called the "golden age of development", economic and social conditions improved at an historically unprecedented pace. Thus, for instance, GDP growth rates in both Eastern and Western Europe doubled relative to those of the interwar years. This performance was accompanied in most countries by a movement toward greater equality in household incomes and a rapid expansion of public expenditure on education, health care, housing, social security and welfare.

However, in both East and West, trends in growth, public expenditure and income distribution changed radically during the period from the first oil shock to the late 1980s. Despite vastly different institutional structures, a large number of parallels has been found between the experiences of the market economies and those of the centrally planned economies.

In both sets of economies the oil shock acted as a detonator for a sharp deceleration in growth that had been rendered inevitable by earlier trends and policies, particularly accelerating inflation in the West and the weaknesses of central planning in the East. GDP growth, which had averaged 4.3 percent and 5.0 percent per year, respectively, in the countries of the Organization for Economic Cooperation and Development and in the centrally planned economies between the early 1950s and 1973, dropped to less than one-half these rates during the subsequent ten years.

In turn, the slowdown in growth prompted a radical reorientation in policies. In the West the objective of full employment was sacrificed, the growth in public expenditure was curtailed and taxation became more regressive. In the East, system reform led to cutbacks in collective consumption and greater reliance on market forces.

In both East and West household welfare suffered, as policies exacerbated the negative effects of slower growth: income differentials widened; the growth of public expenditure on health care and education faltered substantially, and the incidence of poverty increased.

In the West this process may checked or even reversed in the 1990s. In the East, progress toward the market economy during the decade is bound to generate a decline in living standards and widening gaps in equality.

I. INTRODUCTION

This paper sets forth a broad survey of some of the major macroeconomic and policy trends in the industrialized countries, both East and West, that may have had a bearing on household welfare and child poverty during the period from the first oil shock of 1973 to the end of the 1980s.

Any survey of macroeconomic events over such a time span could clearly examine a large number of subject matters and a whole host of countries. To maintain the task a manageable one, the paper is limited to an investigation of three areas in which major changes seem to have occurred that, directly and indirectly, are bound to have affected child welfare in the 1970s and 1980s:

- The pronounced deceleration in overall growth that has been observed in the market economies and in the centrally planned economies of the industrialized world from the mid-1970s onward.

- The changes which took place over the same period in both East and West in public expenditure and taxation as a result of the shortfall in growth and of new attitudes and approaches to economic policy.

- The modifications in household income distribution consequent upon both the lower growth and the alterations in public spending and tax policies.

Space constraints also dictate some limitation on country coverage. On the Western side the information presented includes, as far as possible, data on the seven major economies (Canada, France, Germany, Italy, Japan, the United Kingdom and the United States), as well as on some of the smaller European economies, particularly Austria, the Netherlands, Spain and Sweden. On the Eastern side the attempt is made to cover the Soviet Union and several of the smaller European centrally planned economies, especially Bulgaria, Czechoslovakia, the German Democratic Republic, Hungary and Poland. The frequent lack of reliable data, however, precludes in this instance as detailed an examination as that presented for the countries of the Organization for Economic Cooperation and Development.

The next three sections look in turn at the issues of growth, public expenditure and household incomes. Each section examines the experience of the market economies and then that of the centrally planned economies and ends with some comparative comments. The final section presents a brief summary of the principal arguments, underlines some of the more interesting parallels and differences between East and West and provides a few pointers for the future.

II. GROWTH

That a pronounced slowdown in economic growth occurred throughout the industrialized world in the last two decades is well known. Before the 1970s economic growth had been exceptionally rapid and relatively smooth in both East and West. While few industrialized countries had ever achieved an economic expansion of much more than 3 percent per annum for a prolonged period in the years preceding World War II, virtually none grew by less than 4 percent annually from the early 1950s to the early 1970s. The countries of both Eastern and Western Europe, for instance, roughly doubled their performance from the 2.5 percent annual rate of output expansion that had characterized the interwar period. In the case of Japan, growth trebled to a rate close to 10 percent per annum.

This "golden age" came to an abrupt end in the early 1970s. Evidence for the deceleration is shown in Table 1. Panel A presents the familiar story for the OECD countries: two sharp and sudden breaks in the trend took place after 1973 and 1979 following the oil shocks of those two years. The data also suggest that some recovery in economic activity, albeit modest, occurred in the later 1980s, a recovery which was no doubt tied to the "counter" oil shock of 1986.

Panel B provides tentative Western estimates on a GDP basis for Eastern Europe. While the data are clearly subject to error, they are almost certainly more reliable, as well as much broader in coverage, than the official statistics on net material product. These have always been thought by Western experts to be upward biased, and recent revelations in Eastern Europe about the extent of earlier statistical misreporting have fully confirmed the doubts (Zoteev 1991). As they stand, the data show a deceleration which is very pronounced and not much more gradual than that in the West. Moreover, in contrast to the growth revival in the West in the late 1980s, the performance of the centrally planned economies seems, if anything, to have deteriorated even further in the closing years of the decade.

The OECD Countries

The deceleration which set in among the OECD nations after 1973 was sudden, sharp and pervasive. Every OECD country shared in the negative experience of stagflation in 1974 and 1975. Fifteen countries recorded falls in output during one or the other year; as many as 20 suffered double-digit inflation, and virtually all showed growth rates between 1973 and 1979

Table 1: GDP GROWTH RATES
(Average Annual Percentage Changes)

Panel A: *Selected OECD Countries, 1953-89*

	1953-73	1973-9	1979-84	1984-9
Austria	5.4	2.9	1.4	2.7
Belgium	4.3	2.4	1.4	2.7
Canada	4.7	4.3	2.2	3.9
Denmark	4.1	1.9	1.7	1.7
Finland	5.1	2.4	3.3	4.0
France	5.3	2.8	1.5	2.8
Germany (FRG)	5.4	2.4	1.1	2.7
Italy	5.3	3.7	1.9	3.1
Japan	9.3	3.7	3.9	4.5
Netherlands	4.8	2.6	0.6	2.7
Spain	6.1*	2.2	1.2	4.3
Sweden	4.0	1.8	1.7	2.4
Switzerland	4.4	-0.2	1.5	2.9
United Kingdom	3.0	1.5	0.8	3.8
United States	3.4	2.6	1.9	3.4
Western Europe	4.7	2.5	1.4	3.1
Total OECD	4.3	2.8	2.1	3.5

Panel B: *Eastern Europe and the Soviet Union, 1950-88*

	1950-73	1973-82	1982-8
Bulgaria	6.1	2.4	1.4
Czechoslovakia	3.8	1.8	1.8
Germany (GDR)	4.6	2.6	2.1
Hungary	4.0	1.9	1.4
Poland	4.8	0.5	4.2
Rumania	5.9	3.7	2.9
Soviet Union	5.0	2.1	1.9
Yugoslavia	5.7	5.0	0.9
Eastern Europe	5.0	2.8	2.1
Eastern Europe/Soviet Union	5.0	2.3	2.0

Sources: *National Accounts of OECD Countries* (various), OECD (1990), Maddison (1989), IMF (1990a).
* 1954-73.

that were much lower than those of previous years, the only exception being Norway, which greatly benefited from its large North Sea oil reserves. The story was repeated, if in more moderate form, at the end of the decade. There was renewed recession in 1980-2 and only a modest recovery in 1983-6, at least in Western Europe and Japan.

The immediate cause of these developments was, of course, the two oil shocks of 1973-4 and 1979. The direct impact of these shocks on consuming countries was inflationary and deflationary at one and the same time: inflationary because of the upward push the shocks gave to the prices of essential commodities and deflationary because of the fall in demand that was generated by the shift in world income distribution toward the low-spending nations of the Organization of Petroleum Exporting Countries. As a result, both the aggregate-demand and the aggregate-supply schedules for the industrialized countries as a whole shifted inward in a way which led to a combination of higher prices and lower quantities (Bruno 1984). These effects were superimposed on fragile economies, many of which were already suffering from rapid inflation, and some of which were beginning to slow down in the wake of an earlier tightening of policies. Performance was bound to worsen, at least in the short run.

Yet, these direct effects of the oil price shocks cannot provide the full reason for a medium-term deceleration which very nearly halved the growth rate of the OECD countries over a decade and a half. While between 1960 (or 1950, for that matter) and 1973 the GDP of these nations had risen by some 4.5 percent per annum, growth slipped to less than 3 percent between 1973 and 1989; for Western Europe the deceleration, from nearly 5 percent to only 2.25 percent, was even sharper. Most explanations for this trend of worsening performance point to the operation of a number of additional and interrelated demand and supply factors that contributed to further inward shifts in the aggregate-demand and aggregate-supply schedules over the medium run (Bruno 1984).

On the supply side an important feature of the shock in the mid-1970s was the reluctance of wage earners to bear the inevitable brunt of the deterioration in the terms of trade. Thus, real wage targets in most countries remained geared to the earlier trends of income growth. Yet, the room available for such growth had been sharply curtailed not only by the deterioration in the terms of trade, but also by a medium-run deceleration in productivity growth, itself largely caused by the shock (Bruno and Sachs 1985). In such circumstances wage resistance exacerbated inflation and shifted the adjustment onto profits. These, after slumping in the mid-1970s, fell further in the early 1980s as recession cut into capacity utilization. The drop in profits led in turn to a sharp decline in investment demand. The demand-side slump was intensified by the switch to restrictive policies, designed to curtail inflation, that took place in some countries after 1974 and essentially in all nations after 1979 (Boltho 1984).

A widespread, though not universal, consequence in Europe was a sharp increase in unemployment that stood in stark contrast to earlier trends. In the 1950s and 1960s most of the OECD countries had realized an unprecedented achievement for developed, and for that matter for less developed, societies: the attainment of virtual full employment. Earlier agricultural economies had traditionally experienced underemployment on the land; more recent industrialized societies had suffered from the cyclical unemployment generated by business fluctuations. By the 1960s the economies of Western Europe, Japan and North America had been able broadly to eliminate both these phenomena.

Unfortunately, the achievement was short-lived. By the late 1980s unemployment in most Western European countries had risen to levels not previously recorded during the postwar period (Table 2). In addition, this unemployment carried with it two particularly unwelcome features: a sharp jump in the number of spells of unemployment and a concentration on marginal segments of the labour force. Long-term unemployment, with its attendant cost in human capital erosion, was much more prevalent in the 1980s than it had been in earlier decades; so, too, was youth unemployment, which, in Southern Europe in particular, affected as much as 30 to 40 percent of the relevant age groups.

Japan and the United States were less affected by massive rises in unemployment. There, the growth deceleration was reflected to a much larger extent in a productivity slowdown which limited the erstwhile rapid expansion in real wages. In the United States, in particular, this slowdown was associated with a substantial increase in the number of relatively low-paying and part-time jobs.

Much controversy surrounds the respective roles of demand and supply factors in the worsening performance. It would probably be fair to say that supply forces dominated the experience of the later 1970s. Thus, the climb in unemployment between 1975 and 1979 "should be attributed to the fact that real wages remained above market-clearing levels in most economies" (Bruno and Sachs 1985, page 171). This explanation, however, breaks down through most of the 1980s, when profitability was restored to levels close to, or even above, those recorded in the early 1970s. It was now the continuing, indeed reinforced, tightness of policies that was primarily responsible for the semistagnation of much of the decade (Sachs

Table 2: UNEMPLOYMENT IN SELECTED OECD COUNTRIES
(In Percent Of The Labour Force*, 1960-88)

	1960	1973	1979	1988
Austria	2.4	1.0	2.1	3.6
Belgium	3.3	2.3	7.3	10.0
Canada	6.4	5.5	7.4	7.7
Denmark	1.9	0.9	6.0	7.2
Finland	1.4	2.3	5.9	4.5
France	1.1	2.6	5.9	10.0
Germany (FRG)	1.0	1.0	3.3	7.6
Italy	5.5	6.2	7.6	11.8
Japan	1.7	1.3	2.1	2.5
Netherlands	0.7	2.2	5.4	9.2
Spain	2.4	2.5	8.5	19.1
Sweden	1.7	2.5	2.1	1.6
United Kingdom	1.3	2.2	4.6	8.3
United States	5.4	4.8	5.8	5.4
Unweighted average	2.6	2.7	5.3	7.8

Source: *Historical Statistics* (various).
* The numbers are not strictly comparable across countries.

1983, Bruno 1986). Some indication of this tightness is provided in Table 3, which shows the sharp and widespread switch in the level of real interest rates and in structurally adjusted budget deficits that occurred at the turn of the 1980s.

While the two oil shocks, as well as the labour market and economic policy reactions of the period, can throw a good deal of light on the reasons for the slowdown in growth, they may not tell the whole story. Arguably, some longer-run forces stemming, paradoxically, from earlier successes may also have been at work (Boltho 1982a). In other words, a deceleration would almost certainly have occurred, although perhaps in much less drastic and sudden form, even if the oil shocks had not taken place.

Most of these forces had to do with the exhaustion of certain of the favourable condi-

Table 3: INDICATORS OF POLICY TIGHTNESS IN SELECTED OECD COUNTRIES
(1979 And 1988)

	Cyclically Adjusted Budget Balances[a]		Real Interest Rates[b]	
	1979	1988	1979	1988
Austria	-3.8	-2.2	3.7	4.6
Canada	-3.6	-3.7	0.2	6.5
France	-2.3	-1.0	-0.6	5.7
Germany (FRG)	-5.1	-1.1	3.1	4.5
Italy	-11.5	-10.6	-1.1	3.9
Japan	-5.3	2.0	4.6	3.9
Netherlands	-6.4	-3.6	4.7	4.4
Spain	-3.2	-2.4	--	--
Sweden	-4.0	1.7	2.4	--
United Kingdom	-6.1	-0.1	-1.2	2.6
United States	-1.1	-2.7	0.5	5.3
Unweighted average	-4.8	-2.2	1.5[c]	4.6[c]

Sources: IMF (1990b), OECD Data Bank.
[a] General government net lending in percent of current-price GDP.
[b] Government bond yields deflated by the GDP deflator.
[c] Excluding Spain and Sweden.

tions which had propelled growth in the previous two decades, particularly in Western Europe and Japan. According to some, the tempo of growth was bound to falter because of the gradual saturation of household demand for certain important durables, the production of which had acted as an engine of growth (Mazier et al. 1984). Others lay more stress on the shrinking technological gap between the United States and the rest of the OECD nations, the dwindling scope for transferring labour from agriculture to industry (Lindbeck 1983), or the continuing shift of labour away from industry and toward services.

Yet, the most important single factor which almost inevitably would have fostered deceleration is to be found in the great success of the 1950s and 1960s: the creation of conditions of virtual full employment in the OECD as a whole. This achievement, together "with a diminished supply elasticity of agricultural or foreign workers to the urban sectors of the European economies, was bound to lead, in conditions in which the growth tempo had not slackened, to a strengthening of labour power and to a shift in income distribution away from capital" (Boltho 1982a, page 24). The strengthening of labour is illustrated, for instance, by growing unionization, the strikes of the late 1960s in all the major European economies and the spread of legislation in the early 1970s, inspired by trade unions, to protect employment (Bernabè 1982). The shift of income away from profits is well documented in OECD publications (Hill 1979).

These trends were more pronounced in Europe and Japan than they were in North America. Yet, a worsening in the growth climate had also occurred in the United States in the wake of the expansionary stance of the late 1960s that had been partly induced by the Vietnam conflict. The inflationary consequences of this stance strongly contributed to the breakdown in the early 1970s of the international monetary system created at Bretton Woods. Already well before the oil price shocks, when the discipline of fixed exchange rates had disappeared, simultaneous reflation in many countries had set the world onto a path of dangerously accelerating inflation. The shocks acted as detonators of a crisis, but the underlying deterioration in performance had made some slowdown inevitable.

Eastern Europe

Eastern Europe's growth experience exhibited both similarities and differences with that of the developed market economies. At an aggregate level, the extent of the break in the 1970s and 1980s seems almost identical, particularly if the Soviet Union is excluded from the analysis (see Table 1, page 3). However, the timing of the slowdown differed. While the OECD countries saw their growth tempo interrupted very suddenly by the two oil shocks, the deceleration in most of the erstwhile centrally planned economies occurred more gradually, usually in the second half of the 1970s and, again, in the second half of the 1980s.

A less pronounced reaction to the oil shocks should have been expected given the institutional framework of these economies (Portes 1980). Many of the factors which were so disruptive in the West were either absent or muted in the East. Thus, in principle the centrally planned economies should not have been affected by short-term inflationary or deflationary impulses like those experienced in the market economies, since domestic prices were rigidly controlled and planners could make certain that aggregate demand was always set at, or even above, full employment levels. Given the lack of these initial unfavourable effects, there should have been little need for the short-run aggressive wage bargaining and the medium-term restrictive policy reactions which took place in the OECD countries.

It is true that the impact of the changes in the terms of trade on domestic absorption could not be avoided. However, for two Eastern countries, Poland and the Soviet Union, the changes were actually positive, given the significant level of the net energy exports of these nations. As for the other economies of Eastern Europe, the unfavourable effects should have been felt much more slowly and gradually than they were in the West, thanks to the practice of applying a five-year moving average of world prices to transactions among the countries of the Council for Mutual Economic Assistance. Finally, in so far as oil and other commodities were bought from the West, the ample scope for borrowing on world capital markets that became manifest in the 1970s should have permitted continued imports of needed raw materials, investment goods and technology, thus facilitating, at least initially, the maintenance of rapid growth, as turned out to be the case in many developing countries through the later 1970s.

Despite all this, economic performance sharply worsened. Though most of the five-year plans for the second half of the 1970s incorporated a slowdown, actual performance usually fell short even of this unambitious target. While the immediate impact of the shocks was modest, the longer-term influences were severe. For instance, the deteriorations in the terms of trade suffered by several countries in the East eventually became larger than those incurred in Western Europe. Greater dependence on imported energy was one reason. Another seems to have been an inability to raise the prices of exports to the free-market countries because the economic downturn and protectionist pressures in Western Europe were limiting the demand for the goods of the nations of the Council for Mutual Economic Assistance. By the 1980s these problems were being compounded by the debt crisis, which forced most Eastern European countries into various degrees of austerity.

Yet, however serious these problems, it is unlikely that, on their own, the oil shocks and attendant difficulties were behind the drop of one-half, or worse, in the growth rate. Hence, even more than for that in the market economies, explanations for the deceleration in Eastern Europe must also be sought in other forces, either operating during the period, or stemming from earlier successes.

Bad weather had some influence on agriculture in several countries in the later 1970s. More importantly, the step-up in investment in the earlier years of that decade must have led to more bottlenecks and more unfinished projects than usual (Marer 1981), as well as to an understandable slackening in the investment effort (Alton 1981). More generally, incremental capital-output ratios rose everywhere in the East in the wake of lengthening "gestation" periods, falling capacity utilization rates and an ageing capital stock (Benini 1990). The most dramatic case of slowdown, Poland, owes much to the loss by planners of control over investment and incomes in the mid-1970s, a period of accelerated and ultimately unsustainable growth (Fallenbuchl 1981).

Yet, as in Western Europe, some of the slowdown was almost certainly inevitable, since it reflected the exhaustion of the permissive supply conditions which had fuelled growth in the 1950s and the 1960s. Indeed, the importance of this factor is probably greater for the planned economies than it is for the market economies, because the former relied much more heavily than did the latter on continuously rising inputs of labour and capital to achieve high growth rates in output. But labour reserves in agriculture dwindled; population growth faltered; participation rates rose to record levels, and political constraints made it increasingly difficult to sacrifice consumption in favour of investment. Some slowdown in the pattern of so-called "extensive" growth therefore seemed inevitable.

This inevitability of the slowdown was almost certainly reinforced by the "systemic" difficulties which were hampering the advance of productivity. According to one view, productivity growth decelerated from the mid-1970s onward as the Soviet Union and probably also other economies in the East reached an "equilibrium" technological gap with the West (Gomulka 1986). Until the early 1970s, catching up through imports of technology had been possible; hence, growth had been relatively rapid. Thereafter, however, and despite a continuously wide productivity differential, the static inefficiencies of the system impeded any further closing of the technological gap.

Alternatively, or in addition, systemic problems were augmenting the economic deceleration through other channels. Thus, rigid central planning and even half-hearted attempts at reform were increasingly unable to speed up the rate of innovation and technological progress. In the relatively simple economies of the 1950s and 1960s the centralized command structure had been able to deliver significant gains in basic living standards. When the scale and sophistication of the economies advanced, the well-known informational and incentive difficulties of central planning may have swelled exponentially. As complexity rose, the steadily more cumbersome planning machinery could no longer keep pace, and growth fell off.

Many of these difficulties were well known to the policymakers. Yet, little was done to improve matters. Hungary hesitated on the brink of a market economy for nearly two decades; Czechoslovakia and the Soviet Union, if anything, recentralized their economies after some timid reforms in the later 1960s; the GDR and Rumania stuck to a basically Stalinist model throughout.

Overview

The preceding few pages suggest that a slowdown in the rapid tempo of growth that had been established during the 1950s and 1960s was inevitable in both the market and the centrally planned economies. Structural changes were at work, weakening some of the factors which had propelled Europe and Japan after the war, particularly the heretofore ample supply of low-cost labour in the countryside. Many Western countries were also exhausting the stock of abundant, low-cost American technology as their industries reached best-practice levels of productivity, and part of this effect may have been at work in Eastern Europe, too.

Yet, such forces can explain neither the relative suddenness nor the severity of the crisis which set in during the mid-1970s. The suddenness in the West clearly arose because of the two very disruptive oil price shocks. In the East the direct and indirect effects of the oil shocks were less severe, at least in the 1970s, thanks to the partial insulation provided by central planning and massive external borrowing. However, other special factors, differing from country to country, brought about sudden interruptions in the growth process there.

On the other hand, the severity of the crisis was rooted in both systemic problems and policy responses. In the West the systemic feature which most influenced the period was the persistence of high and climbing inflation. Generated when the power of trade unions and other pressure groups had been thriving thanks to continuous growth and full employment, this inflation was given further impetus by the spiral in commodity prices and was only broken after years of slow expansion and soaring unemployment. Arguably, something similar was also at work in the East. Just as full employment in the market economies had meant that dismissals ceased "to play their role as a disciplinary measure" (Kalecki 1971, page 140), so, too, at least in the Soviet Union, labour shortages had "reduced the manager's ability to discipline workers or his willingness to discharge loafers" (Levine 1982, page 165). In the one case the main consequence was higher inflation, in the other slackening productivity growth. More importantly, however, the mounting problems in the Eastern countries were directly linked to the shrinking capacity of the planning system to cope with the demands of ever more sophisticated economies. This in turn generated rising waste and inefficiencies.

In neither case did policies help ease the problem. Indeed, they may have worsened it, in the one set of countries because of too much activism, in the other because of too much inertia. In the West, while some dose of deflation was inevitable, the sharp monetary and fiscal squeeze of the 1980s appears to have been an exaggerated reaction, which, in addition to slowing growth, precipitated the debt crisis in the Third World and exacerbated unemployment in the OECD without doing much to reduce inflation (Beckerman and Jenkinson 1986). In the East, on the other hand, the policy mistake was to cling far too long, until the very end of the decade, to outdated planning methods. The attempts at reform were few, piecemeal and timid. By creating uncertainty, they may well have encouraged additional inefficiencies.

III. PUBLIC EXPENDITURE AND TAXATION

Characteristic of the "golden age" was steady and extraordinarily wideranging public-sector expansion throughout Europe, Japan and North America. In the erstwhile centrally planned economies the enlargement came from a conscious attempt by policymakers to raise the welfare of the population by directly supplying a greater quantity of various social services. In the OECD it reflected a combination of buoyant tax revenues, which had been generated by brisk growth, and a relatively high income-elasticity of demand for nondefence public goods and traditional "merit" goods, as well as for a new form of "semimerit" good that could be called "security" (Boltho 1982b). Thus, transfer payments from the public sector to households, especially in the form of pensions, were one of the most rapidly swelling items in government spending.

The slowdown in overall growth over the last 15 years has perhaps been milder than might have been expected. The evidence presented in Table 4 shows, for instance, that in all the economies examined here the shares of total public expenditure in GDP, or those of public consumption in net material product, were higher in the late 1980s than they had been either just before the first oil shock, or at the turn of the 1970s.

Indeed, in some countries the increases have been especially remarkable. Italy, Japan and Spain, for instance, have recorded gains in the share of public expenditure in GDP since

Table 4: TRENDS IN PUBLIC EXPENDITURE
(1960-88)

Panel A: *Total Public Spending as a Percent of GDP*				
	1960	1973	1979	1988
Austria	35.7	41.3	48.9	50.6
Canada	28.6	35.4	39.0	44.4
France	34.6	38.3	45.0	50.3
Germany (FRG)	32.4	41.5	47.6	46.6
Italy	30.1	37.8	45.5	50.8
Japan	17.5	22.4	31.6	32.9
Netherlands	33.7	45.8	55.8	57.9
Spain	18.7[a]	23.0	30.5	41.1
Sweden	31.0	44.7	60.7	59.6
United Kingdom	32.3	40.4	42.6	40.7
United States	27.0	30.6	31.7	36.3
Western Europe	31.5	38.5	45.2	47.9
Total OECD	28.0	32.9	38.0	40.2
Panel B: *Total Public Consumption as a Percent of Net Material Product*				
	1960	1973	1980	1988
Bulgaria	3.3	3.6	3.8	5.8
Czechoslovakia	17.8	19.1	20.2	25.8
Germany (GDR)	13.1	15.0	15.8	16.1
Hungary	--	9.0	10.6	11.9
Poland	7.7	10.2	12.4	11.4
Rumania	--	--	6.8	6.7[b]
Soviet Union	7.4	8.9	10.5	11.7
Eastern Europe[c]	11.4	12.7	13.9	15.2
Eastern Europe/Soviet Union[c]	8.2	9.7	11.3	12.5

Sources: *Historical Statistics* (various), OECD (1990), *Comecon Data* (various).
[a] 1964.
[b] 1986.
[c] Excluding Rumania.

1973 that are a multiple of those achieved between 1960 and 1973. In Eastern Europe, if the figures are to be believed, Czechoslovakia has registered an even more impressive performance, despite the fact that it had by far the highest initial share of public consumption in net material product.

The OECD Countries

That the deceleration in public expenditure growth was lower than the deceleration in output growth is perhaps most surprising in the case of the developed market economies. In these countries public expenditure should have been influenced not only by the consequences of the less buoyant economy, but also by important changes in the conduct of policies. At a macroeconomic level, the fight against inflation led to greater stringency in fiscal policy almost everywhere (see earlier); at a microeconomic level, a widespread concern with the alleged disincentive and misallocation effects of excessive government spending and taxation generated strong pressures in favour of cuts, as well as reorientations, in expenditure flows.

It seems clear from the data that these pressures were operative only, if at all, in the 1980s. Between 1973 and 1979, only six years, the share of public expenditure in GDP in the OECD as a whole and in the sample of countries considered here rose by virtually the same amount by which it had risen over the preceding 13 years. On the other hand, developments in the 1980s were more subdued, and several countries were successful in their efforts to bring spending under some sort of control. Indeed, in a few countries, such as Germany, Sweden and the United Kingdom, the share of expenditure in GDP actually declined in the later part of the decade, while in most others it tended to stabilize.

However, such aggregate developments were influenced by a host of factors besides the policy stance, including cyclical swings in activity and relative price movements. More importantly, in the present context, these developments reveal very little about those items of expenditure that most impinge on household welfare, particularly social security transfers and expenditure on merit goods. Evidence for these items is presented in Tables 5 and 6.

As to social security benefits and social assistance grants, the overall impression, for the average of• the countries considered here, seems to confirm what was seen for the aggregate share of expenditure in GDP: the relatively rapid growth of the later 1970s gave way to a marked slowdown during the course of the 1980s.

Yet, care must be taken in interpreting these trends, at least in the European context;

Table 5: PUBLIC TRANSFERS TO HOUSEHOLDS IN SELECTED OECD COUNTRIES*
(In Percent Of GDP At Constant Prices, 1960-88)

	1960	1973	1979	1988
Austria	9.6	12.5	15.8	16.7
Canada	7.3	9.0	10.1	11.9
France	9.4	13.3	17.3	20.3
Germany (FRG)	10.4	12.1	15.3	15.1
Italy	8.6	12.9	14.1	17.9
Japan	4.7	6.0	10.6	12.0
Netherlands	(6.7)	18.7	24.8	25.1
Spain	2.6	8.2	12.7	14.8
Sweden	7.1	11.9	18.0	19.3
United Kingdom	5.6	7.6	9.8	11.2
United States	4.6	8.1	9.3	9.6
Unweighted average	7.0	10.9	14.3	15.8

Source: *National Accounts of OECD Countries* (various).
* Social security benefits and social assistance grants deflated by the private consumption expenditure deflator.

a significant portion of the recorded increases merely reflects automatic effects. Thus, one major item of transfer expenditure, unemployment benefits, soared in the 1980s in the wake of the sharp rise in the number of the jobless (see earlier). A very rough adjustment for this factor suggests that more than one-third of the 1.4 percentage-point gain in the GDP share between 1979 and 1988 for the average of the countries shown here may have been due to increases in unemployment compensation payments (as against less than 10 percent of the gain between 1973 and 1979). As a consequence, other transfer payments rose only very moderately, for example, in Austria, Spain and the United Kingdom, or even fell as a share of GDP, for example, in Germany and the Netherlands.

It is important to note that a shift seems to have occurred within these transfers between the early 1970s and the mid-1980s in the relative importance of pensions and family benefits. The share of the former continued to rise quite rapidly in several OECD countries, reflecting in part the gradual ageing of populations, while the share of the latter fell almost

Table 6: PUBLIC CURRENT EXPENDITURE ON MERIT GOODS IN SELECTED OECD COUNTRIES[a]
(In Percent Of GDP At Constant Prices, 1960-88)

	1960	1973	1979	1988
Austria	11.5[b]	10.5	11.9	11.5
France	--	--	--	10.8[c]
Germany (FRG)	--	10.8	11.9	11.7
Italy	--	9.3	8.7	8.9
Japan	--	5.1	5.5	5.5
Netherlands	6.1	6.2	6.4	5.7
Sweden	5.9[d]	14.8	17.6	15.8
United Kingdom	9.3	10.3	11.1	10.6
United States	5.3	7.0	6.9	6.4
Unweighted average[e]	--	9.2	10.0	9.5

Source: *National Accounts of OECD Countries* (various).
[a] Final consumption expenditure on education, health care, social security, welfare, housing and community amenities deflated by the government consumption expenditure deflator.
[b] 1964.
[c] 1986.
[d] 1963.
[e] Excluding France.

everywhere (Varley 1986). On a real per capita basis, child benefits dropped sharply in Spain and remained nearly stagnant in Italy, Sweden and the United States (ibidem). Of the countries examined here, only Germany and the United Kingdom showed a substantial rise; but in Britain, at least, this probably gave way to declines toward the end of the decade.

The conclusions for current expenditure on education, health care, welfare and housing are similarly unfavourable but even more clear. Following relatively rapid increases between 1973 and 1979, the growth of spending was sharply curtailed in the 1980s in most of the countries for which data are available, but especially in the two high-welfare economies, the Netherlands and Sweden. Only Japan and Italy were able to withstand the general trend. In the former case, however, the increase was toward a figure which was still well below average, while in the Italian case the rise in the 1980s did not fully offset the decline which had occurred in the second half of the 1970s.

The overall impression is unmistakable. In the 1980s the growth of transfer payments to households and expenditure on merit goods decelerated quite sharply. In the 1960s these programmes had been boosted due to demographic forces, expansions in entitlements and improvements in per capita benefits (OECD 1976a, 1976b, 1977). By the 1980s, with demographic considerations still requiring higher spending in most cases and unemployment raising that particular transfer component, the search for economy meant that policymakers had to opt for restrictions on benefits and a halt to extensions in coverage. Indeed, in some countries the privatization of certain government services and the voluntary withdrawal of citizens from public registers for the provision of merit goods were strongly encouraged.

While the growth of public expenditure slowed in the 1980s, both overall and for merit goods and transfers, this was much less the case for taxation. Total tax revenues as a percent of GDP rose as rapidly in the 1980s as they had in the 1970s and more rapidly than they had in the 1960s. This was an inevitable consequence of the priority given to the fight against budget deficits, at least outside the United States (Table 7). The phenomenon was particularly marked in the relatively low-tax countries (Italy, Japan and Spain), but tax pressures rose even in such very highly taxed economies as the Netherlands and Sweden.

Table 7: TOTAL TAX REVENUES IN SELECTED OECD COUNTRIES
(In Percent Of GDP At Constant Prices, 1965-88)

	1965	1973	1979	1988
Austria	34.7	37.1	41.0	41.9
Canada	25.4	30.8	30.6	34.0
France	34.5	35.0	40.2	44.4
Germany (FRG)	31.6	36.3	37.7	37.4
Italy	25.5	24.4	26.6	37.1
Japan	18.3	22.5	24.4	31.3
Netherlands	33.2	41.8	45.0	48.2
Spain	14.5	18.8	23.4	32.8
Sweden	35.4	41.6	49.5	55.3
United Kingdom	30.4	31.4	32.7	37.3
United States	25.9	28.7	29.0	29.8
Unweighted average	28.1	31.7	34.6	39.0

Source: *Revenue Statistics of OECD Member Countries* (various).

In this area, too, aggregate developments masked a trend which probably had important and unfavourable consequences on household welfare: the weight of various kinds of taxes was changed in the total tax take. The most notable shift, in some countries at least, was one away from broadly progressive income taxes to inevitably regressive indirect taxes (OECD 1989). The share of the latter in GDP had gradually decreased in the 1960s and 1970s, largely as a result of the lifting of tariff barriers in international trade. This pattern was reversed almost everywhere in the 1980s as domestic sales of goods and services became subject to higher tax rates. The shift was particularly marked in Spain, where a value-added tax system was adopted following that country's entry into the European Economic Community, but important changes in the respective weights of income taxes and indirect taxes also occurred in the Netherlands, Sweden and the United Kingdom, all of which had traditionally been endowed with a relatively progressive tax structure.

A better general impression of the possible regressive impact of trends in taxation may be gained by an examination not only of indirect taxes but also of social security contributions, the progressiveness of which is usually very limited. Table 8 shows a fairly mixed picture. Italy, in particular, but also Japan and Spain actually reduced the importance of regressive taxation relative to income taxes. At the other end of the spectrum, the Netherlands, the United Kingdom and the United States swung in the opposite direction on a massive scale, while Austria and Germany did so in a more moderate manner.

A further important change common to many OECD countries was a retreat from progressiveness in income-tax schedules. Between 1975 and 1988-9, 21 OECD countries cut their top marginal income-tax rate, and 12 raised their lowest marginal rate (OECD 1989), generating a much more compressed tax structure. In some countries the shifts were very pronounced, with the United Kingdom and the United States leading the way: their top marginal rates declined from 83 to 40 percent and from 70 to 28/33 percent, respectively. Fairly sharp downward changes also occurred in Canada, Italy and Japan.

In summary, despite continual increases in public expenditure, the combined effects of shifts in spending away from major social programmes and in tax policy toward a broadly regressive position meant that in the 1980s most OECD countries spurned or severely moderated the concept of the generous welfare state that had been current during the 1960s. This was most evident in the United Kingdom and the United States, but even Germany, the Netherlands and Sweden were affected. Elsewhere, the impact may not have been as intense, but no economy went against the tide.

Table 8: INDIRECT TAXES AND SOCIAL SECURITY CONTRIBUTIONS
(Selected OECD Countries, In Percent Of GDP At Constant Prices, 1965-88)

	1965	1973	1979	1988
Austria	21.6	23.0	25.6	27.1
Canada	11.9	13.0	13.3	14.7
France	25.0	25.7	29.8	32.3
Germany (FRG)	18.9	21.8	23.1	23.4
Italy	18.8	18.2	18.3	22.8
Japan	8.8	8.9	11.5	13.0
Netherlands	19.7	26.2	28.7	32.9
Spain	10.0	14.0	16.7	21.7
Sweden	15.3	18.7	25.2	27.3
United Kingdom	14.7	14.0	14.4	18.5
United States	9.9	11.6	12.2	13.8
Unweighted average	15.9	17.7	19.9	22.5

Source: *Revenue Statistics of OECD Member Countries* (various).

Eastern Europe

The developments in public expenditure in Eastern European are more difficult to document because of the imperfect nature of the available data. Table 4 (page 13) shows that the share of public consumption in net material product rose throughout the East both before and after the slowdown of the mid-1970s. Hence, on the surface at least, it would appear that, as in the market economies, the worsening overall economic performance was not reflected fully in collective consumption.

This impression is reinforced by the data assembled in Table 9, which presents tentative Western estimates of the share in GNP of government consumption, excluding defence, for the smaller Eastern European economies. While during the ten years up to 1975 this share had actually declined, largely because of the relative buoyancy of the growth in output, the subsequent period witnessed a widespread, if modest, recovery. The levels of public consumption suggested by the data are well below those in Western Europe, where

Table 9: PUBLIC NONDEFENCE EXPENDITURE IN SELECTED EAST EUROPEAN COUNTRIES
(In Percent Of GNP At Constant Prices, 1965-88)

	1965	1975	1980	1988
Bulgaria	10.3	9.8	11.9	12.4
Czechoslovakia	9.6	9.4	9.9	10.2
Germany (GDR)	12.5	11.2	11.3	12.6
Hungary	8.1	7.9	8.5	10.1
Poland	10.1	7.4	8.2	10.0
Unweighted average	10.1	9.1	10.0	11.1

Source: Alton (1981), (1989).

they reached around 17 percent, excluding the defence component, in the late 1980s for the sample of countries considered here. However, not too much should be read into such comparisons, given the shaky nature of the East European figures.

However, as in the case of the Western economies, such aggregate data may not throw much light on how household welfare managed during the period. Piecemeal evidence on budgetary expenditure for social welfare items suggests rising shares in net material product between the mid-1970s and the late 1980s for the GDR, Hungary and the Soviet Union, but declines in Poland and Rumania. None of this provides a very complete picture. A better impression is almost certainly available through an examination of more indirect indicators of the performance in housing, health care and education, the three main areas of social welfare that were controlled by the authorities.

In housing, any negative effect of the economic slowdown appears to have occurred with a relatively long time lag. During most of the 1970s residential construction was buoyant in the majority of the countries of the East, and the rate of housing construction per 1,000 population reached records everywhere outside the Soviet Union. Developments in the 1980s, however, were radically different. The construction of housing declined sharply in most countries, and the growth of investment in housing slumped, with only the Soviet Union able to go against the general trend (Table 10).

The slowdown in the growth of population and the reduced scope for migration from countryside to town can no doubt explain part of the drop in investment registered in most

Table 10: INDICATORS OF HOUSING ACTIVITY IN SELECTED EAST EUROPEAN COUNTRIES

Panel A: *Dwellings Constructed per 1,000 Inhabitants, 1961-87*

	1961-70	1971-5	1976-80	1981-7
Bulgaria	5.4	5.6	8.0	7.4
Czechoslovakia	6.2	8.4	8.6	6.0
Germany (GDR)	4.2	4.7	6.7	7.2
Hungary	6.0	8.4	8.5	6.6
Poland	5.5	6.8	7.5	5.1
Soviet Union	9.9	9.0	7.8	7.4
Unweighted average	6.2	7.2	7.9	6.6

Panel B: *Growth of Investment in Residential Construction, 1965-87**

	1965-70	1970-80	1980-7
Bulgaria	10.8	7.9	3.2
Czechoslovakia	11.4	2.6	-1.6
Germany (GDR)	13.1	9.0	2.0
Hungary	11.0	4.5	-2.8
Poland	7.6	7.1	-2.0
Soviet Union	6.9	3.0	6.8
Unweighted average	10.1	5.7	0.9

Source: *Economic Survey of Europe* (various).
* Average annual percentage changes.

of the smaller East European countries. Yet, the chronic shortages in and the poor quality of much of the housing stock suggest that needs remained significant. Though earlier investment still ensured a steady supply of new dwellings into the 1980s, the short- and medium-run prospects were clearly negative in an already serious situation (UNECE 1990).

The available quantitative indicators for the health sector, on the other hand, point to continuous advances in most of the erstwhile centrally planned economies. Thus, labour inputs rose through the 1970s and 1980s in all countries, bar Hungary, while investment, except in Czechoslovakia and the GDR, either climbed or remained constant (UNECE 1990).

Increases from 1975 onward were also recorded in the number of doctors and hospital beds per population, with the exception of the reasonably well-supplied GDR (ibidem). On the expenditure side, tentative Western estimates of the resources devoted to this sector suggest that the share of health care in GNP, after exhibiting broad stability between 1965 and 1975, rose from 3.1 to 3.7 percent between 1975 and 1985 in the five smaller Eastern European economies considered here (Eberstadt 1989).

Yet, such relatively flattering data masked deterioration in the health status of the population. It has been known for some time that in the Soviet Union, for instance, life expectancy at birth had been declining, in contrast to the experience almost everywhere else. A similar, if less pronounced, trend was also evident in the Eastern European countries (ibidem). The patterns in infant mortality were equally worrying. In more recent years the Soviet Union showed a worsening performance, while the continuous improvement in Eastern Europe fell short of that in the more advanced countries of Western Europe (ibidem).

While some of the reasons for these unfavourable developments may lie in inappropriate dietary patterns or the increased use of tobacco, part of the blame can almost certainly be ascribed to the health-care system, particularly "the mismatch [between the] labor-extensive, low-costs approach of the Soviet health model and the actual needs of the local population" (Eberstadt 1989, page 108). In all likelihood lower economic growth from the mid-1970s onward, while not directly responsible for a deterioration which clearly had earlier and deeper roots, also contributed.

Education probably suffered the least from the economic slowdown. Though investment decelerated in the 1980s, labour inputs continued to gain, as did some of the straightforward physical indicators of performance. Thus, all the countries in the East were able further to increase the percentage of children in preschool education; indeed, in the GDR nine of every ten children in the relevant age groups were enrolled in nursery schools by 1987. While some countries experienced a drop in the total number of people receiving education, this trend primarily reflected changing demographic pressures rather than the slackening of an effort which had always distinguished the centrally planned economies.

Overview

Statistical problems and institutional differences render comparisons very difficult in this domain. Many social services in the West are only partly provided by government and are financed through more or less progressive tax systems. All social services in the East were supplied directly by the state, and the financing was ensured by general budgets in which mildly progressive systems of household taxation played only a relatively minor role.

These differences notwithstanding, the marked and very similar slowdowns in economic growth in East and West inevitably had restrictive effects on the expansion of public spending and, in particular, on a number of items directly linked to household welfare. In the West, while unemployment transfer payments soared, expenditure on health care and education was curtailed, at times sharply. In the East it was mainly investment in housing that suffered, though there were also cutbacks in health care and education.

Interestingly, in both East and West the negative effects on the public expenditure for merit goods lagged somewhat. The initial impact of the recession was concentrated in investment or in material consumption. By the same token, it is likely that a certain amount of time will be required for overall economic recovery, when it comes (sooner in the West, later in the East), to restore the spending on health care, education, housing and transfers to households to the levels it might have reached in the absence of the deceleration in growth.

IV. HOUSEHOLD INCOMES

Household incomes swelled very rapidly in the 1950s and 1960s, indeed more rapidly than did total output. In addition, thanks to the attainment of full employment, the decline in the agricultural sector and the expansion of the welfare state, income inequalities were also reduced, at least in Western Europe.

"Despite a surprisingly stable pretax earnings structure," states Sawyer (1982, pages 216-17), "the distribution of posttax income has none the less changed toward greater equality in those European countries for which reasonably reliable data are available. Fairly pronounced changes have taken place in Italy, the United Kingdom and the Netherlands; more modest ones in France and Germany." Broadly similar conclusions hold for Japan, though not for North America (Sawyer 1976) and the Soviet Union (Braithwaite and Heleniak 1989), where the changes seem to have been rather small. In the United States over the 25-year period from 1947 to 1972, the lowest five deciles and the top decile lost ground to middle-income families in household income distribution. Meanwhile, between 1960 and 1975 there was a remarkable stability in Soviet income distribution statistics.

This picture changed after the mid-1970s. A slowdown in output growth in virtually every industrialized country, deteriorations in the terms of trade in most, and more restrictive fiscal policies, as well as rising unemployment, at least in the market economies, were bound to have severe negative effects on the growth of real disposable household incomes. The poor economic performance in the West was felt to be due, in part at least, to a shift away from profits, while in the East it may have sprung from outdated planning methods. New policies therefore aimed at restoring profitability, and reforms were intended to strengthen incentives and market forces. These were similarly bound to worsen income distribution.

The OECD Countries

For the Western countries covered here, the deceleration in the growth of household income was very sharp indeed, particularly if attention is focused on income obtained from employment and self-employment rather than that from rent, interest and dividend receipts. The aggregate data presented in Table 11 suggest that, unlike the trends in the 1960s, growth in this category of household income, for the average of the countries considered here, was below that of total output from 1973 onward and had declined to not much more than 1 percent per annum by the 1980s; indeed, in the Netherlands and Spain it had turned negative, while in Italy and Sweden it was close to zero.

The proximate reasons for this marked deceleration are illustrated in Table 11, Panel B, which divides the overall slowdown in the growth of real disposable incomes into four main "effects". The first, the deceleration in output growth, is self-explanatory. The second, the income distribution effect, measures the difference between the growth rate of total output and that of primary household income (excluding income from property), both deflated by the GDP deflator. It thus provides some idea of the shift from labour income toward corporate profits and income from capital generally. The third, the relative price effect, measures the impact on real household incomes of differences in the behaviour of the GDP deflator and the private consumption deflator and is therefore influenced by shifts in the terms of trade. The fourth, the policy effect, measures the impact of taxes and transfers in modifying, favourably or unfavourably, the growth of primary real household incomes.

By far the main reason for the slowdown in the 1970s was the abrupt skid in the output growth rate in the OECD. Indeed, had income not continued to shift massively away from profits, household welfare would have suffered a good deal more. The poorer position

Table 11: FROM GDP TO DISPOSABLE HOUSEHOLD INCOME IN SELECTED OECD COUNTRIES[a]
(Average Annual Percentage Changes Across 11 Countries, 1960-88)

Panel A: *Levels*

	1960-73	1973-88	1973-9	1979-88
Real GDP	5.3	2.5	2.7	2.3
Primary household income[b]	5.6	2.1	3.0	1.5
Primary household income[c]	6.1	2.0	3.1	1.3
Disposable household income	5.8	2.0	3.1	1.2

Panel B: *Changes*

	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-2.7	-1.9
Due to:		
Deceleration in output growth	-2.6	-0.4
Income distribution effect	0.0	-1.1
Relative price effect	-0.4	-0.3
Policy effect	0.3	-0.1

Source: *National Accounts of OECD Countries* (various).
[a] Primary household income is here defined as employee compensation and entrepreneurial income; it therefore excludes property income. Disposable household income is equal to primary household income, plus social security benefits and social assistance grants and minus direct taxes and social security contributions.
[b] Deflated by the GDP deflator.
[c] Deflated by the private consumption expenditure deflator.

in the terms of trade also added to the squeeze on personal incomes, while tax and social security policies made a small countervailing contribution.

In the 1980s, on the other hand, the further slowdown in GDP growth had only a relatively small impact, with the bulk of the deceleration in household receipts now accounted for by a very large movement in income distribution away from mainly labour income and toward profits. Relative price shifts continued to work against households, although to a lesser extent than earlier. Finally, the tightening of policies also made a small but negative contribution to the growth of real disposable incomes.

Of course, these are only average trends; they hide diverging country experiences (see the Annex, page 34). In Japan, the United Kingdom and the United States output growth accelerated in the 1980s. Especially in Austria and Germany the terms of trade improved. Nor was the policy stance invariably restrictive; for instance, disposable household income rose faster than did primary income in France, Spain, Sweden and the United States. Yet, the shift in income distribution toward profits was nearly universal (the only major exception being Canada) and was particularly marked in all four of the smaller economies examined here.

While such aggregate trends can easily be illustrated thanks to the existence of timely and internationally comparable data, the same is no longer true of more detailed issues of income distribution, where the information is scanty, often dated and seldom consistent across time and hardly ever across space. The discussion below is therefore inevitably less complete and more tentative. In particular, it makes no attempt at intercountry comparisons.

Some of the evidence on trends in household income distribution is presented in summary form in Table 12. The very broad impression for the 1970s is that posttax income differentials may well have narrowed. This seems to have been the case in Germany, Italy and the United States and was probably also the case in France, Japan and Sweden. Such developments fall in line with the longer-run trends mentioned earlier. Thus, welfare states were still being expanded; tax policies remained broadly progressive, and unemployment had not yet risen very sharply.

On the other hand, the 1980s saw a striking movement in the opposite direction. This was most pronounced in the United Kingdom and the United States, the two countries in the forefront in spurning the more egalitarian principles of earlier decades, particularly in their newly found preference for regressive tax policies. But mounting unemployment (not all of which attracted unemployment compensation payments), the spread of part-time and low-paying jobs, aggregate-income shifts away from wages and toward corporate profits, as well as more restrictive fiscal policies, also led to greater income differentials elsewhere, particularly in the Netherlands. Even Sweden, which shows a very long-run trend toward greater equality, recorded some worsening (Olsson and Spånt 1991).

Eastern Europe

Not unlike Western countries, after the mid-1970s the erstwhile centrally planned economies of Eastern Europe experienced a slowdown in the growth of real household income greater

Table 12: TRENDS IN INCOME DISTRIBUTION IN SELECTED OECD COUNTRIES
(In Percentages[a], Mid-1970s To Mid-1980s)

	Quintile	Mid-1970s	Late 1970s	Mid-1980s
France[b]	Highest	43.6	42.4	43.0
	Lowest	5.3	6.1	5.9
	Ratio	8.2	7.0	7.3
Germany (FRG)[c]	Highest	44.8	39.5	38.7
	Lowest	6.9	7.9	6.8
	Ratio	6.5	5.0	5.2
Italy	Highest	46.4	40.4	42.2
	Lowest	5.2	7.4	6.9
	Ratio	8.9	5.5	6.1
Japan	Highest	37.8	38.0	38.6
	Lowest	8.3	8.8	8.0
	Ratio	4.6	4.3	4.8
Netherlands	Highest	37.1	37.0	38.3
	Lowest	8.5	8.1	6.9
	Ratio	4.4	4.6	5.6
Sweden	Highest	31.4	30.2	30.9
	Lowest	10.7	11.2	11.1
	Ratio	2.9	2.7	2.8
United Kingdom	Highest	38.0	39.0	42.0
	Lowest	6.6	6.5	6.1
	Ratio	5.8	6.0	6.9
United States	Highest	42.8	39.9	41.9
	Lowest	4.5	5.3	4.7
	Ratio	9.5	7.5	8.9

Sources: World Bank (various), Canceill and Villeneuve (1990), Colombino (1991), *Japan Statistical Yearbook* (various), Olsson and Spånt (1991), CSO (1990).
[a] The percentage of disposable household income going to the highest and lowest quintiles. The figures are not comparable across countries.
[b] Primary income in 1984 prices.
[c] Net income.

than the one in total output. Since the accounting categories are not the same, a breakdown similar to that presented for the OECD economies is not possible for Eastern Europe. The simpler picture outlined in Table 13 links Western estimates of GDP growth to Eastern estimates of the growth in real per capita incomes. However, the latter are not strictly comparable to the former and may involve exaggerations of the changes in individual economic welfare in so far as inflation (open and repressed) was usually undervalued in Eastern Europe and the Soviet Union.

Yet, it is unlikely that the data imperfections have masked the broad trends which were at work. The overall impression is not very different from that gleaned earlier for the OECD economies. While the growth of output on a per capita basis slowed by around two percentage points in the East as a whole between the pre-1973 and the post-1973 periods, the

Table 13: FROM GDP TO REAL PER CAPITA INCOMES IN SIX EAST EUROPEAN COUNTRIES
(Average Annual Percentage Changes, 1965-88)

		Levels		Changes
		1965-73	1973-88	1965-73 to 1973-88
Bulgaria	Real GDP per capita	4.0	1.7	-2.3
	Real income per capita	6.2	3.3	-2.9
Czechoslovakia	Real GDP per capita	3.1	1.3	-1.8
	Real income per capita	6.0	2.0	-4.0
Germany (GDR)	Real GDP per capita	3.1	2.5	-0.6
	Real income per capita	4.8	4.6	-0.2
Hungary	Real GDP per capita	3.0	1.6	-1.4
	Real income per capita	5.4	2.0	-3.4
Poland	Real GDP per capita	4.5	1.1	-3.4
	Real income per capita	6.5	2.5	-4.0
Soviet Union	Real GDP per capita	3.5	1.1	-2.4
	Real income per capita	5.4	2.7	-2.7
Unweighted average	Real GDP per capita	3.5	1.6	-1.9
	Real income per capita	5.7	2.8	-2.9

Sources: Maddison (1989), *Economic Survey of Europe* (various).

deceleration in per capita real income growth was nearly three percentage points. The need to maintain, or even step up, the continually high levels of defence expenditure and capital formation must have meant that the curb on absorption required to pay for the deteriorations in the terms of trade had to come primarily from cuts in private consumption.

Individual country experiences differed, of course. The most severe squeeze in living standards in absolute and relative (to GDP) terms was imposed in Czechoslovakia, followed by Hungary and Poland. Real incomes in the GDR, on the other hand, appear to have weathered the slowdown almost unscathed, although the accuracy of East German data is more suspect than is that of the data of most other countries in Eastern Europe.

Assessments of what happened to the distribution of these much more slowly growing incomes are fraught with even greater difficulties in the East than they are in the West. Although survey data on earnings are available, information on household distribution is extremely scanty. In addition, even more so than in the West, the data can be very unreliable as indicators of household or individual welfare. In economies in which the supply of consumer products is often insufficient to meet demand, so that rationing becomes a standard allocating mechanism, "money income ceases to be the sole determinant of [the] capacity to acquire goods; to a degree, fortitude in searching out supplies and standing in queues and plain luck become consequential" (Bergson 1984, page 1,058). The difficulties of drawing strong conclusions from the data are compounded by the existence of special privileges for some members of society, in the form, for instance, of access to restricted shops or special allocations of housing and particularly desirable services, such as foreign travel.

Comparisons across countries, very hazardous at the best of times even in the OECD, are thus virtually impossible in this instance. However, trends over time may be less open to distortions. Some of the scanty available evidence is summarized in Table 14. The general impression is that differentials narrowed somewhat between the second half of the 1970s and the early 1980s, only to open up again later, although for the Soviet Union other statistics show a move in the opposite direction. And piecemeal evidence suggests that poverty may have increased between the late 1970s and the late 1980s in Hungary and Poland, though not in Czechoslovakia (Cornia 1990).

Indeed, it is likely that the more recent movement toward increasing inequality may have been underestimated by the data. Thus, it appears from anecdotal evidence that the "black" economy and the phenomenon of workers taking second jobs had spread in the 1980s in a number of Eastern economies (for example, in Hungary) even before the recent attempts

Table 14: TRENDS IN INCOME DISTRIBUTION IN SELECTED EAST EUROPEAN COUNTRIES
(Mid-1970s to Late 1980s)

Panel A: *Earnings* (The Ratio of the Top Decile to the Bottom Decile)				
		Mid-1970s	Early 1980s	Late 1980s
Czechoslovakia		2.6	2.4	--
Hungary		2.6	2.6	3.1
Poland		3.1	2.5	2.8
Soviet Union		--	3.0	3.2
Panel B: *Household Incomes* (Percent Going to the Highest and Lowest Quintiles)				
		Mid-1970s	Early 1980s	Late 1980s
Hungary	Highest	32.3	32.3	34.7
	Lowest	10.8	11.3	10.5
	Ratio	3.0	2.9	3.3
Poland	Highest	36.9	--	39.2
	Lowest	9.0	--	6.5
	Ratio	4.1	--	6.0
Memorandum Item: Soviet Union (ratio of top to bottom decile)		4.2	4.2	3.4

Sources: Atkinson and Micklewright (1990), Braithwaite and Heleniak (1989).

at economic liberalization. Moreover, increasing supply difficulties must have made access to special shops an even greater privilege than it had been earlier.

Overview

As in growth and public expenditure, East and West exhibited a number of common trends in household incomes after the early 1970s, notwithstanding significant institutional differences. In both the market and the socialist economies the slowdown in growth generally had a significant negative impact on the rise in living standards. The growth of absorption had to be curtailed more than did that of output almost everywhere, and real household incomes in turn suffered more than did overall absorption.

The parallel also held in income differentials. As the size of the income pie became larger (but more slowly), the distribution of the slices changed in similar, less equitable ways in both East and West. During the 1970s, often under the influence of trends and earlier policies, the movement toward greater income equality had continued in many countries. The opposite seems to have been true in the 1980s. Almost everywhere, the data show widening income differentials, probably exacerbated by the widespread cutbacks in public expenditure on a number of merit goods. In the West much of this was due to deliberate policies designed to spurn the egalitarian aims implicit in the welfare state. In the East the goal was less clearly stated, but, in those countries which pursued economic reforms, some widening in differentials was accepted as an inevitable aspect of the process of "marketization".

V. CONCLUSIONS

One of the recurring themes of the foregoing account of major economic trends in the industrialized countries of East and West has been the surprising presence of many parallels through time. Despite vastly different institutional structures, the market economies and the erstwhile centrally planned economies experienced broadly similar macroeconomic, public-expenditure and income-distribution changes both in the boom years of the 1950s and 1960s and in the crisis years that followed 1973.

The growth rates of total output were unprecedented in both sets of countries after World War II. The rapid absorption of surplus agricultural labour by industry and the ample availability of new technologies were among the common factors in this success. Yet, policies must also have played a part. In the West their role was indirect; belief in the power of demand management and other policies to stabilize output and raise growth must have contributed to the high rates of investment that characterized the period. In the East planning turned out to be a relatively efficient mechanism for mobilizing resources in what were still backward economies. In both sets of countries governments wanted high growth and on the whole were able to achieve it.

Similar, too, were the broad social welfare aims which accompanied the growth process. Full employment was considered a priority in both East and West; the opportunities for collective consumption were greatly enlarged in market and socialist economies alike, and income distribution leaned toward balance under the combined influence of autonomous trends, such as urbanization and rising female participation rates, and policy initiatives, such as tax and transfer policies in the West, the compression of wage differentials in the East and much better access to education everywhere.

The oil shocks of the 1970s and the attendant world economic crisis interrupted this halcyon period. In the decade and a half that followed 1973 growth rates were roughly halved; the expansion of collective consumption was cut back, and income distribution patterns widened again under the influence of market forces (such as increasing unemployment in the West and the diffusion of "black" economies in the East) and policies (such as less progressiveness in the tax structure in the market economies and the beginnings of system reform in the planned ones).

However, the oil shocks were arguably no more than detonators. An explosion in the already unstable economic situation was probably inevitable anyway. This was most clear in the Eastern economies, in which the weaknesses of the centrally planned management system were becoming increasingly apparent. A slowdown in output growth would have come even in the absence of other disturbances. The problems in the West may have been less obvious to an expert at the beginning of the 1970s. Yet, the gradual acceleration of inflation through the 1960s boded ill for sustained growth. According to many observers, the achievements of the welfare state had also been sapping dynamism and flexibility.

The slowdown in growth eventually prompted a fairly radical policy reorientation. In the West this occurred throughout the 1980s. In many, if not all, of the Western countries the earlier objective of full employment was sacrificed in the fight against inflation; the growth of public expenditure was severely constrained; reforms often diminished the progressive nature of the tax system, and the trends in income distribution worsened almost universally. In the East, policies were much more timid, at least until the very end of the decade. But here, too, the consequences of slower growth, the needs of defence and the beginnings of more market-oriented reforms led to cutbacks in collective consumption, larger income differentials and a greater incidence of poverty.

In both sets of countries household economic welfare was bound to suffer. Some of this inevitability was the consequence of macroeconomic and systemic trends. However, policies exacerbated the situation more than necessary. This would seem to have been particularly true in the West, where the shift toward a newly found faith in market forces was at times quite radical. The indifference to rising unemployment and poverty levels, the cutbacks in some basic welfare provisions and the almost deliberate encouragement for greater inequality that characterized the policies of several OECD countries strongly suggest that the swing away from the achievements of the 1960s went too far. The policy switch in the East was much less deliberate. There, the major fault of planners and political leaders lay in the initial unwillingness to contemplate wholesale reform, an unwillingness which only worsened the situation and made future surgery that much more indispensable and painful.

Prospects for the future are, as always, clouded by political uncertainty, particularly in Eastern Europe. Barring major new shocks, however, the outlook for the OECD economies would seem mildly optimistic. The supply side has clearly been boosted by continuous technological progress and possibly by a few market-inspired reforms. Demand could become more buoyant now that policymakers are less concerned about the dangers of inflation. And there are encouraging signs that the obsession of the 1980s with cutting back government intervention is beginning to give way to a more balanced and caring attitude.

The picture for the Eastern countries is, unfortunately, much more grim. The postponement of reform for the best part of two decades has made painful shocks unavoidable. The dismantlement of central planning will almost certainly engender a very costly period of adjustment. Full employment, price stability and relative income equality, three of the ostensible achievements of the socialist economies, are bound to be jettisoned as efficiency, incentives and the rationality of prices are restored.

Of course, the former system only delivered a state of full employment that masked massive underemployment, an absence of inflation that hid substantial repressed inflation and a compression of income differentials that bypassed the privileges of the nomenklatura. For the bulk of the population, the loss of these "achievements" will nonetheless be painful. The instability which the new market economies are bound to experience can only, in the short- to medium-run at least, translate into falling living standards.

Over the longer term, the combination of reform and the advantages of an educated labour force will hopefully result in a substantial improvement in performance. This, allied with reasonable growth in the OECD countries, would mean that the picture could look much better by the end of the century. This would be especially true for household welfare if the increasing resources which the "peace dividend" is likely to provide were to be directed to those areas of public expenditure that were neglected, at times even grossly, from the mid-1970s to the late 1980s. Seen in a broader historical perspective, this difficult period could appear as merely a brief hiatus in the rising prosperity of the industrialized world.

ANNEX: FROM GDP TO DISPOSABLE HOUSEHOLD INCOME IN 11 OECD COUNTRIES*

(Average Annual Percentage Changes, 1960-88)

1. Austria

Panel A: *Levels*

	1960-73	1973-88	1973-9	1979-88
Real GDP	4.9	2.3	2.9	1.9
Primary household income[a]	5.7	2.6	4.6	1.3
Primary household income[b]	6.2	2.5	4.2	1.4
Disposable household income	5.7	2.5	4.2	1.3

Panel B: *Changes*

	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-1.5	-2.9
Due to:		
Deceleration in output growth	-2.0	-1.0
Income distribution effect	0.9	-2.3
Relative price effect	-0.9	0.5
Policy effect	0.5	-0.1

Source: *National Accounts of OECD Countries* (various).

* Primary household income is defined as employee compensation and entrepreneurial income; it therefore excludes property income. Disposable household income is equal to primary household income, plus social security benefits and social assistance grants and minus direct taxes and social security contributions.

[a] Deflated by the GDP deflator. [b] Deflated by the private consumption expenditure deflator.

2. CANADA

Panel A: *Levels*				
	1960-73	1973-88	1973-9	1979-88
Real GDP	5.4	3.6	4.2	3.2
Primary household income[a]	5.3	3.4	3.7	3.2
Primary household income[b]	6.0	3.2	4.2	2.6
Disposable household income	5.3	3.1	4.3	2.2

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-1.0	-2.1
Due to:		
Deceleration in output growth	-1.2	-1.0
Income distribution effect	-0.4	0.5
Relative price effect	-0.2	-1.1
Policy effect	0.8	-0.5

3. FRANCE

Panel A: *Levels*				
	1960-73	1973-88	1973-9	1979-88
Real GDP	5.4	2.3	2.8	1.9
Primary household income[a]	5.4	2.1	3.3	1.3
Primary household income[b]	5.6	2.0	3.3	1.2
Disposable household income	5.5	1.9	3.0	1.3

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-2.5	-1.7
Due to:		
Deceleration in output growth	-2.6	-0.9
Income distribution effect	0.5	-1.1
Relative price effect	-0.3	0.0
Policy effect	-0.1	0.3

4. GERMANY (FRG)

Panel A: *Levels*				
	1960-73	1973-88	1973-9	1979-88
Real GDP	4.4	1.9	2.3	1.7
Primary household income[a]	4.5	1.8	2.4	1.4
Primary household income[b]	5.4	1.9	2.5	1.5
Disposable household income	4.5	2.0	2.9	1.3

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-1.5	-1.6
Due to:		
Deceleration in output growth	-2.1	-0.7
Income distribution effect	-0.1	-0.3
Relative price effect	-0.7	0.0
Policy effect	1.3	-0.6

5. ITALY

Panel A: *Levels*				
	1961-73	1973-87	1973-9	1979-87
Real GDP	5.0	2.8	3.7	2.2
Primary household income[a]	4.6	1.5	2.5	0.8
Primary household income[b]	5.2	1.8	2.7	1.1
Disposable household income	5.3	1.4	2.6	0.5

Panel B: *Changes*		
	1961-73 to 1973-9	1973-9 to 1979-87
Deceleration in real disposable household income	-2.7	-2.1
Due to:		
Deceleration in output growth	-1.3	-1.5
Income distribution effect	-0.8	-0.2
Relative price effect	-0.3	0.1
Policy effect	-0.2	-0.5

6. JAPAN

Panel A: *Levels*				
	1960-73	1973-88	1973-9	1979-88
Real GDP	9.6	3.9	3.6	4.0
Primary household income[a]	9.9	3.8	4.3	3.5
Primary household income[b]	9.8	2.9	3.0	2.8
Disposable household income	9.4	2.9	3.4	2.6

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-6.0	-0.9
Due to:		
Deceleration in output growth	-6.0	0.4
Income distribution effect	0.5	-1.3
Relative price effect	-1.3	0.6
Policy effect	0.9	-0.7

7. NETHERLANDS

Panel A: *Levels*				
	1960-73	1973-88	1973-9	1979-88
Real GDP	4.8	1.8	2.7	1.3
Primary household income[a]	6.5	1.4	3.3	0.1
Primary household income[b]	7.5	1.3	3.4	-0.1
Disposable household income	7.8	1.7	4.6	-0.2

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-3.2	-4.8
Due to:		
Deceleration in output growth	-2.2	-1.4
Income distribution effect	-1.0	-1.8
Relative price effect	-0.9	-0.3
Policy effect	0.9	-1.4

8. SPAIN

Panel A: *Levels*				
	1960-73	1973-86	1973-9	1979-86
Real GDP	7.2	1.9	2.2	1.6
Primary household income[a]	8.9	1.4	3.5	-0.3
Primary household income[b]	9.3	1.3	3.7	-0.7
Disposable household income	9.4	1.1	3.1	-0.5

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-86
Deceleration in real disposable household income	-6.3	-3.6
Due to:		
Deceleration in output growth	-5.0	-0.6
Income distribution effect	-0.4	-3.1
Relative price effect	-0.3	-0.6
Policy effect	-0.7	0.8

9. SWEDEN

Panel A: *Levels*				
	1960-73	1973-88	1973-9	1979-88
Real GDP	4.1	2.0	1.8	2.1
Primary household income[a]	3.5	1.6	2.8	0.8
Primary household income[b]	3.7	1.4	3.0	0.4
Disposable household income	3.0	1.0	2.2	0.3

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-0.9	-1.9
Due to:		
Deceleration in output growth	-2.3	0.3
Income distribution effect	1.6	-2.3
Relative price effect	0.0	-0.6
Policy effect	-0.2	0.7

10. UNITED KINGDOM

Panel A: *Levels*				
	1960-73	1973-88	1973-9	1979-88
Real GDP	3.2	1.9	1.5	2.2
Primary household income[a]	3.5	1.2	0.9	1.4
Primary household income[b]	3.7	1.6	1.4	1.8
Disposable household income	3.4	1.8	1.7	1.8

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-1.6	0.1
Due to:		
Deceleration in output growth	-1.7	0.7
Income distribution effect	-0.8	-0.2
Relative price effect	0.2	0.0
Policy effect	0.7	-0.4

11. UNITED STATES

Panel A: *Levels*				
	1960-73	1973-88	1973-9	1979-88
Real GDP	4.0	2.7	2.4	2.8
Primary household income[a]	3.9	2.5	2.2	2.6
Primary household income[b]	4.4	2.3	2.3	2.2
Disposable household income	4.4	2.2	2.2	2.2

Panel B: *Changes*		
	1960-73 to 1973-9	1973-9 to 1979-88
Deceleration in real disposable household income	-2.2	0.0
Due to:		
Deceleration in output growth	-1.5	0.4
Income distribution effect	-0.2	0.0
Relative price effect	-0.3	-0.6
Policy effect	-0.2	0.1

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