Samuelson's forecast for 1974: the effects of the energy crisis

By John Moulder

1974 will definitely be a year of recession, according to Paul A. Samuelson, junior Professor of Economics.

In predicting the year of recession, Samuelson directly conflicted with most of the forecasts issued prior to October 1973, declaring that "none of these predictions made any big event of the 'energy crisis' stated Saunders.

He expressed these beliefs in a recent seminar on "The Energy Crisis and the State of the Economy," along with Lester C. Thurow, Professor of Management and Economics, and Paul W. MacAvoy, Professor of Management.

Samuelson foresees a 2½ percent drop in the Gross National Product (GNP) for the first two quarters of the year, with a rise of 2½ of one percent during the third quarter and a final deficit of 4½ of one percent for the year as a whole. He also predicted that a wise rate of inflation will be prevalent, with a rise in the consumer price index of 7 or 8 percent while unemployment reaches approximately 6½ percent by the end of the year.

"Most of the other forecasts showed a drop of the gross rate below four percent which is far for the long run," Samuelson said, "but those who predicted a recession or a definite decrease in growth were greatly in the minority."

Thurow limited himself to the "Energy Crisis" in general and termed it "a minor blip in the face of human events. The only way to look at the Energy Crisis properly is to see how much, in terms of human labor time, it has taken to produce one BTU of energy throughout history. If one were to plot this as a graph, one would see that the amount of labor needed has steadily decreased with new ideas, but small fluctuations."

"Now, in the 1950's the Persian Gulf oilfield was discovered," Thurow continued, "thus the only thing the embargo of Persian Oil has done is to put us back on the old trend line."

In response to this, Samuelson asked Thurow what he would consider major, "If this just throws us back to 1958 and we therefore don't bother ourselves with it, then what should we worry about? I would consider being thrown back to 1958 a major catastrophe of the modern economy."

Thurow said that New England will pay more than its fair share of the cost of the energy crisis and therefore we feel an initial bit of pain before fuel prices settle down. He emphasized that the real problem stems from large shifts in price and not from the actual price that one has to pay.

According to MacAvoy, the extent of the fuel shortage predicted for the first quarter of 1974 is decreasing hourly. "If one takes forecasts of shortages and plots them against their date of issue, one can see that there is a definite lessening of the number of forecasts we are supposed to be short. The June 1973 forecast predicted a shortage of 4 million barrels, while January of this year shows us missing only 1½ million. Extrapolating these points one might even get a small surplus."

MacAvoy presented four possible reasons for this behavior. According to him the Arab embargo is leaking out of the system. "We're getting a large amount of Arab oil from Canada and Venezuela. Also, up until recently we've been having temperatures like Florida used to have and Florida has been having weather like we normally do. This of course lessens demand."

MacAvoy said that we can live with the Energy Crisis but that it will require smaller cars, more insulation, better government regulation of the oil industry and more precise controls of import prices. This last measure was in reference to the possibility raised earlier of embargoes of Peruvian oil from the United States in order to make the production of synthetic oil economically feasible. As a result of such import restrictions being utilized worldwide, MacAvoy said that he could see the major effect of the Arab embargo as simply depriving the Arabs of the major portion of the world's oil trade.