in the rate of inflation in the U.S., real interest rates have remained at very high levels and threaten to abort recovery in industrial countries. American officials now seem of the view that a reasonably satisfactory recovery will not materialize in the U.S. unless interest rates go down. Such high rates of interest in the U.S. have also led to some distortion of exchange rates, particularly as regards the Japanese yen. Some easing of interest rates in the U.S. would improve the prospects for recovery not only in that country but also in the low-inflation countries, like Japan and Germany. In addition, it would afford more margin of manoeuver in other countries to reduce their own rates, although this would depend on the level of their respective inflation rates. Such developments would of course be beneficial to Canada and the world economy.

Generally, various weaknesses in the implementation of existing policies are seen as having reduced the impact of monetary restraint on prices and compounded the depressive effects on output and employment. Such weaknesses relate to insufficiently supportive fiscal policies, to the implementation of monetary restraint, per se, and to the failure to tackle rigidities and other structural problems.

Medium Term Outlook

To assess the medium-term implications of the current policy stance of industrial countries, and the consequences of relaxing that stance, a number of alternative scenarios for the mid- to late-1980s have been examined. Based on present non-accommodating policies industrial countries are expected to increase their average rate of growth to slightly more than 3 per cent over the 1984-86 period and at, the same time gradually reduce the average rate of inflation, measured in terms of GNE deflators, from its projected 1983 level of about 7 per cent to 5-5½ per cent by 1986. This outcome with respect to growth would bring rates in line with the average for the 1973-77 period (although significantly above the experience of the past two years). The implied average level of unemployment for 1986 would represent little improvement over the current level of about 7 per cent. As to the implications for developing countries, prospects generally show an improvement from assessments of last year. The financing of the implied current account deficits in the aggregate is considered feasible, although within the sub-groups of low income countries and "other" net oil importers individual cases of adjustment and financing difficulties are predicted.

In essence the above scenario would provide the basis for a return to non-inflationary growth in the industrial countries during the latter part of the decade with a marked decline in unemployment. Non-oil LDCs would have made progress in reducing their debt service burdens and would be in a position to expand their exports in the latter 1980s as world growth prospects improved. Alternatively should policy makers relax monetary restraint in the face of rising unemployment, or fail to develop fiscal policies and policies affecting the supply side that are consistent with restrictive monetary policies, prospects would