Risks of Stagflation in the European Economy in 2012 and 2013

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“Stagflation” was first used by Iain McLeod, a British politician, in a speech to the Parliament in 1965 and this word started to be popular. In 60th years the situations occurred, which the advocates of the traditional Keynesian theory could not explain. The correlation between inflation and unemployment in various countries did not develop as assumed by the Phillips curve. Instead of dropping as unemployment rose, prices did not even stagnate but kept rising, in some cases even accelerating their rise.

Stagflation in USA in the 70th years of last century

Main reasons:

Significant increase in regulatory steps in the years leading to the stagflation and increased number of state interventions in the economy, attempts to control prices and wages in the first stage of the stagflation, which did reduce inflation in the short run, but only intensified the inflationary pressures later.

The fading economic growth impulses caused by the previous engagement in the Vietnam war, dramatic scaling back of US presence in this conflict, and a vast reduction of war expenses.

Departure from the Gold Standard, and thus the creation of space for fundamental loosening of the government's monetary policy, loss of the currency's purchasing power against other currencies of business partners.

1969	1971/I	1971/VIII	1972	$80^{th}/90^{th}$
1$: 4DM	3,66DM	3,22DM	2,83DM	1,8DM

External price shocks caused by reduced supply of oil, and the ensuing demand pressure on prices.

Inconsistent economic policy of the US administration at the time, which mixed decentralisation efforts and planned economy approaches.

Restriction on trade through the introduction of import premiums, i.e. essentially the creation of customs barriers.

Rome, about 200 A.D.

Probable reasons:

**The number of regulatory interventions in the economy rose substantially;
free food market was curtailed through price controls in favour of some customers,
grain and subsequently other products were later distributed for free.**

People were deprived of the right to choose their occupation freely.

**The Empire reached the maximum of its expansion, which limited further income of the state budget, and the state was unable to respond by cutting costs.
Partly because it needed to finance its military,
partly due to the ever-increasing welfare costs.**

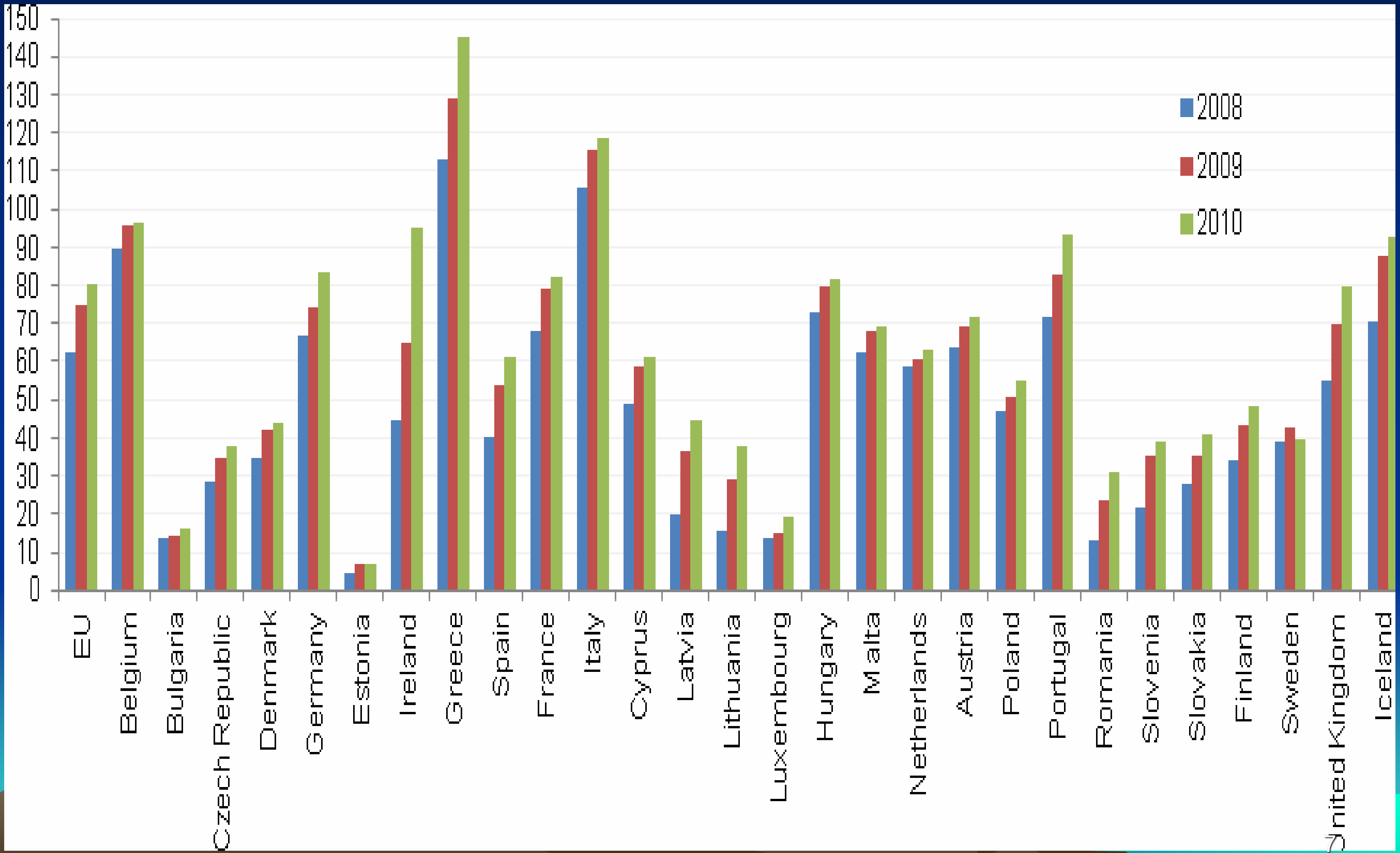
**The currency was stripped of its "golden" or "silver" standard,
i.e. depreciated by ever-increasing issues of new money that was not covered by goods.**

The economic policy witnessed substantial fluctuations, and the fluctuation cycles were getting shorter. In the times of the Republic and in the early Empire, the cycles of legible policies lasted for decades; they began to shrink dramatically from about 100 AD, and later the emperors ruled for single years, sometimes even months.
However, their economic concepts differed substantially.

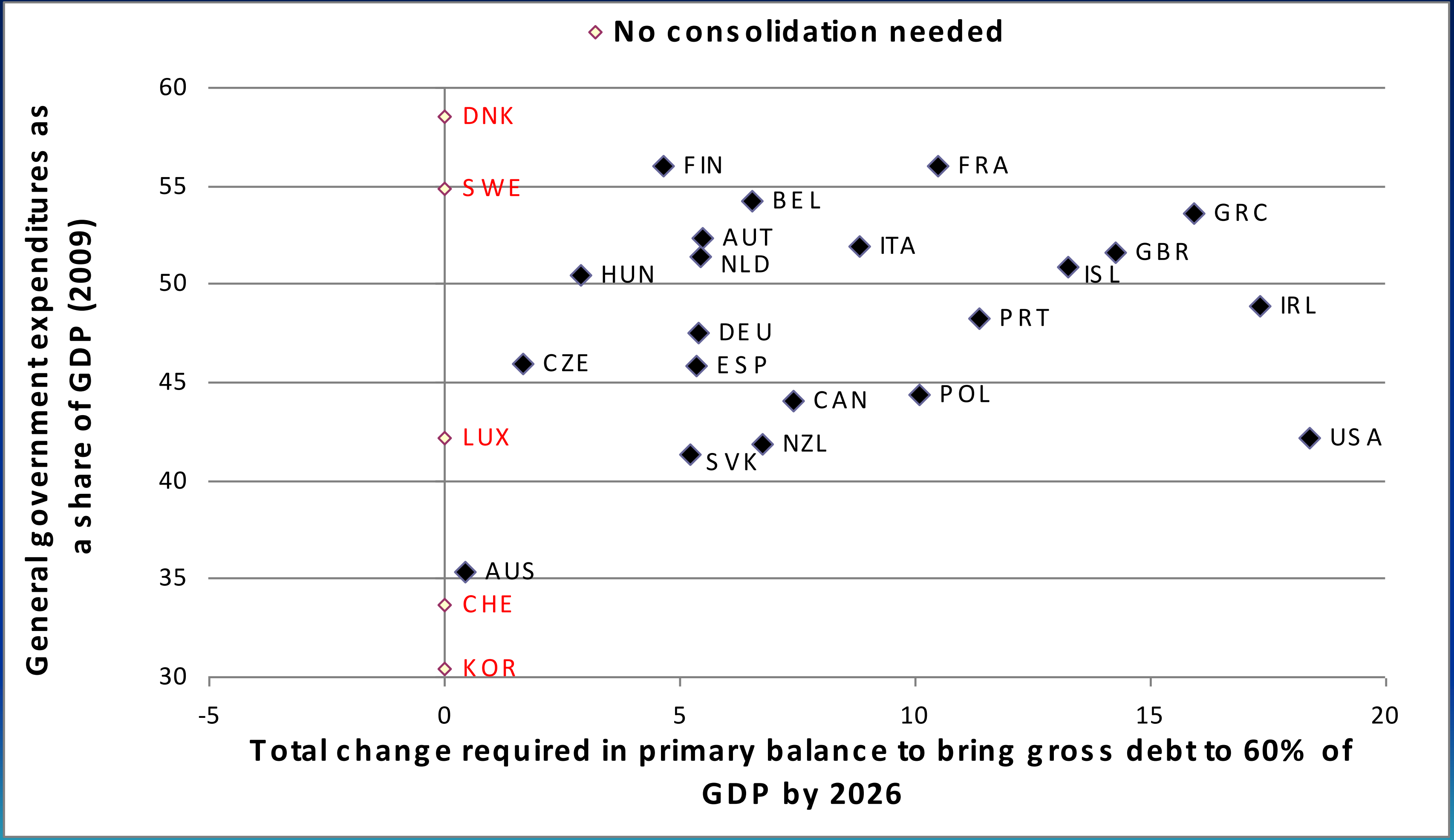
The Empire faced ever-increasing external pressure, to a large degree due to the increasing aggression in the border regions, but restricted trade, i.e. export of Rome's problems beyond the Empire, also played a role – the trade was curtailed, among other things, by the low quality of the currency and by various administrative barriers and customs measures.

General government gross debt [% GDP]

Source: EUROSTAT http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&plugin=1&language=en&pcode=tsieb090

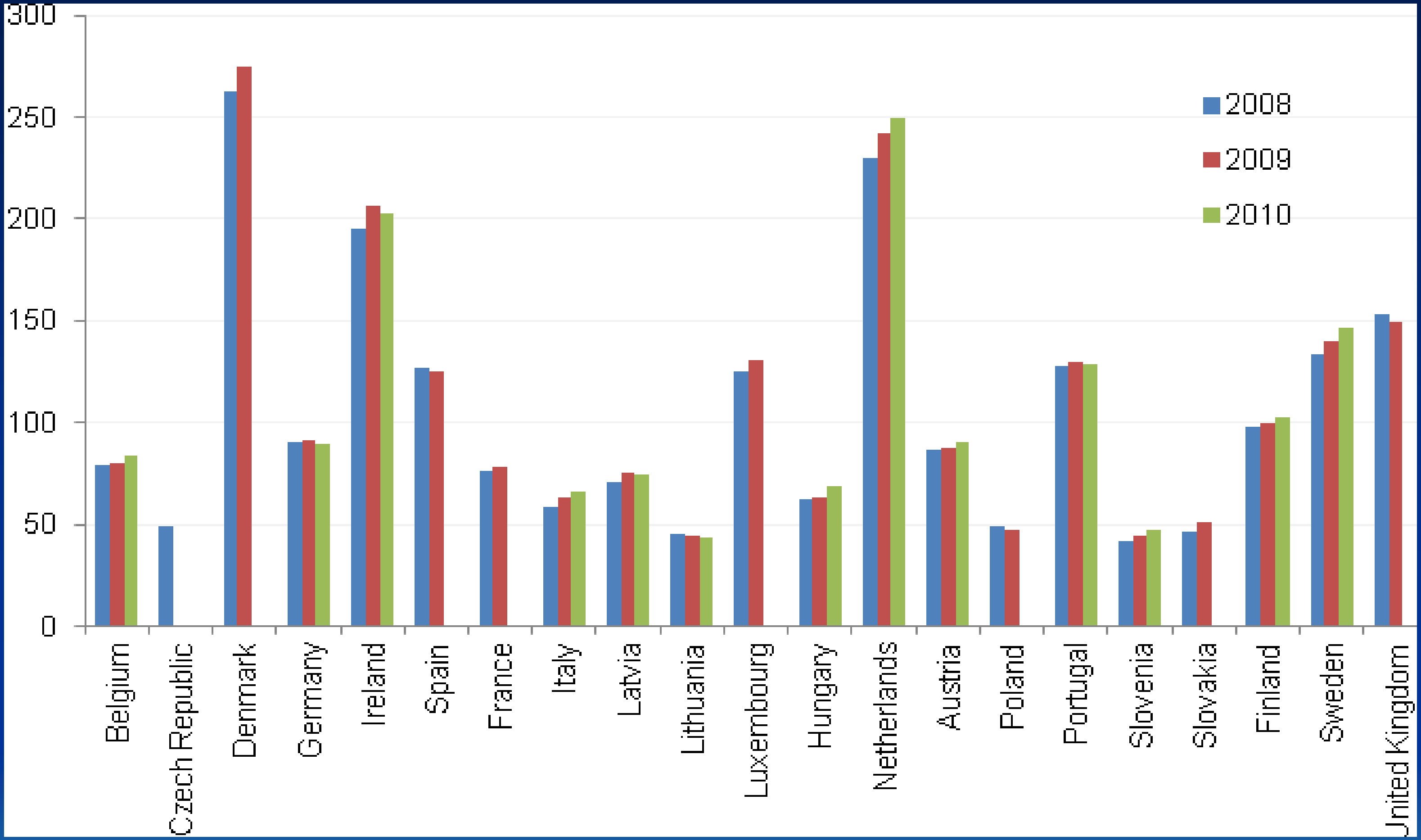


Fiscal consolidation requirements



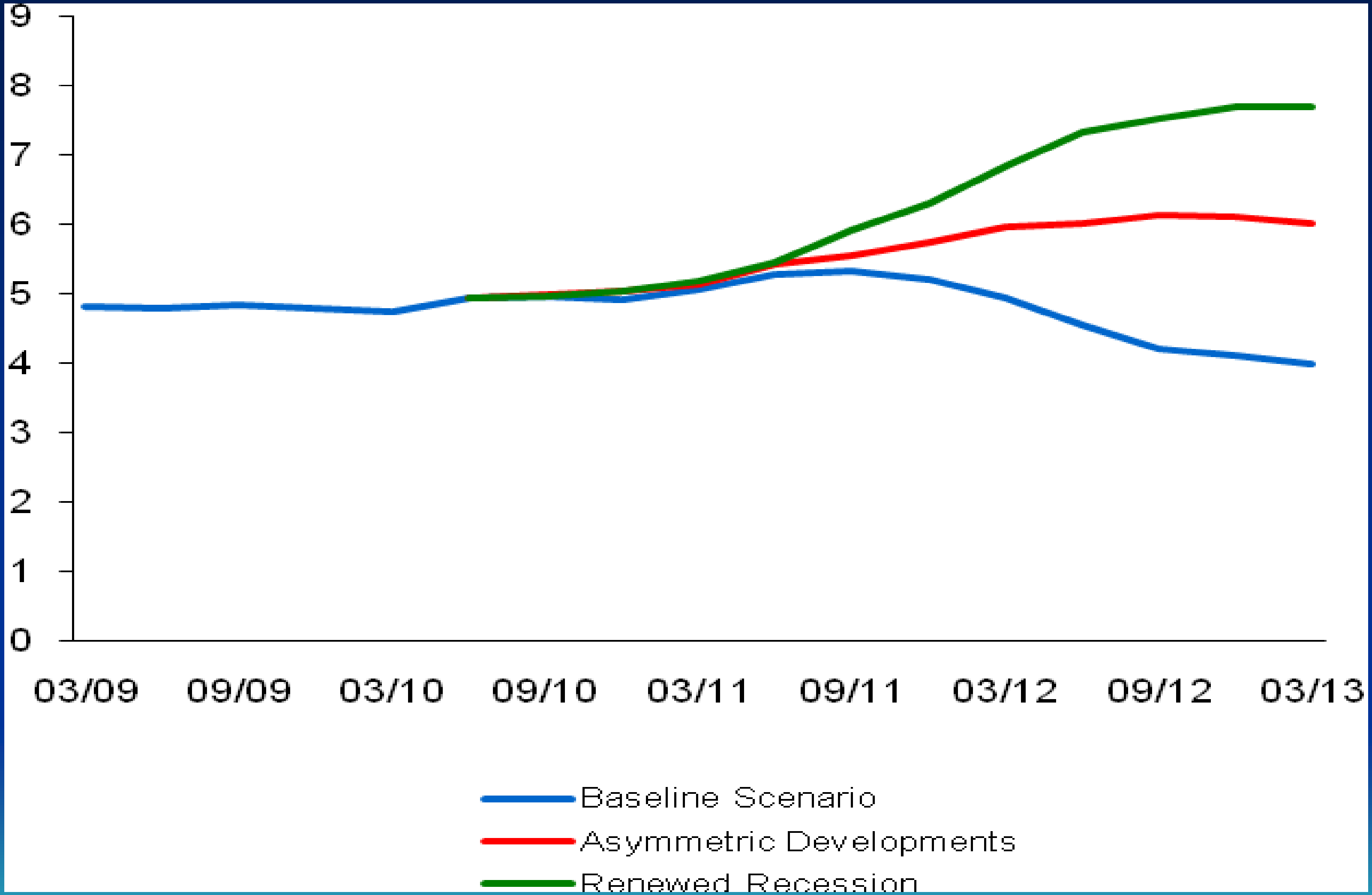
Source: OECD, Government at a Glance, 2011

Gross debt-to-income ratio of households [%]



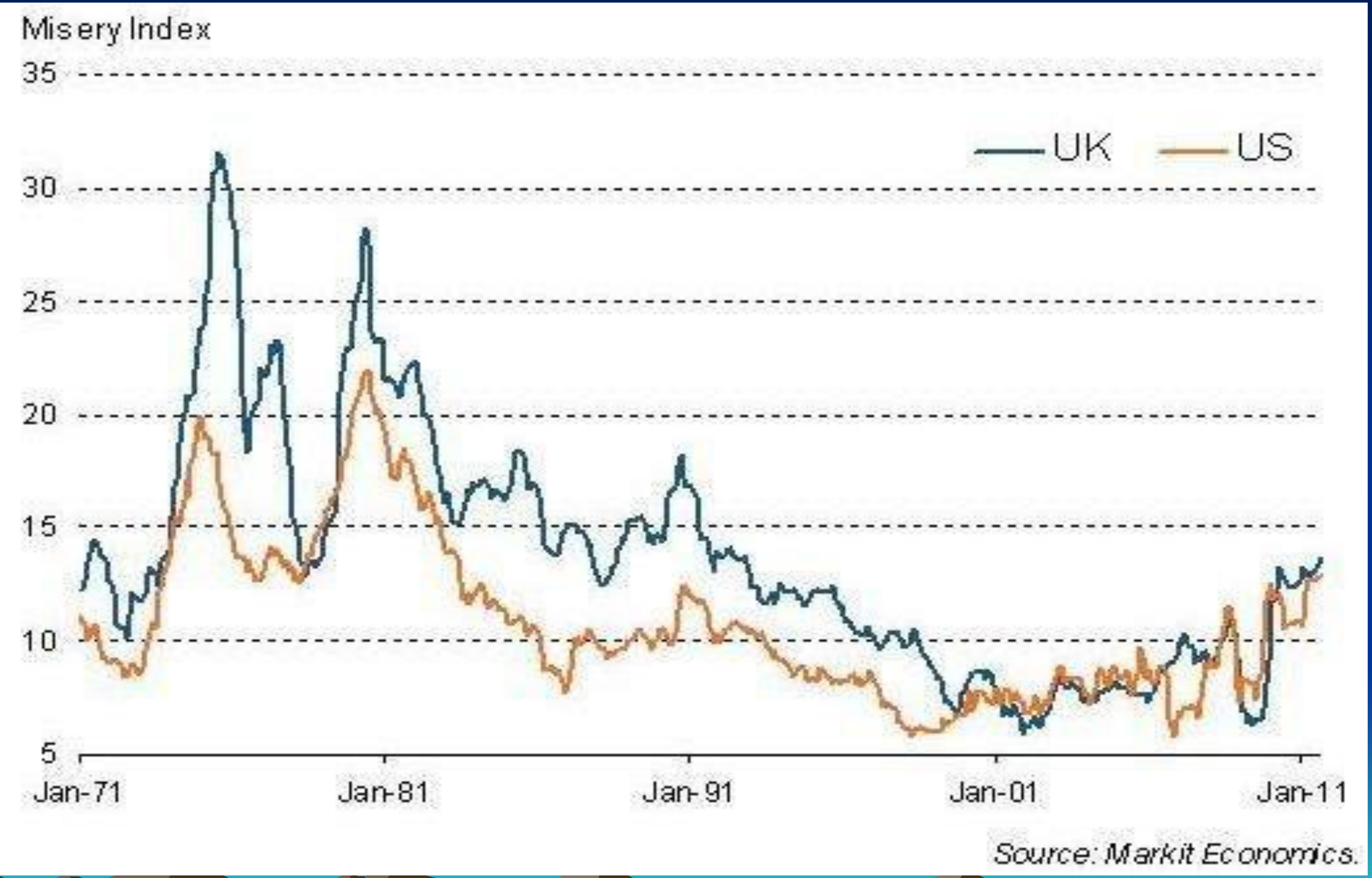
Source: EUROSTAT

12-month default rate on bank loans to households



Source: CNB Financial Stability Report 2010/2011,
http://www.cnb.cz/cs/financni_stabilita/zpravy_fs/fs_2010-2011/index.html

Misery index for the USA and the United Kingdom



Rate of Inflation, Unemployment and Misery Index in selected countries

	Inflation		Unemployment		Misery index	
	10/2010	09/2011	10/2010	09/2011	10/2010	09/2011
Euro 17	1.9	3.0	10.2	10.0	12.1	13.0
EU	2.3	3.3	9.7	9.5	12.0	12.8
Czech Republic	1.9	2.1	6.9	6.7	8.8	8.8
Germany	1.6	2.9	6.7	6.0	8.3	8.9
Greece	4.8	2.9	14.2	17.5	19.0	20.4
Spain	2.3	3.0	20.6	21.2	22.9	24.2
France	1.8	2.4	9.7	9.9	11.5	12.3
Italy	1.9	3.6	8.5	7.9	10.4	11.5
Hungary	4.0	3.7	11.1	10.3	15.1	14.0
Slovakia	1.0	4.4	14.2	13.4	15.2	17.8
United Kingdom	3.3	4.6	7.8	8.2	11.1	12.8

Source: Eurostat

Conclusion

It seems that we cannot support the notion that Europe as a whole is under a threat of stagflation.

Moreover, the rising inherence of the states in the economy may cause many complications that are now hard to predict.