

An Analytical Study of Stagflation: Between the Crisis of the Seventies and Economic Trends During the Ukrainian Crisis

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Abstract:

The continuation of the current stagflation depends on two key factors. First, the interaction between persistent labor market tightness, supply chain bottlenecks, and the nature of central banks' responses to high inflation rates through interest rate hikes, which they have adopted as a primary tool in combating inflation. Second, the duration of the Russian-Ukrainian crisis and its impact on energy prices, food supply, and global growth. It is worth noting that, based on past experiences, this inflationary surge is unlikely to last more than two years. However, this assessment may prove incorrect if unexpected crises arise.

Keywords: Stagflation, Ukrainian Crisis, COVID-19 Crisis, Energy Prices, Food Prices.

JEL Classification Codes: E01, E31, E21

1. INTRODUCTION:

Global inflation has sharply increased from low levels in the middle of the year, driven by a rebound in global demand, supply chain disruptions, and rising food and energy prices, particularly since the onset of the Russian-Ukrainian war.

Although forecasts suggest that inflation may decrease after reaching its peak in the current year, and that it may return to levels near those of 2019 by 2024, there are growing risks that it may remain high due to the ongoing global supply disruptions and the fading of some structural factors that had kept inflation in check over the past three decades. On the other hand, economic growth has moved in the opposite direction, sharply declining

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since the start of the year, and it is expected to remain below the average growth rate of 2010-2020 for the rest of the decade.

In light of these developments, there are risks that the global economy may head towards stagflation—a combination of rising inflation and slowing growth. This scenario bears a striking resemblance to the situation in the 1970s, which was a period of stagflation that caused significant harm to the global economy. The stagflation of that time led to substantial increases in interest rates to curb inflation, which resulted in a global recession and triggered a series of economic crises in developing and emerging market economies.

The following problem arises:

What is stagflation, and how might it manifest in the 2020s? Is it a repetition of the 1970s?

To address this, the following hypotheses are proposed:

- There is considerable debate surrounding the current stagflation, as the current rise in inflation could lead to sustained upward pressure on prices after two decades of low and stable inflation.

The similarity between the current cycle and the stagflation of the 1970s due to the negative effects of real interest rates and the

2. The Concept of Stagflation

1.2 Definition:

The concept of stagflation requires an understanding of inflation, recession, and unemployment. Inflation is defined as a continuous and sustained increase in the general price level, while recession is seen as a decline in aggregate demand that leads to a slowdown in the sale of goods and products in the market, resulting in a gradual reduction in profits,

workforce, and production units, as well as an accumulation of unsold goods and inventory. This leads to widespread issues in economic actors' ability to meet their financial obligations on time, ultimately resulting in the phenomena of bankruptcy and unemployment. (Ma'rouf, 2006, p. 30)

Unemployment is defined as the condition in which a number of people in society remain without work or a job, despite their earnest efforts to find employment. These individuals may either be unemployed altogether or engaged in jobs that consume only part of their time or energy. Unemployment can be categorized into different types, such as frictional, structural, and seasonal unemployment.

Once we have defined these three concepts, stagflation can be described as the coexistence of inflation—meaning the continuous rise in prices—with increasing unemployment. In other words, it is the condition where the number and rate of unemployed workers, who seek employment without success, rises. Stagflation can also be seen as a situation where high rates of inflation and unemployment exist simultaneously. Therefore, it can be defined as a scenario where continuous increases in the general price level occur alongside growing unemployment and declining levels of national output and growth rates over a specific period. (Osama , , 2003, p. 67)

2.2 Measuring Stagflation:

The process of measuring stagflation is done through a composite index adopted by economists, which consists of the sum of the inflation rate and the unemployment rate. The stagflation index can be expressed as follows: **Stagflation Index = Inflation Rate + Unemployment Rate**

Thus, some economists believe that a country's economy is experiencing stagflation if the stagflation index exceeds 8%, provided that both the inflation rate and the unemployment rate are increasing. However, despite this index being considered significant, the 8% threshold raises several issues. For example, the stagflation index may exceed this figure while only one of the inflation or unemployment rates stands at 4%. In this case, it cannot be concluded that the economy is experiencing stagflation.

Economists generally agree that if the stagflation index exceeds this threshold and both inflation and unemployment rates rise simultaneously, we can say that the economy is facing stagflation. A 4% unemployment rate is considered natural, likely reflecting frictional unemployment. Likewise, a 4% inflation rate does not necessarily indicate a level of inflation that poses a threat to the economy. Ultimately, the presence of stagflation in an economy depends on its ability to bear the pressures of inflation or the burden of unemployment. (Ma'rouf, 2006, p. 77)

3. Indicators of Stagflation in an Economy

There are several signs that indicate the presence of stagflation in a country's economy, which can be outlined as follows: (Khaled , , 2009, p. 145)

1.3 Decline in Economic Growth Rates:

A significant decline in economic growth rates is one of the most important indicators of stagflation. We can observe that the decline in growth rates began in capitalist countries that experienced stagflation in the early 1970s, following a period of economic recovery. These countries had achieved high growth rates during that period, but these rates soon began to decline sharply. For example, Japan's growth rate dropped from 9.9% in 1973 to 1.8% in 1974, and then fell further to 1% in 1975. Similarly, France's economic growth rate dropped from 5.4% to 3.1% and then to 0.3% during the same period. (Batoul , 2006, p. 167)

2.3 Continuous Rise in the General Price Level:

Economic inflation is one of the most common economic phenomena affecting different economies. This phenomenon began in capitalist countries after World War II, and its intensity increased during the 1970s, 1980s, and 1990s. Inflation in the United States reached 10%, while in Japan, it peaked at 24.5% in 1974. In the UK, inflation was 9.1% in 1973 and doubled to 16% in 1974. In France, inflation was 7.3% in 1973 and reached 13.7% in 1974.

3.3 Continuous Decline in Profit Rates:

Profit rates are the main driving force behind capital accumulation and production expansion. A decline in these rates leads to the opposite effect. Achieving good profit rates depends on optimal labor utilization, market commodification, tax rates on profits, productivity growth, as well as technological advancements and their application in the production process. A continuous decline in profits represents one of the signs of stagflation. For example, corporate profits in the UK between 1950 and 1954 were about 25.2%, but this rate dropped to 12.1% in 1970. In the United States, profit rates fell from 8.6% in the early 1950s to 5.4% in 1973.

4.3 Rising Unemployment Rates:

Unemployment is primarily attributed to a lack of aggregate demand, which leads to subsequent negative effects. Therefore, the economic variable that can effectively control the employment level is the total expenditure level. Unemployment is typically a short-term cyclical issue; however, it became a structural long-term issue beginning in the 1970s. In the United States, the unemployment rate reached 7% in 1980 and rose to 9% in 1982, resulting in the loss of approximately 2 million jobs. In the UK, the OECD reported in its semi-annual report that about 3 million people were unemployed in 1982.

There are several other indicators that suggest the presence of stagflation, including:

- Declining productivity growth rates
- Reduced capital formation rates
- Deterioration in the utilization of production capacity
- Growth in the budget deficit

4. Similarities and Differences Between the Seventies and the Current Period

Global consumer price inflation rose steadily during the 1970s,

starting from a range of 1.7% to 4.4% annually in the late 1960s and early 1970s. By 1973, inflation surged to 10.3% after the first oil price shock, caused by the oil export ban to the West led by Saudi Arabia.

Inflation continued at a rapid pace for the remainder of the 1970s and remained high until the global recession in 1982. As a result, the average inflation rate from 1973 to 1983 was around 11.3% annually, more than three times the average of 3.6% annually from 1962 to 1972. This rise in inflation during the 1970s coincided with a significant depreciation of the US dollar. (World Development Report. : , 1983)

4.1 Inflation Between the Seventies and the Pandemic:

While the rise in inflation since the global recession in 2020 has been less severe than after the 1975 recession, the expected slowdown in growth is likely to be much more pronounced. Between 2021 and 2024, global growth is expected to slow by 2.7 percentage points, more than double the rate recorded between 1976 and 1979. The slowdown is expected to be more noticeable in advanced economies, but it will also be significant in developing economies and emerging markets.

Over the current decade, global economic growth is expected to slow by 0.6 percentage points below the average level from 2010 to 2020. This structural weakness is similar to the growth slowdown experienced during the stagflation of the 1970s. (The Ukrainian Crisis and the Pains of Stagflation Sweeping the West Retrieved August 20, 2022,, 2022)

4.2 Key Vulnerabilities in Emerging Markets:

In the 1970s and 1980s, as is the case now, rising debt, inflation, and weak financial positions led to vulnerabilities in developing countries and emerging markets facing tightening financial conditions.

The stagflation of the 1970s coincided with the first global wave of debt accumulation in modern history. The decline in real interest rates globally and the rapid development of syndicated loan markets encouraged increased borrowing in regions such as Latin America and many low-income countries, particularly in Sub-Saharan Africa.

In Latin America, total external debt increased by 12 percentage points of GDP over the decade, while in low-income countries, it rose by 18 percentage points. Most of this debt was in foreign currency and short-term. Capital flowed from oil-exporting countries to developing countries and emerging markets with fiscal deficits and current account imbalances. When central banks in advanced economies, particularly the Federal Reserve, began tightening monetary policy in the late 1970s to curb inflation, a series of debt crises erupted.

By contrast, the period from 2010 to 2020 saw the fourth wave of global debt accumulation, which continues today. This period was marked by the largest and fastest increase in government debt in developing and emerging economies over the past fifty years. Indeed, several low-income countries now face or are on the brink of a debt servicing crisis. The World Bank reports that foreign debt in middle- and low-income countries reached \$8.7 trillion by the end of 2020. (The Ukrainian Crisis and the Pains of Stagflation Sweeping the West Retrieved August 20, 2022,, 2022)

The size and speed at which debt has accumulated pose significant risks. Additional vulnerabilities have emerged due to growing exposure to non-traditional official creditors and commercial debt, which, coupled with the risk that inflationary pressures could lead to sharp tightening of monetary policies in major advanced economies, could reignite a series of financial crises in developing and emerging markets, as seen in the 1980s.

If the pressures of current stagflation continue to escalate, developing and emerging economies will likely face significant challenges again due to their weaker resilience to inflation, rising financial vulnerabilities, and deteriorating growth fundamentals. This underscores the need for these

economies to strengthen their financial and external protective barriers, enhance their monetary policy frameworks, and implement reforms to stimulate growth.

Before the pandemic, many studies focused on the remarkable decline in inflation over the past five decades. Global inflation dropped from a peak of 16.9% in 1974 to 2.3% in 2019. This downward trend was observed broadly across both advanced economies and developing markets. Between 1974 and 2019, inflation in advanced economies fell from 15.3% in 1974 to 1.3% in 2019, while in developing economies and emerging markets, it dropped from 17.5% in 1974 to 2.6%. These reductions were driven by a greater focus of policymakers on price stability as a primary goal and by globalization, which liberalized labor, product, and financial markets.

In fact, inflation declined substantially in the 1990s and the first decade of the 21st century, a period some have referred to as the "Great Moderation." By the early 2000s, deflation became a significant concern in some advanced economies.

By 2019, prior to the COVID-19 pandemic, inflation had fallen below target ranges in most advanced economies with inflation targeting frameworks, and it remained within target ranges in developing and emerging economies from 2012 to 2019. (The Stagflation Nightmare: The Terrifying Economic Recession , 2022)

4.3 Similarities with the 1970s Crisis:

The similarities between the current crisis and the situation in the early 1970s lie in several key elements, including supply shocks, rising global inflation in the short term, preceded by a long period of ultra-loose monetary policies in major economies, as well as the notable recent fiscal expansion and expectations of weaker long-term growth. These elements echo the growth slowdown that was unexpected in the 1970s, along with the

vulnerabilities faced by developing economies and emerging markets regarding the tightening of monetary policy in advanced countries, which is essential to curb inflation. The main points of similarity include: (The Stagflation Nightmare: The Terrifying Economic Recession , 2022)

Supply Shocks: The disruptions in supply caused by the pandemic and the more recent shocks in global energy and food prices due to the Russia-Ukraine war are comparable to the oil shocks in 1973, as well as those in 1979 and 1980.

The 1970s saw the largest energy and food price shocks in the previous fifty years. In comparison, the period from April 2020 to March 2022 experienced the second-largest increase in energy prices and the third-largest increase in food prices since 1970.

Moreover, the monetary policy conditions before these shocks—both now and in the 1970s—were ultra-loose, with the global average real interest rate being 0.5% between 1970-1980 and 2010-2021. The experience of the 1970s tells us that delays in raising interest rates will ultimately require larger increases to curb inflation. Given that debt in developing and emerging economies has reached its highest levels in decades, the increase in debt tied to global borrowing costs and currency depreciation could trigger financial crises in these countries, similar to what occurred in the early 1980s.

Weak Growth: The world emerged from the recession caused by the COVID-19 pandemic in a weakened state, much like the post-recessionary stagflation that followed the global recession in 1975. In the near term, inflation is likely to remain high, as supply and demand shocks will continue to affect wages and prices. However, there are reasons to believe that these pressures will be temporary.

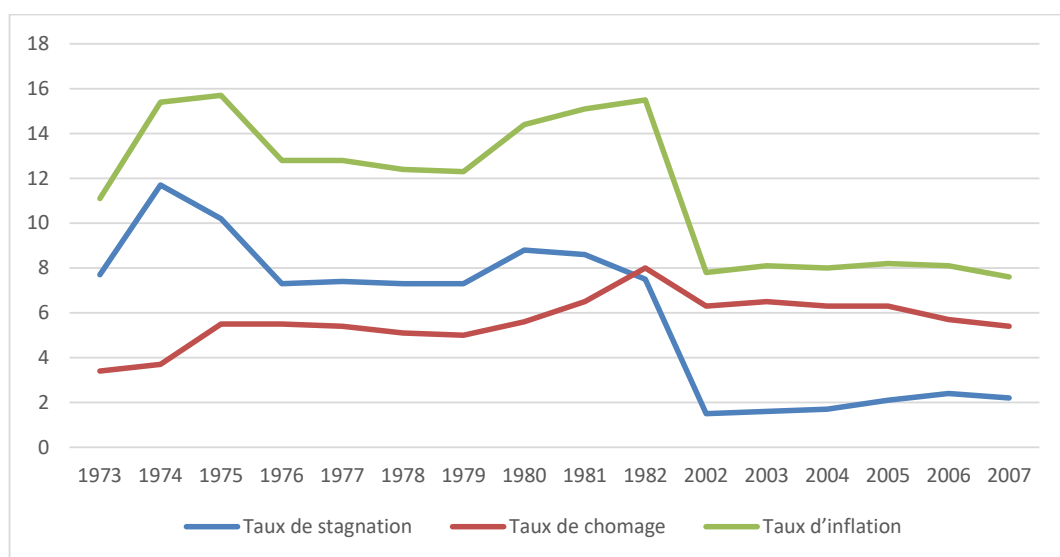
Unlike the 1970s, central banks now have established targets for inflation, and in many cases, they have built considerable credibility over decades. Therefore, inflation expectations are likely to stabilize, especially if central banks signal their intent to control price pressures.

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While central banks are tightening monetary policies and withdrawing fiscal incentives provided during the pandemic, demand-side pressures are expected to subside. Additionally, when considering the supply disruptions caused by the Ukrainian war in pricing operations, commodity prices will stabilize, even if they remain at high levels.

As global production lines and logistics systems adjust, supply bottlenecks will ease. Furthermore, many wealthy nations have become less reliant on cheap energy prices, and most central banks are now more independent in their operations.

Figure 1: Evolution of Stagflation Inflation Rate



Source: (Batoul , 2006, p. 230)

4. Differences and Policies Addressing Stagflation

The current phase also differs from the 1970s in several key aspects: (The Ukrainian Crisis and the Stagflation Pains Sweeping the West, 2022)

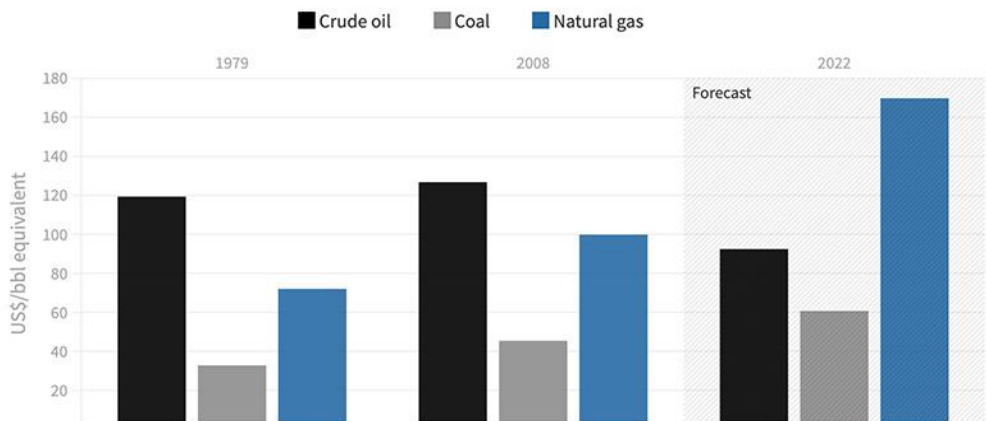
- **Significant Decline in Growth Projections:** Global growth is expected to slow to 2.9% this year, down from 5.7% in 2021. This reflects a nearly one-third reduction from the January 2022 projections, which had forecasted a 4.1% growth rate for this year. The primary cause of this downward revision has been the sharp rise in energy and food prices, along with supply chain disruptions and trade disturbances caused by the war in Ukraine and the necessary normalization of current interest rates.

The COVID-19 pandemic has already caused a major setback for income growth and poverty reduction efforts in developing economies. The consequences of the ongoing war in Ukraine are compounding the challenges many of these economies face, with a projected growth rate of just 3.4% in 2022—barely half the rate of 2021 and well below the average growth rate from 2011 to 2019. Similarly, growth projections for middle-income countries have been sharply revised down for 2022, losing 1.3 percentage points compared to January's forecast.

Figure 2: Evolution of Energy Prices

Some energy prices are at their highest levels since the 1970s

Natural gas, coal, and crude oil prices (U.S. dollars per barrel equivalent)



Source: World Bank Group via the June 2022 Global Economic Prospects • Note: Figure shows the annual price of coal, Brent crude oil, and European natural gas, deflated using U.S. CPI. 2022 shows the current price forecast. Shaded area represents a forecast.



Real per capita income in 2023 is expected to remain below pre-pandemic levels in about 40% of developing economies. In many countries, avoiding a

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recession will be difficult. As natural gas supplies are constrained, particularly for fertilizer production and energy grid operations in poorer countries, announcing large increases in production will be critical to restoring non-inflationary growth.

- **Risk of Persistently Higher-than-Average Inflation and Lower-than-Average Growth for Many Years:** This scenario—unseen since the 1970s—is a significant concern. From 2021 to 2024, global growth is expected to slow by about 2.7 percentage points, more than double the slowdown experienced from 1976 to 1979. Weak growth is expected to persist throughout the decade due to low investment in most regions of the world. With inflation now at its highest levels in several decades across many countries, combined with expectations of slow supply expansion, there is a risk that price growth will remain higher for a longer period than currently anticipated.

Figure 3: Evolution of Basic Consumer Prices

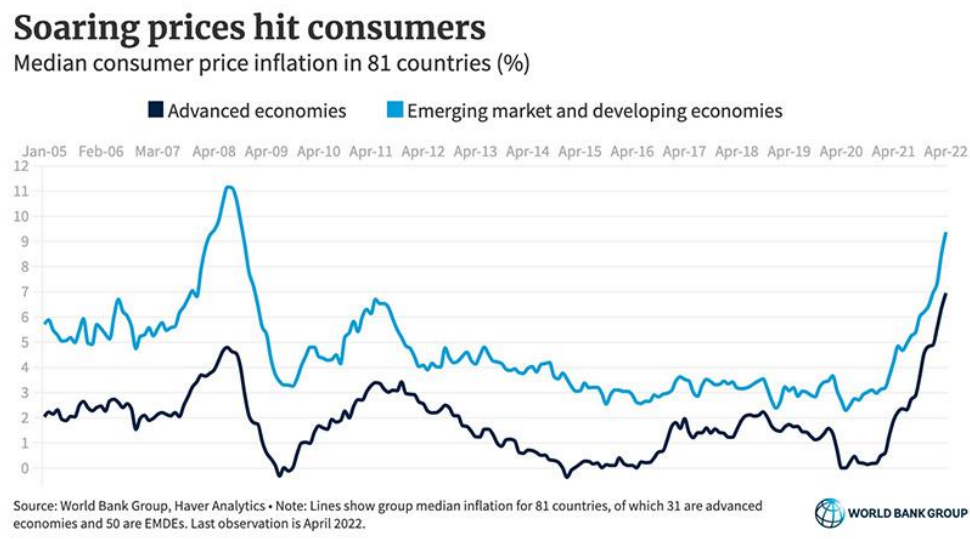
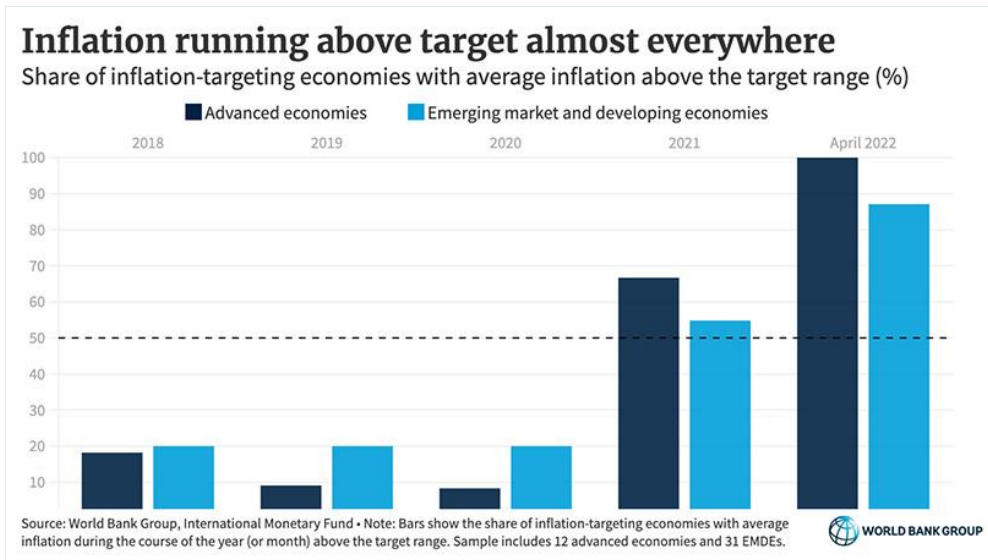


Figure 4: Inflation Rate Exceeding Target



- **External Public Debt in Developing Economies at Unprecedented Levels:**

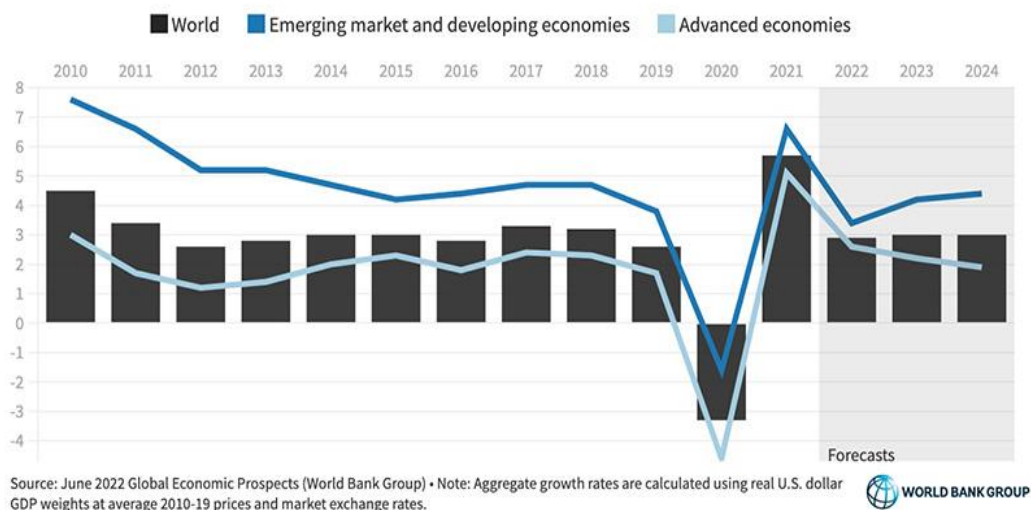
The external public debt in developing economies has reached record levels today. Most of this debt is owed to private creditors, and a significant portion has variable interest rates, which could suddenly rise. With tighter global financing conditions and currency devaluation, debt distress—previously confined to low-income economies—is now spreading to middle-income countries.

The end of monetary easing in the United States and other advanced economies, coupled with the subsequent rise in global borrowing costs, represents another major headwind for the developing world. Moreover, over the next two years, most of the financial support provided in 2020 to combat the pandemic will no longer be in effect, although debt levels will remain high. With the removal of policy easing measures, it will be essential to address income inequality gaps and strive for higher incomes for all by using financial and monetary tools that can enhance supply chains, small businesses, and capital allocation processes.

Figure 5: Evolution of Economic Growth Rate

A steep slowdown is underway

GDP growth (%)



To reduce the risks of stagflation, policymakers around the world will need to implement targeted measures. In this exceptional era, marked by interwoven global crises, policymakers must focus their efforts on five key areas: (The Stagflation Nightmare, 2022)

First: Efforts must be made to mitigate the harm caused to people affected by the war in Ukraine. This will require coordinating the response to the crisis, including the delivery of emergency food, medical, and financial aid to war-torn regions, sharing housing burdens, providing support, and possibly resettling refugees and internally displaced persons.

Second: Policymakers must resist the sharp rise in oil and food prices. It is essential to increase the supply of basic food and energy commodities. Markets are always forward-looking, and merely announcing upcoming supplies will help reduce prices and inflation expectations. Every country

should work to support social safety nets and avoid imposing export and import restrictions, as these measures tend to amplify price increases.

Third: There is an urgent need to intensify efforts to alleviate debt burdens. Debt vulnerabilities were already acute in low-income countries before the pandemic broke out. As debt distress spreads to middle-income countries, the risks to the global economy will grow in the absence of swift, comprehensive, and large-scale relief processes.

Fourth: Authorities must work to strengthen health preparedness and efforts to contain the COVID-19 pandemic. Expanding vaccination efforts in low-income countries, including COVID-19 vaccines, should be a high global priority.

Fifth: It is crucial to accelerate the transition to low-carbon energy sources. Reducing reliance on fossil fuels will require increased investment in electricity grids, cleaner energy sources, and enhanced energy efficiency. National policymakers should focus on establishing climate-smart regulatory frameworks, adjusting incentive structures, and strengthening land use regulations. Restoring long-term prosperity depends on resuming faster growth in a more stable and rules-based policy environment. There is good reason to expect efforts to rebuild the Ukrainian economy and revive global growth to double, including those led by the World Bank, once the war in Ukraine comes to an end. At the same time, policymakers must be vigilant in addressing other threats to development worldwide: soaring food and energy prices, ongoing stagflation pressures, increasing debt burdens, widening inequality gaps, escalating instability, and the numerous risks posed by climate change.

5. Conclusion:

From the above, we can conclude the following:

The current circumstances also differ from the 1970s in several important ways. The dollar, which was extremely weak in the 1970s, is now strong. During the period from 1973 to 1974, oil prices quadrupled, and then

doubled again between 1979 and 1980. Today, after adjusting for inflation, oil prices are only two-thirds of the level they were at in 1980. Furthermore, the balance sheets of major financial institutions are generally strong today, whereas they posed a significant risk in the 1970s.

Additionally, economies around the world have become more resilient than in the 1970s, with less structural rigidity related to wages and labor markets. Policymakers are in a better position today to counteract the headwinds of stagflation. The credibility of monetary policy frameworks has also improved: central banks in both advanced and many developing economies operate under clear mandates for price stability. This, alongside the fact that current technologies and capital have the ability to provide substantial increases in supply, has helped stabilize long-term inflation expectations.

- potential for a price spiral driven by wage increases.
- Differences in the management of monetary policy that may help prevent the onset of another stagflationary cycle.
- Energy and food prices are still lower than they were following the sharp increases of the 1970s, coupled with improved economic resilience and the ability to withstand shocks.

Therefore, the study adopts a descriptive-analytical approach, providing economic and social explanations to identify the similarities and differences between economic, energy, and food crises, and their impact on countries worldwide, comparing the period of the 1970s with the current period, especially after the COVID-19 crisis and during the Russian-Ukrainian war.

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