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**DIRECTORATE-
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A F F A I R S**

**THE ECONOMIC SITUATION
IN THE COMMUNITY**

4

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QUARTERLY SURVEY

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The Economic Situation in the Community

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Contents

	<i>Page</i>
Introduction	3
I. The overall situation	5
A. <i>The balance-sheet for 1962</i>	9
1. Demand	9
2. Production	13
3. The balance of the markets.	17
B. <i>Outlook for 1963</i>	25
C. <i>Economic policy</i>	30
II. The situation in each of the Community countries	33
A. <i>Federal Republic of Germany</i>	35
1. Balance-sheet for 1962	36
2. Outlook for 1963	41
B. <i>France</i>	45
1. Balance-sheet for 1962	46
2. Outlook for 1963	53
C. <i>Italy</i>	56
1. Balance-sheet for 1962	57
2. Outlook for 1963	63
D. <i>Netherlands</i>	66
1. Balance-sheet for 1962	67
2. Outlook for 1963	73
E. <i>B.L.E.U.</i>	77
Belgium	77
1. Balance-sheet for 1962	78
2. Outlook for 1963	84
Grand Duchy of Luxembourg.	87
1. Balance-sheet for 1962	87
2. Outlook for 1963	89

Graphs

1. Industrial production	15
2. Intra-Community trade	21
3. Businessmen's views on the industrial situation :	
a) Federal Republic of Germany	37
b) France	47
c) Italy	59
d) Netherlands	69
e) Belgium	79

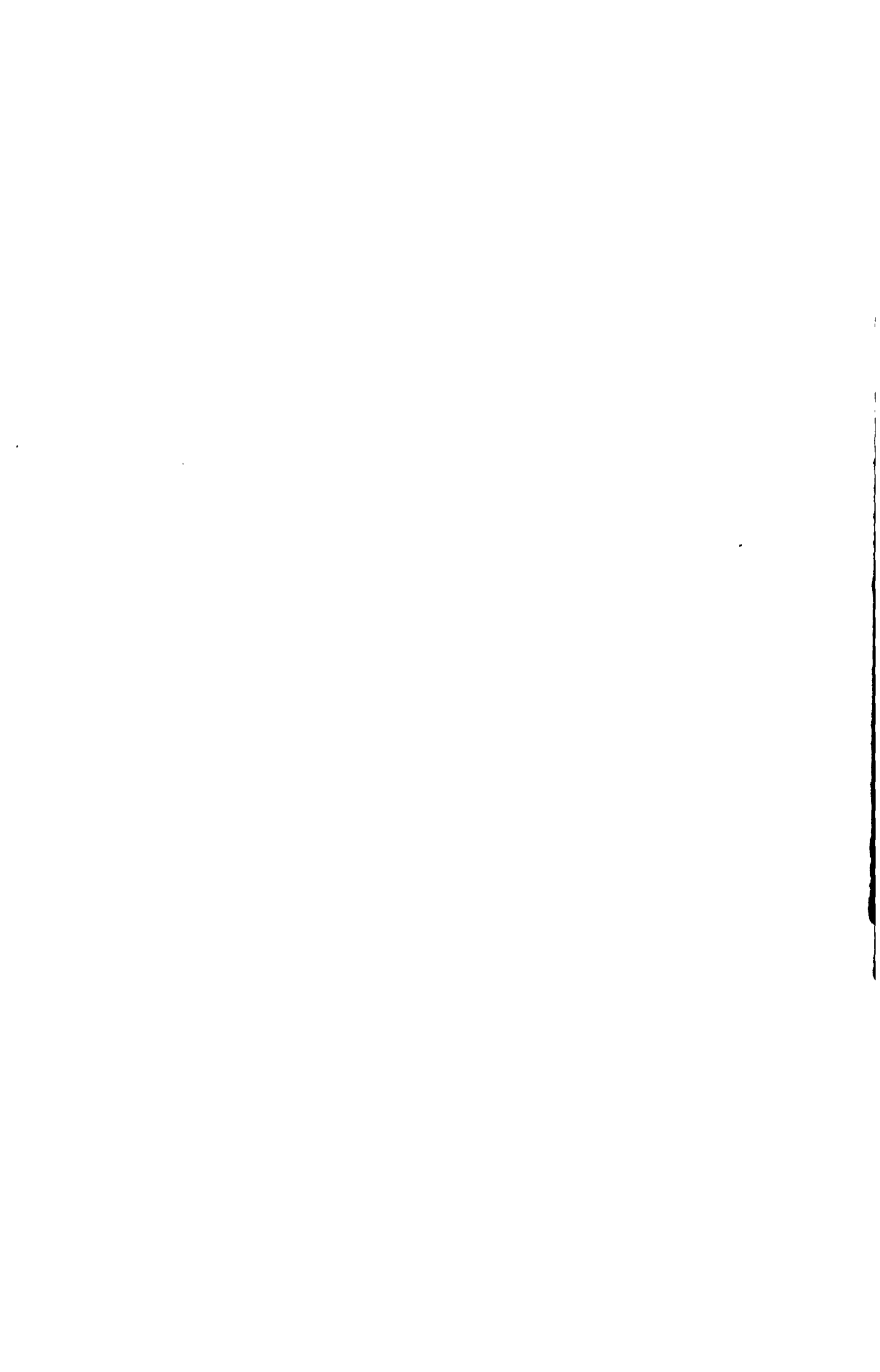
Introduction

The practice hitherto has been for the first quarterly Survey in the yearly series to serve as an annual report. This has meant that the previous year's balance-sheet and the forecasts for the current year have had to wait until the beginning of April, when a whole quarter year had gone by.

Although there are of course statistical reasons for continuing this procedure, the need to have by an earlier date the fullest possible picture of the year ending and a preview of the whole of the next year has proved stronger. This is chiefly due to economic policy considerations. By April policy for the current year has already been largely determined and can scarcely be altered in the light of forecasts in any way that will affect economic developments that year. Economic and conjunctural policy even demand that preliminary estimates for the following year should already be available in the spring, since the main lines of the central budget are first laid down at that time. It is clear, however, that these are still very tentative and in the main provisional.

Nevertheless, the Survey must also be adapted as far as possible to these needs. For this reason, beginning with this issue, the last of each set of quarterly Surveys will be in the nature of an annual report, with a balance-sheet of the year ending, and estimates for the whole of the one ahead. This will not greatly add to the statistical or other difficulties of analysis and prognosis now that in all Member States, under the decision to make general use of the economic budget technique, the relevant work will have been done.

This does not mean that the data contained in the present Survey exactly reflect the member countries' economic budgets. To begin with, the Commission's Quarterly Survey do not lend themselves to the sort of detailed and technical presentation required for national economic budgets. Furthermore, some Member Governments attach importance to the economic budgets they submit to the Economic Policy Committee being treated as confidential. Finally, the Commission wishes to continue to reserve the possibility of introducing into its Surveys forecasts and evaluations which are the expression of its own opinions and which might differ on this or that point from national official statements and figures. This has been done in the present Survey; although, as always, they have been thoroughly discussed with experts from the member countries, the arguments and forecasts contained therein are published under the Commission's sole responsibility and do not necessarily correspond precisely with the official economic forecasts of member countries. We wish to emphasize once again the hypothetical nature of the forecasts and also their essentially neutral character : they set no targets.



I. THE OVERALL SITUATION

In 1962 the Community's economy made further progress. The real gross internal product was probably up about 4.5 % on 1961, after a rise of 5.2 % between 1960 and 1961 and 7.1 % between 1959 and 1960. Industrial output in 1962 was about 6 % higher than in the previous year (1961: + 6.6 %, 1960: + 13.1 %).

The real gross internal product has thus increased by 27 % in the five years since the Rome Treaty came into force, i.e. between 1957 and 1962; industrial output alone rose no less than 40 %.

Nevertheless, there has been an unmistakable slowdown in economic growth. This was indeed to be expected in 1961 after the investment boom which decisively influenced economic development between the spring of 1959 and mid-1960 and led to a particularly high growth rate of the internal product in 1960. However, the slowdown continued between 1961 and 1962, although it was not so marked.

Whereas in 1961 the fall in growth rates was chiefly attributable to material obstacles—labour was in very short supply in most member countries—slower expansion of certain elements of demand was an increasingly determinant factor in 1962.

The weakness of demand was most noticeable in the case of exports. In fact, the Community's sales abroad hardly rose between 1961 and 1962. The economic upturn in the USA was not sufficiently vigorous to offset completely the inhibiting effects on world trade of previous recessions. Up to the spring of 1962, moreover, the United Kingdom was in the grip of a recession, while growth flagged in other important non-member industrial countries. Last but not least, balance of payments considerations prevented the developing countries from importing more from the Community.

The growth of internal demand was likewise somewhat slower; particularly fixed investments by undertakings expanded at a declining rate. This was mainly an after-effect of the rather exaggerated boom in 1959/60, which put a heavy strain on the labour market and triggered off cost increases that squeezed profit margins—the more so as weak external demand and stiffer foreign competition limited the possibility of marking up prices. In addition, it became more difficult to find outside finance for investments because of changes in payments balances and weaker stock markets. It is true that the "EEC factor" continued to have positive effects, i.e. investments made with an eye to the common market increased, though on the whole the propensity to invest clearly declined.

Public investment expenditure and house-building certainly remained quite expansive, but their growth, real and nominal, was checked by the bad weather which fairly seriously hampered building activity in general in the early months of 1962.

In view of these sluggish trends affecting most of the components of demand, private consumer expenditure, increasingly became the chief motor of growth. Wage incomes rose steeply in nearly all member countries, while the expansion of other incomes, although slower, continued to be substantial. The increase in private consumption expenditure was therefore still somewhat greater than in 1961. Meanwhile, as a result of the faster rise in prices, partly attributable to the effects on the supply of certain farm products of the bad weather in some member countries in the first half-year, the volume increase in consumption was somewhat smaller than in the previous year.

Internal trade was again responsible for the main contribution to improved market equilibrium. In value it went up about 13 % between 1961 and 1962, following a rise of 15 % between 1961 and 1961. Compared with 1957 the Community's internal trade has grown about 85 %.

But imports from non-member countries also again rose considerably—about 9 % in value and volume between 1961 and 1962, bringing the cumulative increase

since 1957 to about 25 % in value and about 48 % by volume. As imports again rose faster than exports, the trade balance further deteriorated: it showed a deficit of about 1 500 million dollars after being almost in balance in 1961.

Nevertheless, as already mentioned, it was again not possible to keep prices stable. Leaving aside abnormal developments in farm prices, the moderate but steady upward trend in prices of services and industrial products continued. This was, however, due less and less to ex ante imbalances between the expansion of supply and demand but increasingly to the after-effects—in the form of rising costs—of the earlier upswing of the investment pendulum.

The outlook for the Community's economy in 1963 is highly propitious even though a further slight slowdown in the expansion of demand is expected. Thus, a limited rise in demand from non-member countries may be anticipated: the shifts in the relative cost situation in recent years will exercise certain influence here. However, it is mainly a matter of the relatively weak expansion of demand in important non-member industrial countries and the limited foreign exchange availabilities of the developing countries. These factors particularly hamper the Community's capital goods exports, which are a comparatively weighty component of its export pattern.

A further slackening of the growth of investments by enterprises is also to be expected although in some member countries profits have probably taken a turn for the better. Given normal weather conditions, however, this slackening will be largely offset by a very sharp rise in total building investments over 1962, so that the growth of overall gross fixed investment might finally be only very little below that of 1962 (about 5 % in real terms).

Private consumption will again go up appreciably, though possibly at a rather slower pace than between 1961 and 1962.

Since the slowdown, albeit slight in the expansion of total demand will chiefly affect imports, the growth rate of gross Community product may be about 4.5 %—practically the same as between 1961 and 1962: the rise in industrial output could be 5 %.

Prices might be more stable in 1963, thanks, among other things, to the slower rise of wages costs per unit/product expected in certain member countries. The rate of productivity has improved and pay increases should be a little smaller than in 1962.

Imports will certainly continue to rise in 1963. However, mainly owing to the better 1962 harvests and the rather slower growth of overall demand, the rise

will be smaller than last year. Since exports are expected to grow only moderately the trade balance will again deteriorate. Nevertheless, the current payments balance should continue to show a surplus, although this will again be smaller.

As already said, these are eminently favourable development prospects. A slight temporary slowdown in the growth of total demand after last year's boom is only to be expected and even in some ways desirable: it promises a slight easing of labour markets, a better price climate, and a brake on rising costs. Although further measures to stimulate expansion do not at present seem called for in the Community, the prospects outlined above nevertheless demand that a particularly wary eye be kept on the development of demand in 1963. They are in fact based on the assumption that the Community does not have to contend with any strong recessive tendencies from outside and that no too sharp decline—much less a fall—occurs in the expansion of investment by enterprises. If—contrary to expectations—signs of such development should emerge, conjuncture policy must be able and ready to act at the appropriate time in support of demand. The Commission has sent the member Governments recommendations whose implementation should further enhance the already intrinsically high state of readiness to parry any tendencies for economic activity to flag.

A. The balance-sheet for 1962

1. Demand

After declining somewhat from 1960 to 1961, the expansion of total demand in the Community again slowed down between 1961 and 1962.

For 1962 as a whole it was plain that external demand (in the sense of actual exports of goods and services to non-member countries) practically ceased to provide any stimulus to the Community's economic development. True, exports of goods in the first half of 1962 were up 3 % in value and 2 % by volume over the corresponding period of 1961, but in the third quarter they were down 2 % in value compared with the previous year. Although, according to still incomplete results, things shaped better in the fourth quarter, the growth rate in value of exports for the whole of 1962 was probably hardly over 2 %. Between 1960 and 1961 the rise had been 5 % (value) and 3 % (volume).

This development roughly reflects the world trend, which was marked by an appreciable slackening of expansion in the non-member countries compared with 1961.

The economic situation in the United States in particular disappointed hopes entertained in many quarters. Thus it became increasingly more obvious in 1962 that the rise in fixed investments by enterprises—which would have needed to be pretty considerable to ensure adequate expansion of total production—was flagging. Furthermore, after the second quarter, enterprises again became noticeably reluctant to keep up stocks. Finally, exports of goods and services became stabilized in the third quarter (taken as a whole). As a result of the lack of drive in these components of total demand—highly important in their overall effect—the expansion of employment became increasingly slower and full employment was far from being achieved. This in its turn helped to curb the growth of private household incomes and consequently of their spending. As a result of the more halting development of overall demand, the growth of production steadily declined. The real gross national product rose by no more than about 0.25 % (seasonally adjusted) between the second and the third quarter of 1962 and industrial output (also seasonally adjusted) could only just achieve an increase of 1 %. However, the economic climate seems to have brightened a little towards the end of the year. Although the seasonally adjusted index of industrial production in October was slightly below the September level, certain indicators—higher spending on consumer durables and new orders for durables in general, a rather greater utilization of capacity and consolidation of prices in the steel industry—show that economic expansion probably rallied in the fourth quarter. The recovery of stocks and shares in November might also be to some extent a sign of a more hopeful appraisal of economic prospects. In any case the gross product probably went up only about 4 % between the fourth quarter of 1961 and the

fourth quarter of 1962, compared with 7 % a year previously. Although for 1962 as a whole the growth rate of the real gross national product over 1961 was probably 6 %—in itself a very noteworthy expansion—this is statistically partly in fact attributable to the rapid advance in 1961.

The Community's exports to the United States reacted promptly to the slowing down of economic expansion in that country. Whereas in the first quarter of 1962 they were up 24 % in value over the corresponding period of 1961, in the third quarter already 1 % less was exported to the United States than in July/September 1961.

In the United Kingdom economic activity picked up in the first six months of 1962 after the reverse suffered in the second half of 1961, partly due to restrictive measures taken on balance of payments grounds. In fact, the run-down of stocks did not continue in the second quarter and increased public investment spending partly offset the continuing slackness of private investment. Private consumption also picked up in the first half-year. However, to judge by the feeble progress made in the summer and autumn, a new slowdown of production seems to have begun in the third quarter. Labour market figures also point in the same direction: the number of vacancies fell appreciably in recent months while the proportion of unemployed (as a percentage of the employee labour force) rose by November 1962 to 2.4 % (1.7 % in November 1961). Although the United Kingdom's real gross national product in 1962 was probably up about 2 % on 1961, this mainly reflects, on the one hand, the setback suffered in 1961 and, on the other, the upturn in January/June 1962—followed by modest expansion only.

Community deliveries to the United Kingdom clearly declined in the first quarter of 1962, since when they have picked up a little. Their 1962 total is, however, unlikely to be appreciably above that of the previous year. By contrast, between 1960 and 1961, they rose 3 % in value.

In the other EFTA countries economic expansion as a whole distinctly slowed down. Nevertheless, it was still livelier than in the United States or the United Kingdom. As a result, a fairly satisfactory expansion of Community exports to EFTA was still possible and they probably rose about 5 % in value between 1961 and 1962 (13 % between 1960 and 1961).

The effects on the developing countries of the slower expansion in many industrial countries—in particular the persistently cautious policy of enterprises in the management of their raw material stocks and the consequent relatively low imports of such materials—naturally had repercussions on the industrial countries, since demand by the developing countries for their products faltered. In fact raw material prices on world markets continued to sag until the end of summer. (It is true that some recovery can be observed since November, but it came too late to have any important influence on the year's results.) This factor and the trend of their sales by volume have not exactly encouraged the developing countries to step up their purchases, although they have improved their

current payments balance—mainly by curbing of imports. In any case, the foreign exchange availabilities of some of these countries were influenced by flights of capital connected with internal political and economic conditions.

The fact that development aid from the industrialized countries probably again increased slightly and especially that the Community on occasion considerably stepped up its imports of farm products (mainly from South America) did not suffice to offset the effects of these trends.

To all this must be added the influence of the political events in Algeria. Community exports to that country fell sharply and the 1962 total was probably about 30 % lower than in 1961.

On the whole, therefore, Community sales to the overseas developing countries dropped about 6 % between 1961 and 1962. To those associated with the Community the fall was about 15 % in value, mainly because of the downturn in exports to Algeria. In the previous year there was still a rise of 2 % despite a 6 % decline in exports to the associated countries.

On the other hand, Community exports to the European development countries again rose considerably. This applies to trade with Greece, whose association with the Community came into force on 1 November 1962. Economic developments in Greece seem to have been very favourable. In the first half-year at any rate industrial production was 8 % higher than in the corresponding period a year ago; harvests again reached the exceptionally high 1961 level; the payments balance improved, and price rises at home remained within very narrow limits.

Unlike external demand, the Community's internal demand remained fairly buoyant and was practically the sole motor of economic growth. In the year-to-year comparison it rose as fast as between 1960 and 1961, but a slight slowdown in the conjunctural growth-rate could be noted during the year.

This last applies particularly to the development of gross fixed investment. The fact that, in the year-to-year comparison, this was only 5.5 % higher by volume than in 1961—which in turn was a good 9 % better than in 1960—is partly attributable to the more sluggish cyclical trend in 1962. Partly, however, it was a continuing reflection of the slower rate of growth which had already set in in 1961.

For the Community as a whole the slowdown has so far affected only fixed investments by enterprises, while public fixed investments may well have increased even somewhat faster than in 1962 than in 1961.

The reasons for the hesitant development of investment by enterprises have already more than once been alluded to at some length in this survey. An enumeration

of the most important factors—which differ in their make-up and significance from one member country to another—should therefore suffice here: the aftermath of the last American recession and its impact, material and psychological, on world business; poorer export prospects in the developing countries; sharply increased capacities following the recent investment boom, and entrepreneurs' uncertainty as to whether demand will continue to expand rapidly enough to make full use of any more new capacity; increasing external competition; shrinking profit margins in 1961—and already to some extent in 1960—due to pay increases appreciably in excess of the growth of productivity, coupled with limited possibilities for raising prices, and due to heavier taxation; as a consequence, more limited possibilities for the self-financing of investment; in the Netherlands a restrictive credit policy and physical controls to curb the expansion of industrial building; in several other member countries strains on the money or capital markets, due either to a smaller inflow of liquidity from transactions with abroad or to cash surpluses of public authorities or, finally, to psychological factors. Naturally, the slump on the stock markets adversely affected the financing of investment through the capital markets. The stimulus provided, on the one hand, by the urge to rationalize and, on the other, by the speedier increase of private consumption could not fully prevail against these inhibiting factors. The same applies to the fact that in 1962 despite fresh increases in wages costs per unit product profits again fared better in certain Community countries than in the two previous years. This was due to cheaper raw materials and semis, as a result of relative easing of the effective tax burden, higher turnover and higher prices.

On the whole, building investment in 1962 was very uneven, largely as a result of the exceptionally bad weather in the early months. Nevertheless, effective demand in 1962 as a whole was clearly above the 1961 level. Once again demand was particularly high in house building. Stocking hardly added to total demand in 1962. Firms continued to be cautious in managing their raw materials stocks but loosened up a little as the year advanced and output rose. The rund-down of stocks of semis occasionally noted in the steel consuming industries in particular, largely ceased. In some countries the better 1962 harvests compared with 1961 led to higher stocks of some farm products.

In contrast to the trend in investment the growth of consumer expenditure over the whole year was somewhat more rapid than between 1960 and 1961.

In the first place nominal public consumption in almost all member countries rose even more strongly, with wage and salary increases in the public sector playing an essential part. But in real terms too the increase in public consumption between 1961 and 1962 was generally greater than in the previous year except in France.

The growth of private consumers' expenditure for 1962 as a whole as compared with 1961 was doubtless greater than in the previous year. However, since consumer prices again rose—in some cases appreciably—the volume increase in private consumption was rather smaller; according to the latest estimates, it was about 5.4 %, as against 6.2 % between 1960 and 1961.

In general, private consumption expenditure developed almost in step with the expansion of incomes. In particular total wages and salaries again rose considerably—even more rapidly than between 1960 and 1961, except in the Federal Republic of Germany and Luxembourg. In four member countries (the Federal Republic, France, Italy, the Netherlands) the increase was 10 % or more. This expansion was mainly attributable to big wage increases; the Community's total employee labour force again rose but more slowly than in the previous year; in addition, the number of actual hours worked continued to fall in the Federal Republic of Germany and the Netherlands, although not to the same extent as in 1961.

Transfer incomes also rose faster than between 1960 and 1961, mainly thanks to higher pensions. On the other hand the share of company income or income from property in the income of private households may have expanded more slowly.

The expansion of consumer expenditure was again more largely concentrated on consumer durables, including luxury goods. For example, purchases of motor vehicles measured by the number of newly licensed passenger cars and light vans, probably went up 17 % between 1961 and 1962, compared with 15 % between 1960 and 1961. Expenditure on travel and holidays again showed a comparatively vigorous increase. However, these structural changes, in the long-term bound up with rising living standards, were sometimes overlaid in 1962 by the effects of rising food prices leading to relatively high spending on this item of expenditure.

2. Production

The slight slowdown in the expansion of total demand, combined with a spurt forward of imports—particularly of finished goods—was reflected on the production side in a corresponding decline in real growth. Physical obstacles had hardly anything to do with this; the inhibiting effects of inadequate production capacity and labour shortages in some fields—particularly building—had already been active in the previous year, and increased very little in strength in 1962.

According to the Index of the Statistical Office of the European Communities, the industrial production of the Six (excluding building, food, beverages and tobacco) went up by almost 6 % between 1961 and 1962 (6.6 % between 1960 and 1961). The growth rate thus corresponded almost exactly with the Commission's forecasts published in these Surveys at the beginning of the year.

The seasonally-adjusted growth of industrial output seems to have begun to slow down after March compared with the last three months of 1961 and the first quarter of

1962. This was attributable in the main to an increasingly hesitant development of output, in keeping with the trend of demand, in the capital goods industries. To this must be added relative stagnation in certain basic materials and semis (particularly iron and steel and non-ferrous metals) and continuing weakness in industries structurally affected by shrinking demand (particularly, certain branches of mining). Against this, many consumer goods industries—some of them “traditional”—advanced strongly in the course of the year.

Thus following the considerable increase in internal demand and the rather more favourable turn in exports the production of passenger cars and light vans went up between 1961 and 1962 by about 15 %, as against 2 % between 1960 and 1961. The chemical industry and most branches of the electrical engineering also evinced quite rapid growth. Conversely, the growth-rate flagged very clearly in mechanical engineering, where orders fell off in several countries (especially the Federal Republic of Germany). On the whole, growth in the textile industry was only very moderate because of the relatively slow increase of internal demand and weak exports.

In contrast to industrial output, building production for 1962 as a whole probably increased only little despite generally lively demand—and even continuing “over-demand” in some countries. This is primarily attributable to production losses, caused by the exceptionally bad weather in the early months of the year, which could not be fully made up later. In some member countries labour shortages also continued to act as a brake. The net result was that in housing construction—the number of building permits granted in 1962 was up a little on 1961—the volume of work in hand rose appreciably, while rather fewer dwellings were completed than in 1961.

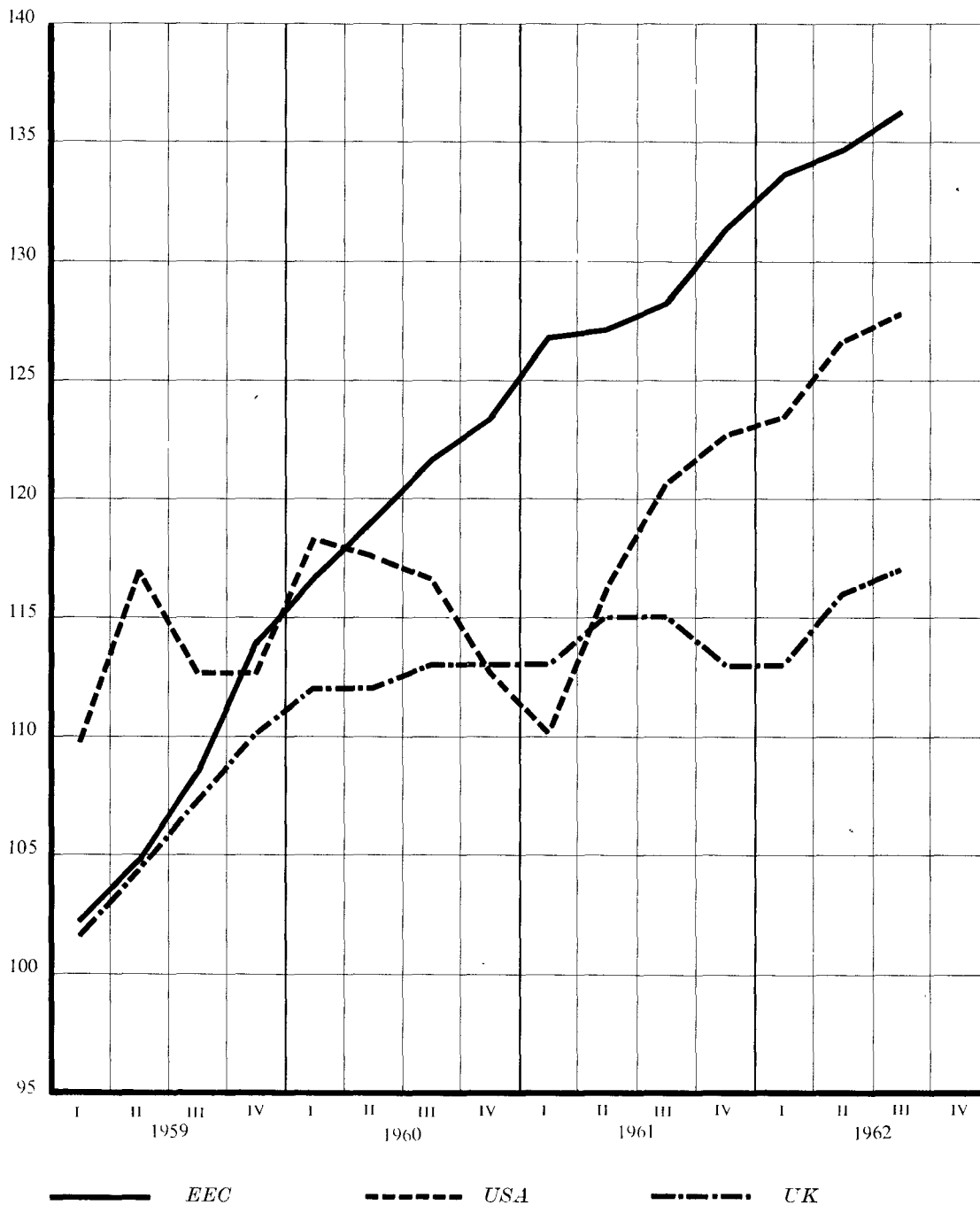
Agricultural output again made a larger contribution to the growth of the Community product than in the preceding year. Contrary to 1961, harvests were on the whole normal and for certain crops even excellent. Only in Italy was the output of some plant products less favourable than in other member countries because of drought in several regions. In the previous year the situation had been exactly the other way round.

The Community’s grain harvest reached the record year of 56 million metric tons, as against about 50 millions in 1961. Livestock production in recent months—as in the first half-year—again rose, although here too the rate of growth tended to slacken a little.

In the services sector expansion continued to be substantial in 1962. This applies particularly to those branches directly serving private households, i.e. travel, personal services, the maintenance of consumer durables and private transport. Against this, railway transport, which rose by only 2 % or 3 % over 1961, and internal waterways and sea transport, expanded less briskly than in the previous year. On the whole the contribution to the gross national product accounted for by the services sector probably grew more slowly.

INDUSTRIAL PRODUCTION

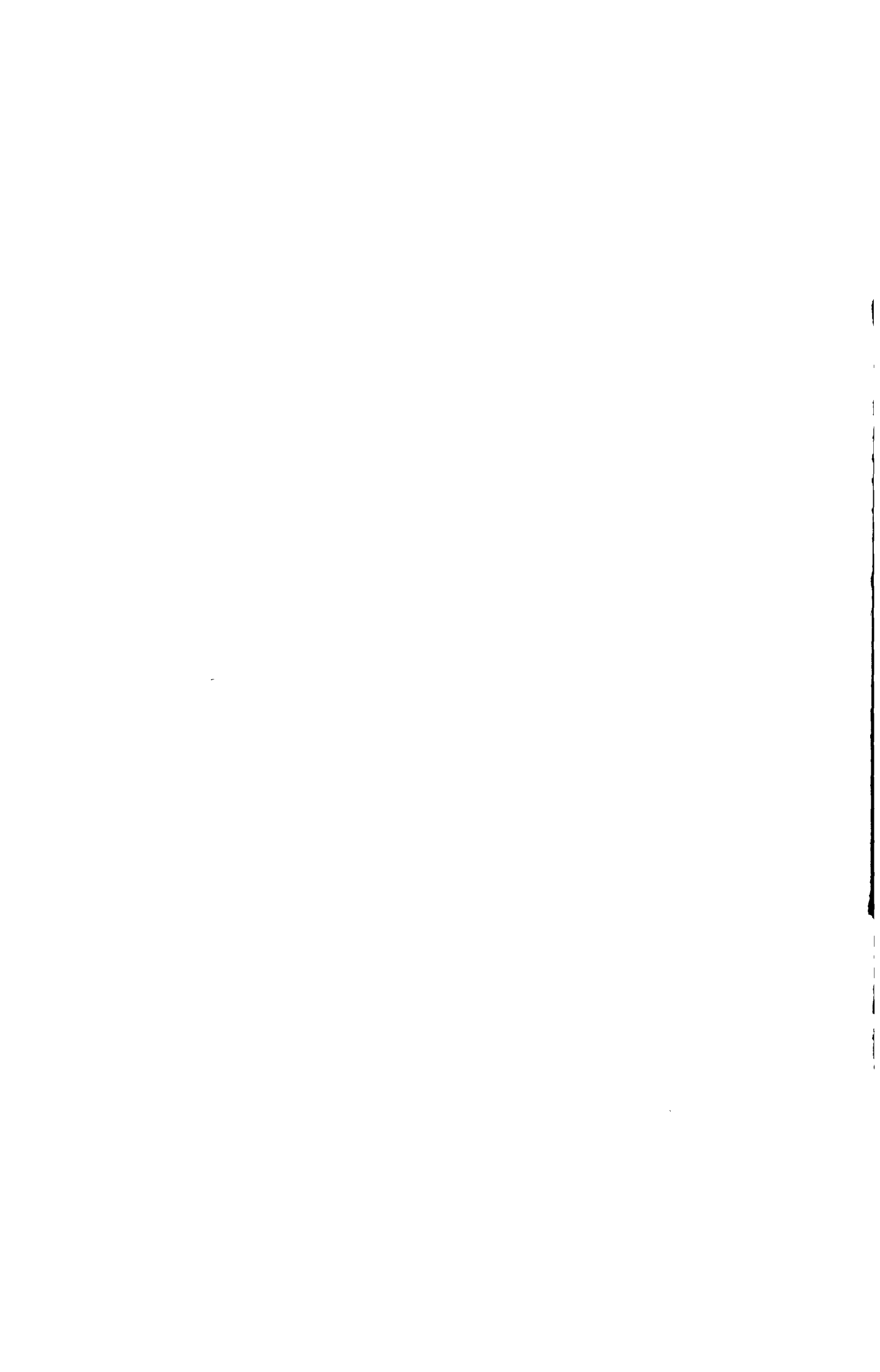
Quarterly average of seasonally adjusted indices



EEC : Indices prepared by the Statistical Office of the European Communities.

USA : Indices published in the "Survey of Current Business".

UK : Indices given in the "Economic Review" published by the "National Institute of Economic and Social Research".



The combined result of the way the individual production factors developed was that the Community's gross national product probably rose between 1961 and 1962 about 4.5 % by volume, as against 5.2 % between 1960 and 1961. This, too, tallies with the forecasts.

This slight slowdown in growth was accompanied by a somewhat smaller increase of total employment. Productivity therefore rose to roughly the same extent as in the preceding year.

The number of wage-earners in industry increased only little. Taking into account the further slight shortening of the working week and longer holidays, the number of hours actually worked was probably hardly any greater, so that production per man-hour most likely grew in roughly the same proportion as total production (6 %). The activity rate in agriculture certainly continued to decline, so that the increase in total employment was almost exclusively accounted for by services.

The year-to-year comparison shows that in 1961 the unemployment figures, already exceptionally low in most member countries save Italy, continued to fall in some of them, though generally not as steeply as in 1961. In Italy there was a further abrupt decline, to a level about 20 % lower in mid-1962 than a year earlier. In France on the other hand, there was a rise at mid-year caused by the registration of repatriates from Algeria. As to the underlying trend, the fall in unemployment in most member countries in the second half-year would seem rather to have given way to a slight upturn, either because the growth of demand for labour slowed down, or because the working population increased (particularly under the influence of the post-war bulge in births). However, these factors have as yet done little to mitigate the shortages on the labour markets of several Community countries.

It is important to note that in 1962 migration of workers within the Community again helped to maintain a better balance—by way of increased employment and production that would not otherwise have been possible, and lower unemployment and rising incomes that could have been hardly likely without such an influx. The latter remark applies particularly to Italy, since in 1962 considerably more Italians were working in the other Community countries than in 1961.

3. The balance of the markets

Unlike internal output the expansion of the Community's imports has quickened. The year-to-year growth rate in value of imports of goods (as defined in external trade statistics) from non-member countries was 7 % in the first quarter of 1962, 7.5 % in the

second, and as much as 11 % in the third. On the basis of this development and the partial figures available for the remainder of the year, the rise for 1962 as a whole over 1961 can be estimated at about 9 %, compared with 5 % between 1960 and 1961. As the average value of imports varied only slightly, the increase in volume was probably roughly the same.

This very sizeable expansion of purchases by non-member countries is mainly attributable to a faster rise in imports of manufactured goods. Consonant with the trend of the various components of internal demand, imports of capital goods tended to slow down, while purchases of consumer goods increased considerably over the whole year. Furthermore, imports of farm products were particularly high in the first half-year and even up to the summer of 1962. They were favoured by the poor harvests of 1961 and the inclement 1962 spring weather in several member countries. However, their growth in the last months of the year again slowed down as a result of the much better 1962 harvests, especially of grain. Imports of raw materials continued fairly weak, for the fall in world market prices, which lasted till October, and the more modest expectations of production of enterprises, furnished inducements to continue to keep stocks down to a minimum. Nevertheless, a slight upturn in raw material imports began to be perceptible in some member countries in the second half year.

Latin America, the United States and the United Kingdom probably benefited most from the speedier growth of Community imports.

The year-to-year growth rate in value of Community imports from these countries in the first three quarters of the year was 16 %, 10 %, and 20 %, as against 0 %, 6 % and 13 % in the same quarters of 1961. Latin America particularly stepped up its deliveries of crude oil and grain; the United States sent considerably more farm products and capital goods, while the United Kingdom increase probably consisted mainly of consumer durables. Against this, total exports of the other EFTA countries to the Community rose rather more slowly than in 1962. The associated overseas countries and territories were able to export more to the Community in terms of value : the year-to-year growth rate (value) was 6 % in the first 9 months (compared with 8 % in the same period of 1961). Since the third quarter of 1962 the growth of these countries' exports to the Community even seems to have gathered some momentum.

The Community's internal trade, i.e. the exchange of goods among Member States, again expanded appreciably more strongly between 1961 and 1962 than trade with non-member countries. This reflects not only the continuing process of interpenetration of the member countries' economies—further encouraged by cuts in customs duties at the beginning and middle of 1962 and other measures in the most varied fields—but also the fact that the economic situation in the Community, compared with non-member countries as a whole, remained more expansionary. For the full year, internal trade in 1962 was probably up about 12 % in value over 1961, whereas the rise was 15 % between 1960 and 1961.

Although at the time of writing statistics of internal trade by categories of goods were available only for the first half of 1962, partial country results and other indicators show that for the whole year consumer goods accounted for the lion's share of the increase in intra-Community trade. Against this, the growth of trade in investment goods fell off in the first half-year, if seasonal factors are left out of account. The same was probably the case in the second six months also. The expansion of trade in raw materials and semis, which was slight during the first six months of the year, probably gathered some momentum in the second half. January/June 1962 saw a lively expansion of internal trade in farm products; this was due in the main to the fact that Italy's 1961 harvest and its output of fruit and vegetables in the spring of 1962 were good, while in the other member countries precisely the opposite was the case so that the demand for imports rose. The provisional 1962 harvest figures show that output of vegetables and fruit in Italy has suffered a setback, while in most areas of the Community results were much better. Trade in farm products may therefore have been less brisk in the last quarter of 1962.

The trade balances of individual member countries with their partners in the Community show a deterioration in the first nine months of 1962 for the Federal Republic of Germany—whose surplus however continued very high—and for France. On the other hand, a definite improvement is to be observed for B.L.E.U., with practically no change for the Netherlands and Italy. The downturn in the Federal Republic's surplus is explained first, by slacker exports, notably capital goods, and secondly, by a sharper increase in imports. The latter in turn may be attributed partly to the above-mentioned factors, which determine imports of farm products, but also perhaps to some extent to rising internal prices and costs and the revaluation of the mark. The chief cause of the decline in the French surplus—mainly in the third quarter—was probably the relatively rapid growth of internal demand. In contrast to this, expansion of internal demand in B.L.E.U. in 1962 was fairly weak, so that imports from the other member countries did not rise to any marked extent. Against this, exports went up sharply among other reasons because there was some improvement in B.L.E.U.'s competitive position within the Community. Imports into the Netherlands grew at a slower pace because of the more moderate economic expansion, and exports were no livelier. In Italy the sharper rise in imports was more than offset by the expansion of agricultural exports, which was very pronounced at times.

Despite the slightly slower growth of total demand—accompanied in any case by a more modest expansion of internal supply—and despite considerably increased imports and internal trade, as well as keener competition under the stimulus of lower customs duties, prices in the Community again rose. On the year's average the rise over 1961 was probably somewhat larger than from 1960 to 1961.

Consumer prices sometimes went up fairly rapidly as a result of the unfavourable output of certain plant foods referred to several times before. However, in the second half-year there was again some downward adjustment of item. Italy and France were

exceptions, the former because of the fairly moderate 1962 harvests for several products and the latter specifically because of farm income support measures.

Prices of manufactured goods continued their steady climb, but the pace tended to slacken in some member countries. It was only in Italy that it clearly put on a spurt. Towards the end of the year consumer prices of industrial products were up by about 5 % in Italy, 3 % in the Federal Republic and France, and a little more than 1 % in Belgium and Luxembourg, compared with a year earlier. Prices of services rose somewhat more sharply—and also faster than in 1961, one of the factors involved being higher rents and increased charges for public services to offset earlier rises in costs.

Although prices rose most steeply in countries where the expansion of demand was liveliest, in the Community at large it was nevertheless the pressure of costs rather than the pull of demand which sent prices up in 1962. However, this pressure seems to have abated a little in some member countries during the year as the upward push of wages weakened, productivity increased more rapidly and profits also looked up thanks to lower raw material prices and an easing of fiscal pressure in certain cases. Accordingly there was less attempt to pass on increased labour costs per unit product in the form of higher prices. The slower expansion of demand and sharper competition naturally also played a part in the process.

With the terms of trade practically unaltered, the considerable increase in imports, combined with fairly hesitant exports, led to a serious deterioration—of something like \$1 500 000 according to the customs returns—in the Community's trade balance between 1961 and 1962. However, almost \$200 million of this is accounted for by statistical changes in the computation of imports, and does not therefore genuinely represent a deterioration reflected in the balance of payments. Another \$200 million approx. concerns trade with the franc area: from the Community point of view this must also be left out of account in the balance of payments with foreign currency areas. Still, there remains a fairly considerable amount (over \$1 000 million) which must have helped to bring about a sizeable reduction of the surplus on the Community's current payment balance. Although it is not yet possible to establish the Community's balance of payments for 1962, it may be noted that the capital balance is likely to be better than last year's, despite further, though less extensive, public debt repayments abroad.

Between January and October 1962 the member countries' official gold and foreign exchange reserves rose by only about \$400 million, as against \$1 100 million in the same period of 1961.

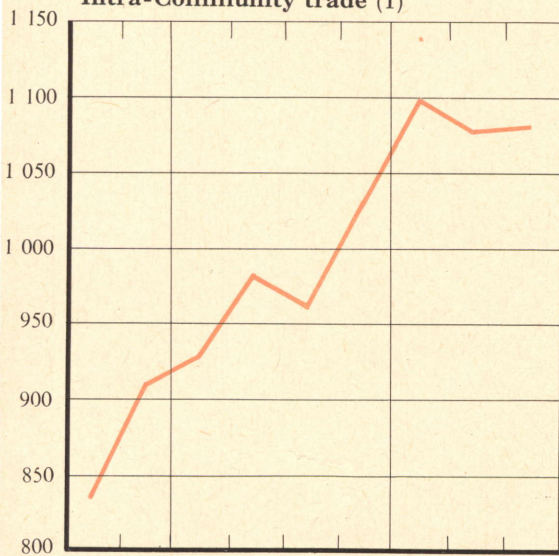
In 1962 internal liquidity underwent a certain change, mainly for balance of payments reasons. Whereas in the previous year transactions with abroad had provided all member countries with a great deal of extra internal liquidity, this was the case in 1962 only in France and Belgium. In France money repatriated from Algeria further strength-

COMMUNITY TRADE

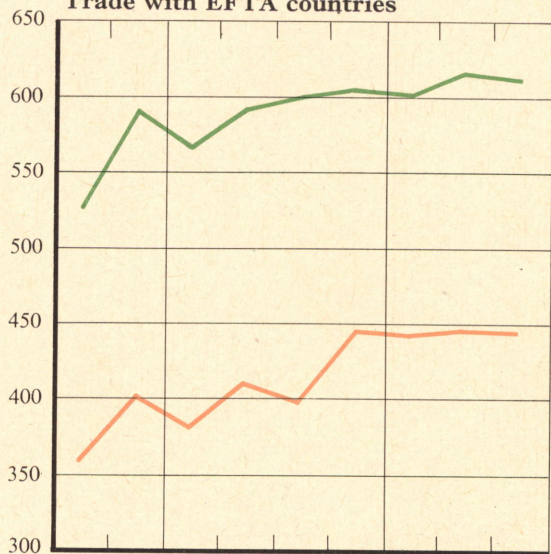
Monthly averages

In millions of dollars

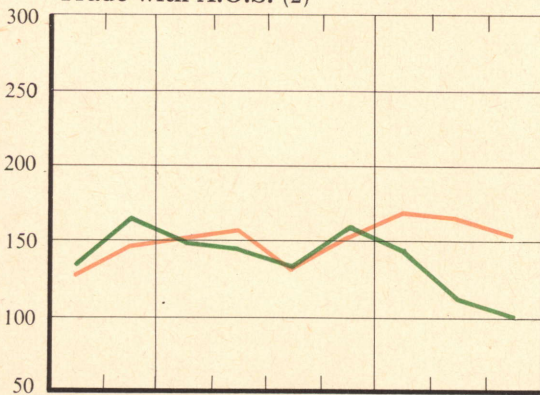
Intra-Community trade (1)



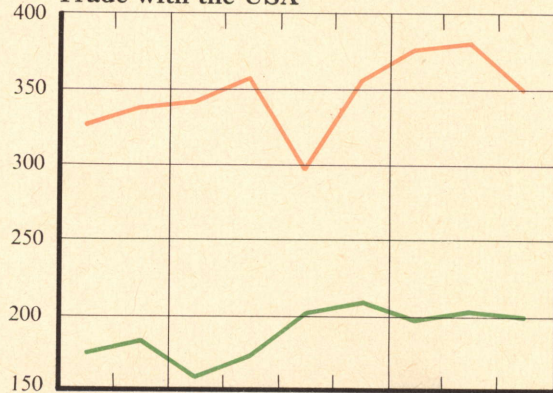
Trade with EFTA countries



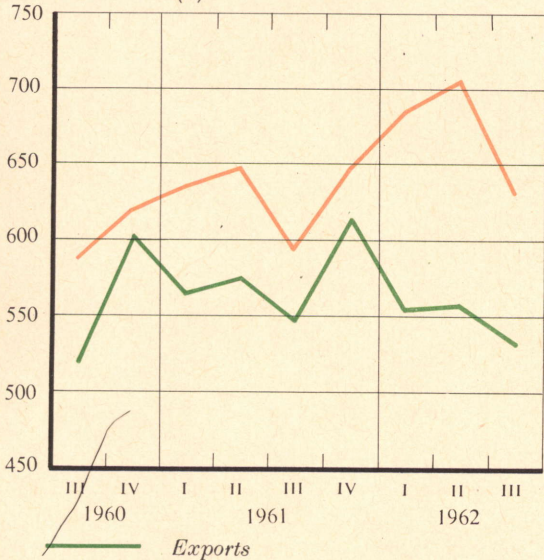
Trade with A.O.S. (2)



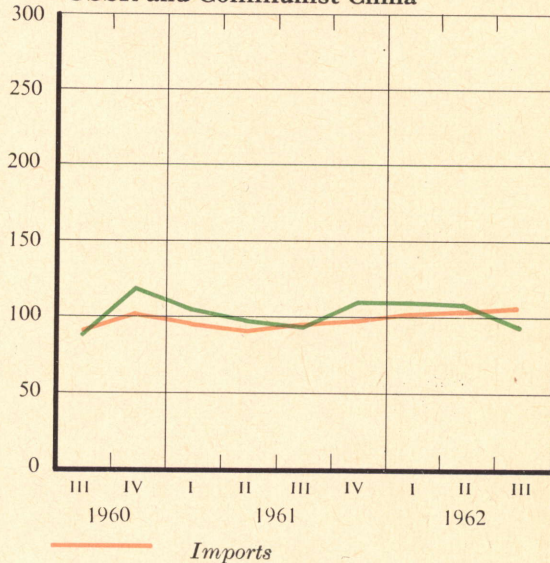
Trade with the USA



Trade with developing countries (3)



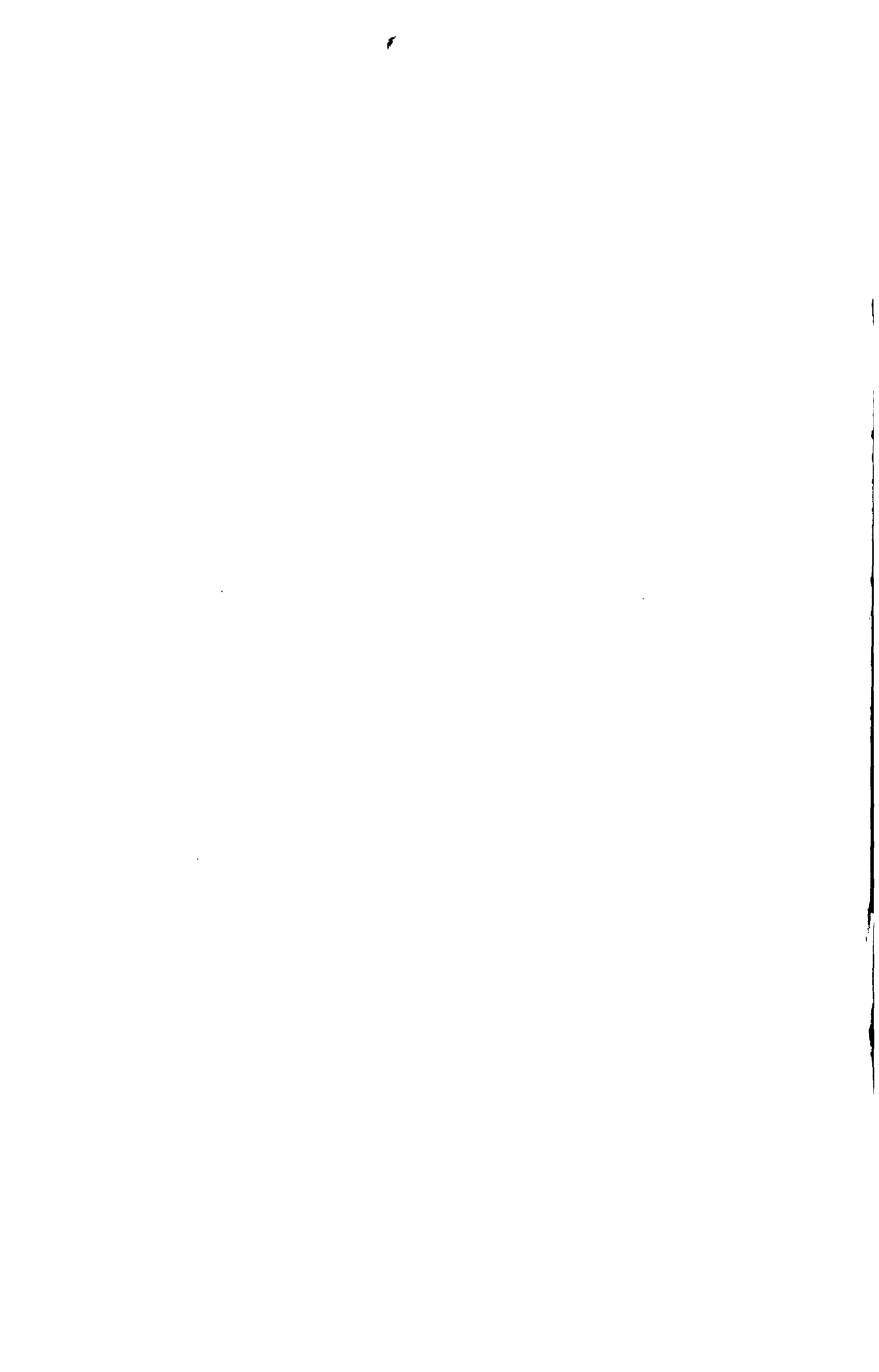
Trade with Eastern Europe, USSR and Communist China



According to import returns.

A.O.S. : Associated Overseas States (overseas departments, countries and territories).

According to GATT classification : non-industrialized regions other than A.O.S.



ened liquidity. In both countries the monetary authorities in fact permitted this increase of domestic liquidity, in the sense that, because of their surplus balance of payments position, they made no attempt to counter it. France merely took measures to channel the inflow into long-term rather than short-term investments. In the Netherlands, the Central Bank continued to follow a restrictive money and credit policy, raising Bank rate and putting a quantitative limit on credit, while in order to avoid any pronounced shortage of ready capital the State refrained from mopping up liquidity by loan issues. A lower ceiling than in the previous year was set for the placing of foreign issues on the Netherlands capital market. Finally, a relatively large influx of private capital helped to prevent any grave bottlenecks in liquidity, the more so as the Central Bank operated its minimum reserve policy very flexibly. In the Federal Republic of Germany the Bundesbank generally allowed the effects of the changes in the payments balance and the other liquidity—restricting factors—in particular further considerable cash surpluses on internal transactions by the public authorities—to have free play on the internal liquidity situation. Among other results this meant that the banks ran down their foreign exchange holdings considerably in the course of the year in order to procure mark liquidities.

The expansion of bank credit was less pronounced in 1962 in most member countries. According to the country concerned, the reasons were the contraction of bank liquidity, greater prudence on the part of the banks following falling stock markets and finally a slower growth of demand for credit, specifically due to the fact that the profit position of enterprises was no longer as unfavourable or that the muted conjuncture and diminished propensity to invest reduced the demand for finance. In Italy demand for bank credits remained very lively, since the capital market in that country was exposed to special disturbances due to the climate of opinion among investors.

On the whole capital markets did not shape very favourably. Stock markets were hard hit by price falls spreading outward from the United States, though also to some extent due to a certain change in the general economic climate in Europe and the somewhat artificially inflated bull market. This naturally had an inhibiting effect on the possibilities of raising capital on the various markets. Demand was therefore all the more strongly attracted to fixed-interest securities which were on the whole easier than in 1961. Finally, in some member countries (Federal Germany and Belgium) the State too had greater recourse to the capital market than the year before. Consequently some strain appeared on the bond market in Italy, in the Federal Republic of Germany and also at times in Belgium and the Netherlands; interest rates rose, particularly in Italy and the Federal Republic. In Belgium the trend for these to fall, which was partly attributable to special measures for the reform of the money market, again asserted itself when the temporary strains had passed.

In general the cash position of public budgets developed as might have been expected, given the economic situation. While the growth of income slowed down or remained relatively sluggish, expenditure went up sharply—in some cases faster than

ever. Only in Italy there was no sign of a change in the high surplus, and in Luxembourg too expenditure ran fairly parallel with the economic trend. Thus on the whole public budgets helped to counter the slowdown in the growth of total demand. This even applies to the Federal Republic of Germany, where domestic transactions continued indeed to yield cash surpluses, though these were nevertheless appreciably smaller.

B. Outlook for 1963

Assuming, as is very probable, that no strong recessive trends invade the Community from abroad, adequate economic growth may be expected to continue in 1963. True, the pace of expansion of total demand will again weaken somewhat, but the underlying trend will remain sufficiently rapid to ensure roughly the same increase in output as between 1961 and 1962, the more so as the slight slowdown in the expansion of demand will probably in the main affect imports.

This forecast anticipates only limited stimulus to the economy from external demand. In fact, the way external orders are shaping points to no great expansion of exports in the coming months. The available forecasts for non-member countries moreover show that for their economies the lull will continue for at least a good part of 1963. In addition, the deterioration in recent years of the competitive position of most Member States, as their costs are rising more rapidly than in such important non-member industrial countries as the United States and Great Britain—and will certainly continue to do so in 1963—might well put a brake on the Community's exports. In recent years, moreover, these countries have made considerable efforts to push their exports.

The Community's total exports to non-member countries in 1963 should thus rise only a little compared with the previous year, assuming that the leading industrial countries in fact apply an effective conjunctural policy.

This assumption particularly concerns the United States, where, despite recent signs of a better economic climate, the danger that growth will come to a halt at the beginning of 1963 still does not seem to have been completely averted. In 1962 already the Administration was concerned to combat the slowdown of expansion by an active policy to promote liquidity and by fiscal measures, particularly more generous depreciation allowances and tax reliefs for investment by enterprises. A general lowering of income and corporation tax is now planned which, since it can only be adopted by Congress in the course of the year, is to come into force retroactively from 1 January 1963. The implementation of these measures, essentially planned with an eye to a long-term growth target, could in the meantime also have an important bearing on the more immediate economic situation. Other favourable factors are the comparatively low stockpiles and further increases in public expenditure. Care will need to be taken, however, that the support effect of these measures is not brought to bear too late in 1963.

The Community's exports to the United States, which went up about 11 % between 1961 and 1962 but tended to fall off in the summer of 1962, will at best probably show only a limited rise in 1963.

The United Kingdom's recovery in the first half of 1962 lost some momentum in the second six months. The weakness of investment by enterprises and the modest growth of private consumption—which was essentially a reflection of the stabilization of employment—call for prudence in forecasting how the economy will shape in 1963. True, the Government in November 1962 took measures which might alter these trends, in particular a reduction of turnover tax on motor vehicles, an increase of public investment and an easing of depreciation procedures for private investment. However, some of these measures will take some time to make their effects felt. In any case, for 1963 as a whole compared with 1962, a moderate increase in Community deliveries to Great Britain is expected.

Against this, exports to the other EFTA countries will probably not increase as much as in 1962, in view of the prevailing economic trends in those countries.

Forecasts of exports to the developing countries are very divergent, according to whether the associated overseas countries and territories or the other primary producing countries are intended. The Community's sales to the first group became stabilized in 1962, if seasonal factors are left out of account, but 1963 may well see an improvement as a result of the strengthening of the foreign exchange availabilities of these countries, as a result of high imports by the Community and increased help under the new Association Agreement. The possibility that—in the annual comparison—the fall in exports to Algeria will be halted in 1963 and even give place to a recovery is another favourable factor. The prospects for exports to the other extra-European developing countries are much less certain. Since forecasts for 1963 show that the raw material purchases by the industrial countries will probably expand comparatively little—even if world market prices rally—only a moderate increase of exports from the member countries to the developing countries as a whole is to be expected.

Internal demand in the Community should again expand fairly vigorously. Nevertheless, the growth will again be somewhat less pronounced than in the previous year.

Gross fixed capital investment will probably rise only slightly more than between 1961 and 1962. The growth of fixed investment by enterprises—equipment purchases and spending on industrial building—will again probably fall off a little. In some member countries—the Federal Republic of Germany and Benelux—it might tend to mark time. In France on the other hand a further rise is to be expected and in Italy—granted certain assumptions as to the development of public investment and housing expenditure, some recovery in the growth of investment by enterprises is not to be excluded. However, for the Community as a whole, it must be expected that the slacker trend will continue. This is the continuation of a development which could already be observed in 1961 and 1962 and the causes of which were listed above when analyzing the economic situation in 1962. Even if some of these factors should lose in importance in the course of 1962—if, for instance, the profit position of enterprises again improves because the increase in wage costs per unit product becomes smaller with progress in productivity and rather

slower wage rises—the resulting fresh stimulus to private investment can hardly be expected to make itself felt in 1963.

Unlike investment by enterprises, public investment will remain buoyant and probably grow even faster than between 1961 and 1962. Only in the Federal Republic of Germany is there likely to be some slowdown following the restrictions imposed under the “Stabilization” Programme. Against this however, an even more significant increase should take place in Italy, where the large-scale projects to improve structures will now enter on the phase of implementation.

In addition, demand for housing will remain expansive in 1963. The restrictions on demand planned in the Federal Republic of Germany will practically not affect 1963, the more so as the carry-over of unfinished building was particularly high at the end of 1962. In France (especially because of the need to house repatriates from Algeria) and in Italy (thanks to probable increases in State aid) a speed-up may even be expected. Only in Belgium is there any possibility of a trend towards stagnation.

By and large, building investment should also grow more than in 1962 because the labour market situation will probably make it possible to step up numbers in the building industry. Assuming better weather, an additional factor should be the elimination of the handicaps which held up building activity in the first months of 1962 with adverse effects throughout the whole year.

The brighter outlook for building investments—considering the importance of this item in total gross fixed investment—justifies a forecast for the latter of a real increase of about 5 % between 1962 and 1963.

It is always very difficult to predict developments in investment in stocks. On the basis of probable trends in the world economic situation and also of the now less expansive prospects for internal demand, it can in any case be asserted that the movement of stocks will not boost total demand to any materially greater extent in 1963 than hitherto.

Consumption expenditure will again go up strongly in 1963, when it should be the decisive factor in economic growth.

First, public consumers' expenditure will go on rising, although probably in some member countries rather less strongly than between 1961 and 1962. This will be due chiefly to the fact that the wage and salary increases budgeted for in the public services will not be as considerable as in 1962. Real public consumption on the other hand will slow down its growth only slightly.

Private consumer expenditure will again go up quite appreciably, although a certain slowdown of expansion is to be expected in this important component of demand. First, the rise in average hourly earnings will be smaller; secondly, employment in terms

of total hours worked will hardly increase. The numbers employed will rise more slowly and hours worked probably decline a little. Nevertheless, the increase in mass incomes will remain considerable, the more so as further rises in transfer incomes are likely. In addition, the quieter prices anticipated will favour the expansion of real private consumption in comparison with 1962. The real growth rate might attain 4.8 %, as against 5.2 % between 1961 and 1962.

With this estimated development of demand, the growth of total supply would slow down somewhat. This does not, however, apply to domestic output in general.

Although industrial production (less building and the food and semi-luxuries sector) might rise somewhat less, it would nevertheless be about 5 % higher in 1963 as a whole than in 1962 (the rise was 6 % between 1961 and 1962). It will be particularly capital goods that will slow down, although relatively strong advances may still be expected in branches, like electrical engineering, specializing in the capital goods needed for rationalization. Against this, the development of internal demand will again favour the consumer goods industries, particularly those producing luxury durables. Thus, the output of the motor-car industry, into which the Commission's services have carried out a confidential special investigation in co-operation with experts from the industry, can in any case be expected to develop favourably in response to internal Community demand. On the other hand, output might continue to be anything but expansive in certain basic materials and semi-products, particularly iron and steel. Here, however, the determining factor will be the weakness of world markets rather than the development of domestic demand—which might on the contrary again liven up, although only to a slight extent.

For services, expansion between 1962 and 1963 will probably be at much the same pace as between 1961 and 1962. Assuming normal weather conditions for agricultural production and higher building output than in the previous year, the increase in the real total gross Community product between 1962 and 1963 should again reach 4.5 %.

As regards the employment situation in the Community, demographic forecasts for 1963 give roughly the same natural increase of working population as in the previous year. In Italy, the Netherlands and France it will again be considerable. Moreover in France repatriation from Algeria and the shorter military service will also contribute to raising the manpower potential over the whole year. In the Federal Republic of Germany, where no appreciable natural increase of the working population is to be expected, it will again be necessary, if production is to advance, to call in more foreign workers—even if on a smaller scale than in 1962. It is true that it will hardly be possible on the whole fully to meet the extra demand for labour, among other reasons because of the puny reserves of adequately trained and mobile manpower at present available. Nevertheless, the labour markets of some member countries, particularly the Netherlands and France, might prove slightly more comfortable.

A further increase in imports is to be expected in 1963. However, this will probably be smaller than in the previous year; after the relatively favourable 1962 harvests less farm products will be imported, and the expansion of total demand is tending to taper off.

Trade will probably again expand more vigorously among the member countries than with non-member countries. Growth might, however, also slacken somewhat, not only because of the slight slowdown in the expansion of demand but also because in Italy—one of the leading exporters of farm products—harvests were only middling, while in the other member countries they were better than in the previous year.

As already clear from the trend in the latter half of 1962, there might be a general tendency for prices to become more stable. Signs are not wanting that this will be the case; the return to normal of the supply in farm products; the absence of strain on many markets in goods; and the expectation of a slower growth in wage costs per unit product. Prices of services in general will, however, continue to rise, the more so as the tariffs of some public services are adjusted, with the usual time-lag, to the preceding sharp rises in wage costs.

Given the anticipated development of external trade, a further deterioration of the Community's trade balance is to be expected in 1963. However, it will not be as sharp as in the previous year. The balance of transactions should in any case continue to show a considerable surplus. Whether the reduction of this surplus will be reflected in the overall payments balance cannot be predicted, in view of the uncertainties as to capital movements.

C. Economic policy

As mentioned several times already, the forecasts of economic development in 1963 have been made on the basis of certain hypotheses concerning economic policy inside and outside the Community.

They rely particularly on conjunctural policy in leading non-member countries—above all the United States—maintaining adequate economic growth. Because of the relatively rapid expansion of its internal demand and thus of its imports—which have grown faster than exports—the Community has in contrast to pre-Community Europe for years been a stimulating factor in the world economy and will probably continue to be so in 1963. It is therefore desirable that it should be enabled to continue to increase its exports at an adequate rate. In practice this will largely depend on conjunctural developments in the non-member countries.

It is true that there would still be no danger of any recession in the Community, if the impulses from outside should be slightly recessive. For the effect of the present integration process in encouraging expansion in the Community is too strong, and the degree of independence from external economic fluctuations has probably increased substantially. And some components of internal demand, particularly private consumption, still contain ample growth potential of their own. Finally, public investment and consumer expenditure will continue to rise in virtual independence of the general economic trend.

But certain effects must be reckoned with in the case mentioned above—in particular a further trend for investment by enterprises to flag—which would entail an appreciable slackening of economic growth as a whole. This would mean that conjunctural policy in the Community would immediately be called upon to take special measures to buttress growth, particularly of course if—contrary to present expectations—very strong recessive influences invaded the Community from outside.

In order to be armed for any eventuality and in a position to keep internal demand expanding, the Economic Policy Committee has long been studying the available instruments of conjunctural policy : how they are to be used and where and how improved. In the light of these investigations and discussions the Commission, towards the end of 1962, sent recommendations to all member Governments. It is highly important that these be given immediate and the most careful possible consideration, so that even unexpected developments may be countered more promptly and effectively than seems possible at present.

No fresh monetary and credit or finance policy measures seem to be necessary to boost demand in the immediate future. As explained above, public finance is already

stimulating total demand, not least by virtue of the stabilizer effects of the slowing-down in the growth of incomes on the one hand, and the continuing vigorous expansion of expenditure on the other. In any case care must be taken that greater deficit financing does not make too many inroads on the possibilities, other than self-financing, available to enterprises for financing their investment.

In general, heed must be taken to see that money and capital markets develop favourably in relation to the needs of financing investment—and even that they positively encourage the propensity to invest. In any case member countries whose payments balance has worsened should not allow the full effects of this to react on liquidity, but should, so far as the price situation permits, take counter-measures to strengthen their own internal liquidity. In this connection the commercial banks should resort as little as possible to repatriation of their foreign exchange holdings or to borrowing abroad, since such operations tap off other countries' liquid and foreign exchange—which is hardly desirable whether from the standpoint of the international payments and exchange situation or from that of the world economy. In addition, there are of course relatively narrow limitations on such a method of supporting internal liquidity.

These considerations do not exclude the fact that in certain member countries price stabilization still demands a policy of curbing the expansion of internal demand in certain fields. It is true that, where they still exist, general credit restrictions will have to be gradually eased, since they particularly hamper private investment, which even without them is tending to weaken. But planned measures to curb building demand and bring it into line with supply possibilities are certainly still justified in some member countries, the more so as this is a market which can hardly be helped to any material extent by imports and in which excess demand immediately sets off price and wage rises which tend to snowball throughout the whole economy. In any event such restraints on demand must be carefully differentiated and harmonized with the availabilities of the various branches of building on the one hand, and with remoter needs—as revealed in the relevant long-term estimates of overall economic development—on the other. For instance, there would be little point in throttling back expenditure on road-building, first because capacities in the branch in general are adequate and the manpower requirement slight in view of the high standard of mechanization, and secondly because restrictive measures today may in a few years' time create bottlenecks in the economy which it will then not be possible to eliminate so rapidly.

In addition, curbs on expansion could be largely avoided in so far as the elasticity of supply can be enhanced. In the building sector it may be noted that there are still a number of ways of doing so—e.g. encouraging the modernization of building enterprises, greater use of winter building techniques, training schemes.

If it also appears advisable—at any rate in some member countries—to keep the development of consumer incomes within limits, this is not because private consumption as a factor in demand is tending to outstrip supply possibilities, but because of the effect

on costs of too rapid jumps in income : affecting prices and, where it is not possible to pass on increasing costs in the form of higher prices, squeezing profit margins and therefore, in some instances discouraging the propensity to invest.

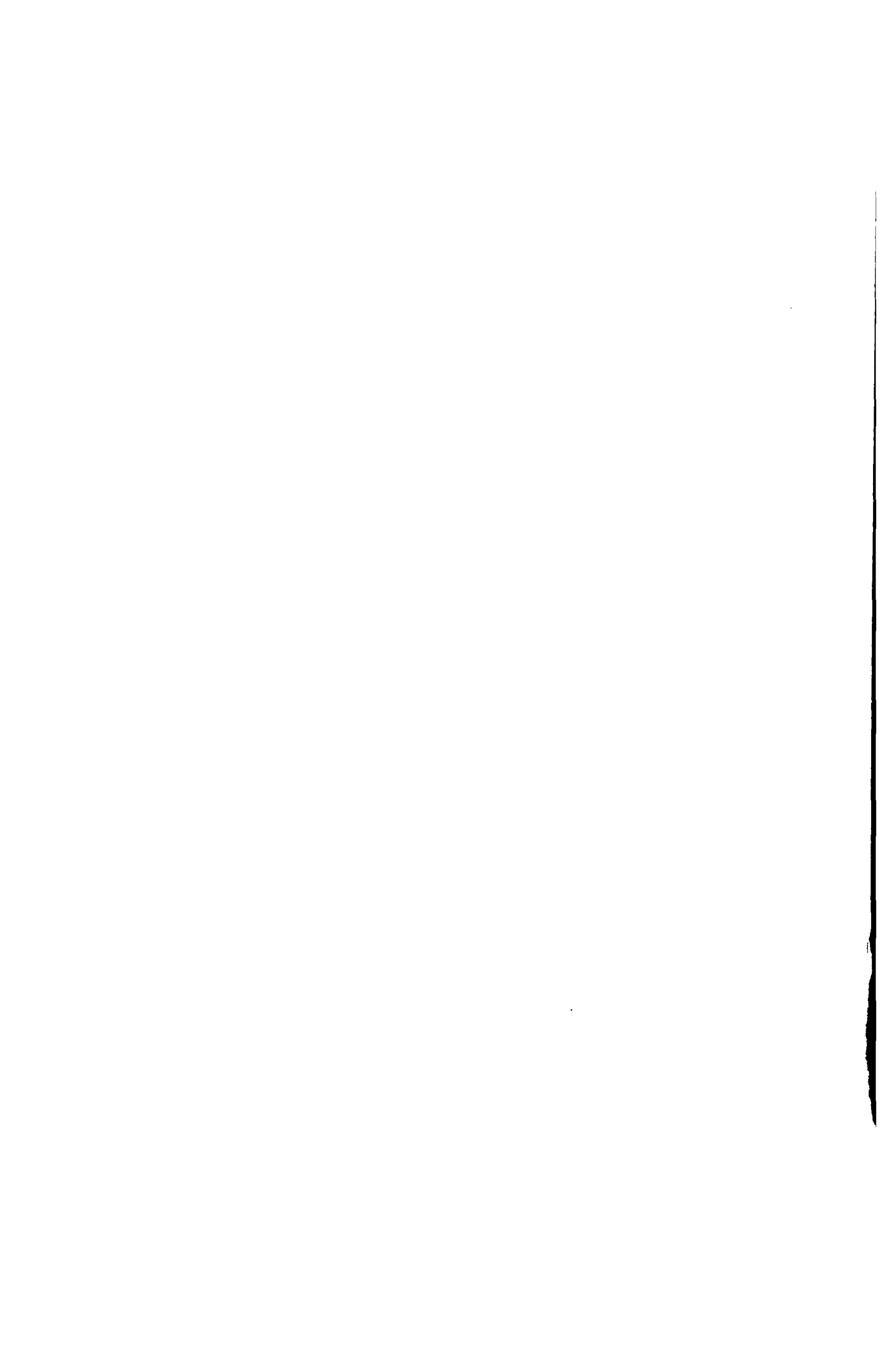
In these Surveys the Commission has several times expressed views on these problems and on the inferences to be drawn from them in the matter of conjunctural and income policies. Although, with more rapid productivity increases, somewhat slower wage rises, sluggish raw material prices and an easing of the tax burden, these problems should lose some of their edge in certain countries in 1963, they will in general continue to be present and even, in some countries, remain quite acute. In the longer term it would be quite on the cards that this costs trend could seriously jeopardize the ability of Community industries to compete with non-member countries.

It is therefore vital that the Governments should continue their endeavours to increase understanding by both sides of industry of the necessary conditions under which overall aims of price and growth policies for the economy can be attained. In so doing it will be necessary to keep in mind from the outset that success will only be possible if broad mutual agreement exists, and the wage policy is applied in the setting of a longer-term and comprehensive incomes policy which should be developed as quickly as possible, and finally, if other instruments are actually brought to bear to stabilize prices. No wages policy is possible without an efficient price policy.

As will be clear from the above remarks on economic policy, the Commission believes that global measures to restrict demand with a view to stabilizing prices should no longer be necessary in any member country. Moreover, as things now stand, such a policy could hardly serve such an end without gravely impairing real economic growth. But this is not to say that any other means of promoting price stability should not be employed. On the contrary, there is urgent need for (a) fresh tariff cuts, in particular anticipated reductions under Article 15 (2) of the EEC Treaty; (b) continuation of liberal trade policies towards the non-member countries, including the abolition of consumer taxes of equivalent effect to duties; (c) more active competition policy, including scrutiny of current practices in price-forming and fixing, elimination of restraints on competition and rationalization of trade channels; (d) further encouragement of labour mobility and vocational training in the Community. The member countries' payments balances and reserves are still strong enough to allay any fears as to the consequences of greater encouragement to imports.

Finally, it is again pointed out that the price policy decisions which, under the common agricultural policy, are to be made in the spring of 1963 in respect of important farm products will have a considerable bearing on the internal stability of currencies.

**II. THE SITUATION IN EACH
OF THE COMMUNITY COUNTRIES**



A. Federal Republic of Germany

In 1962 as a whole, expansion was again rather slower than in the year before. Real GNP seems to have gone up about 4 % and the index of industrial production 4-5 %. The corresponding increases in 1961 were 5.3 % and 6 %.

There are various reasons for this slackening of pace: in the first place, the extremely bad weather checked the growth of production in the early months of the year; secondly, the limited availability of additional labour, hindered the expansion of home supply; lastly demand had a more restraining influence than in 1961. In the course of the year there were definite signs of quieter conditions in business activity.

There were three main contributory factors: foreign demand rose only moderately, the propensity of enterprises to invest declined, and imports increased sharply.

Nevertheless, total demand again rose perceptibly. In particular, there was a considerable increase in private consumption—probably about 5.5 % in real terms. Gross capital investment also went up, though considerably less in real value than in 1961. The building market continues to show pronounced signs of excess demand.

The movement of wages in 1962 was of great importance for the economic trend. As the labour market remained extremely tight, the increase of wage costs per unit of output already noticed in 1961 continued, though at a slower pace. The rise in wages had a beneficial effect on the expansion of private consumer demand, and to this extent was a factor sustaining growth; but at the same time it damped down external demand and discouraged capital investment by firms.

Although prices continued to rise (but now less as a result of demand than of higher costs), the weakening of export and investment demand, together with increasing competition from imports, prevented price increases that would have completely offset the increase in costs.

The outlook for 1963 indicates that economic growth will continue, though a further slackening in exports must be reckoned with and the expansion of equipment investment will again slacken off. Building, however, should increase more sharply than in 1962, assuming normal weather. Private and public consumption in particular will continue to expand, but more slowly than in 1961. Once again the expansion of demand in general will be rather less than in the previous year.

Employment can scarcely increase any further in view of the continuing tightness of the labour market. Productivity will progress, however, and there is reason therefore to expect a 3.5 % - 4 % rise of industrial production; the real growth of GNP can be estimated at 3.5 %, given normal harvests. As imports will go up more slowly than in 1962, though certainly faster than exports, the surplus on current account will presumably decline a little further. The price level will again be slightly above that of the year before, but the rise will probably slow down perceptibly.

The main task of short-term economic policy will be to call a halt to the rise in costs. This will hardly be possible without an incomes policy, which should however also be the subject of an agreement in the context of short-term economic policy. The economic report to be published by the Federal Government at the beginning of 1963 might be a valuable aid for reaching agreement on this between the various groups concerned—particularly between the two sides of industry and between them and the Government.

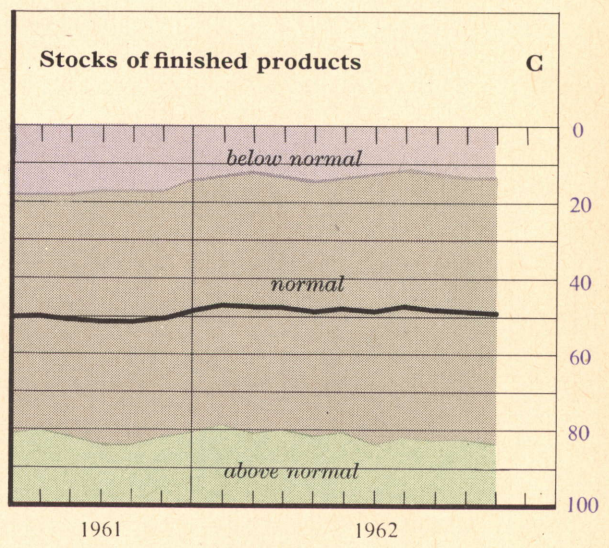
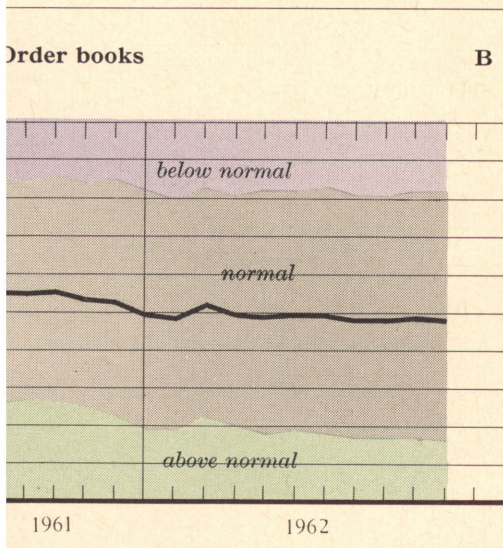
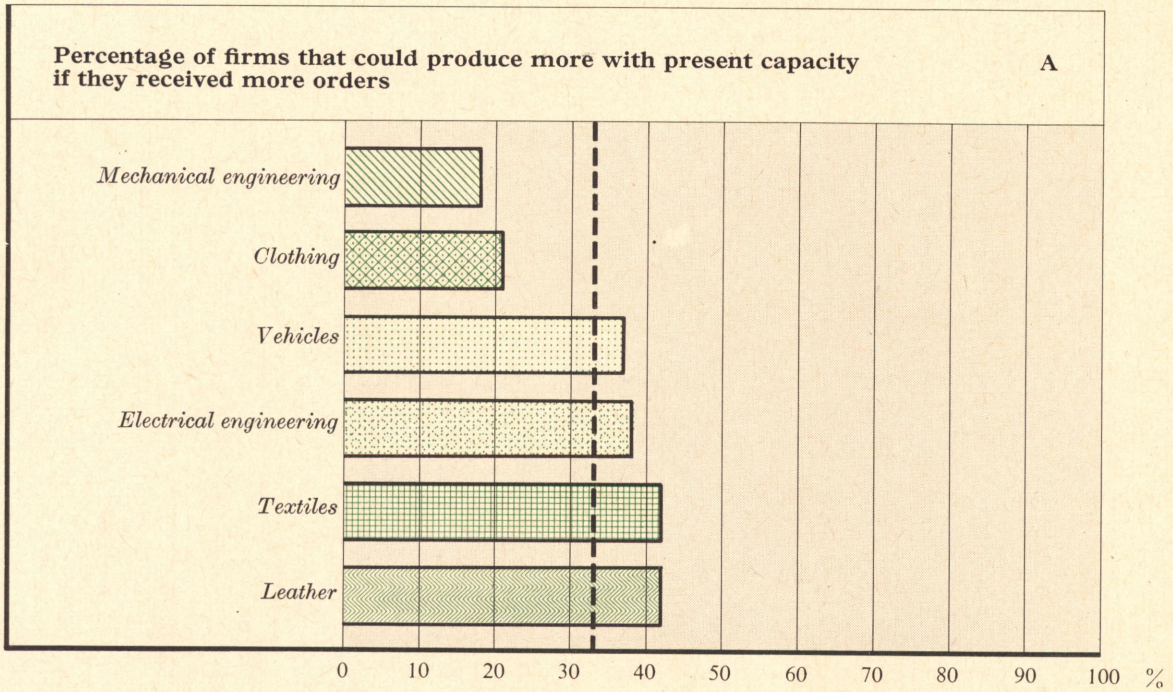
At the same time it will be advisable for those who direct short-term economic policy to be ready to combat in good time any excessive slowdown of investment.

1. Balance-sheet for 1962

The development of external demand, which even in the second half of 1961 had not provided much stimulus, remained very weak in 1962. The year-to-year growth rate of goods exports in the third quarter (3.3 % in value according to foreign trade statistics) was about the same as in the first two quarters (3.2 % and 3.0 %); over the whole year it should prove rather higher (October 8.6 %). Earnings from services, which went up only slightly in 1961, have been more favourable in 1962. Total exports of goods and services in terms of national accounting, i.e. including exports to West Berlin and the Soviet Zone of Germany, are therefore likely to have increased in 1962 by about the same volume as in 1961 (3.6 %).

The decline in the propensity of firms to invest already noted in 1961 continued in 1962 and was more and more reflected in a fall-off in the expansion of their actual capital expenditure. The increase of investments in equipment, to judge by the rate of expansion of sales of home-produced and imported capital goods, tapered off in the course of the year. The growth rate for the whole year at constant prices was probably between 4 % and 5 % (as against 11.7 % in 1961).

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION

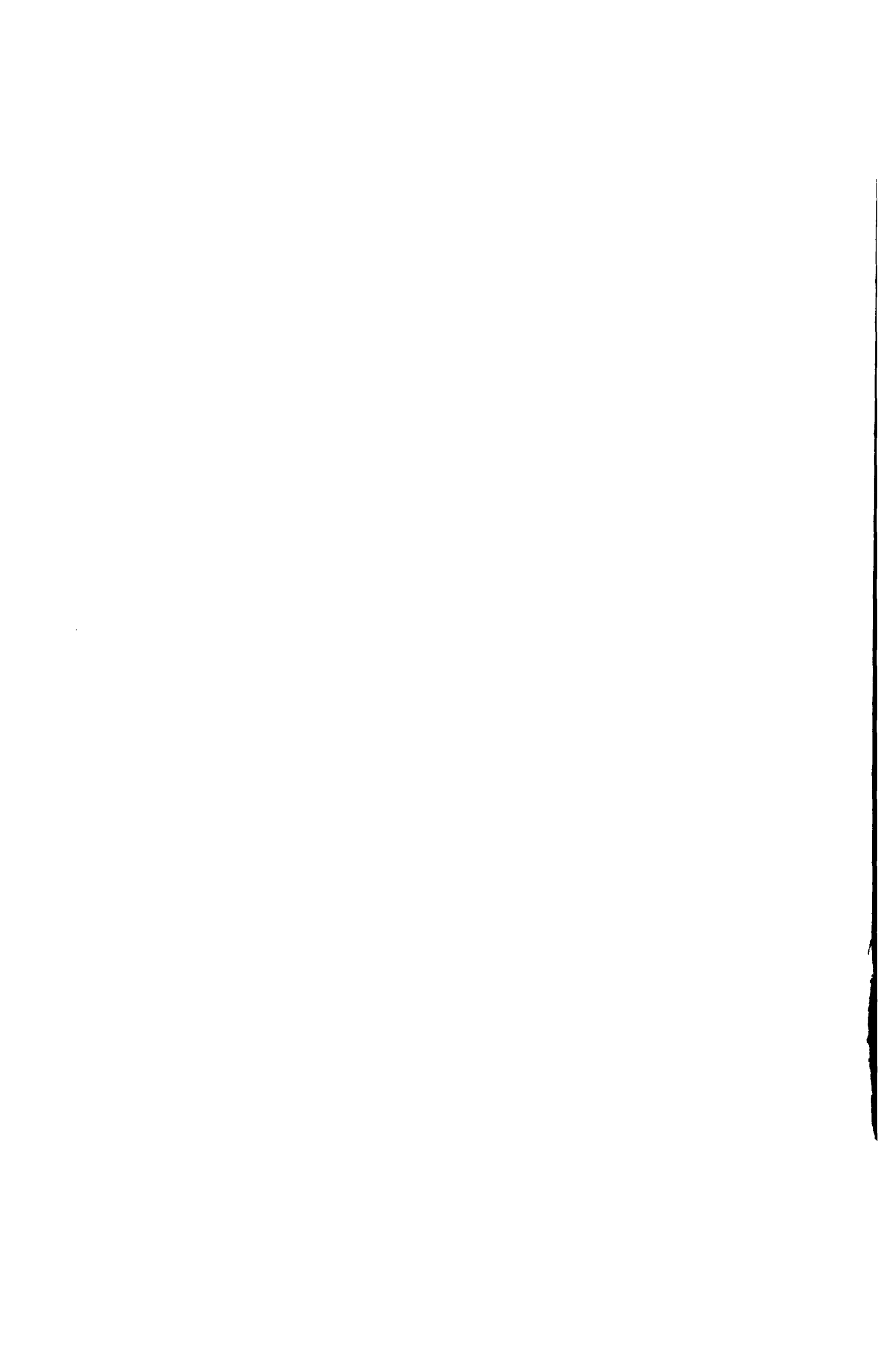


Answers to questions of the EEC business survey, carried out in the German Federal Republic by the IFO-Institut.
 Note: The following branches of industry are not yet included in the survey: chemicals, petroleum, metals.

GRAPH A: Answers to this question (from the survey made at the end of October 1962) are given for six branches of industry. The percentage for industry as a whole is shown by the dotted vertical line.

GRAPHS B and C: The three colours (green, grey and violet) show the percentages of the three different answers. The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows:

- by 0.03 for the answer "above normal";
- by 0.02 for the answer "normal";
- by 0.01 for the answer "below normal".



Building was still hampered by a shortage of labour, and was also hit by bad weather in the early months of the year. In the first quarter of 1962, production in the building industry proper was about 8.5 % below the corresponding level for 1961, whereas in the second quarter it was again about 8 % above and in the third quarter some 7.5 % above the 1961 level.

In the light of probable developments in the fourth quarter, it may be assumed that gross fixed investment in 1962 will have gone up in real terms by between 4 % and 5 %. The increase is therefore of the same order as was forecast by the Commission at the beginning of the year. In 1961 the increase was still 10.1 %.

Investment in stocks has not provided much fresh stimulus for economic activity in 1962. But in some important products—and this is particularly the case for steel—the rundown of stocks by the processing industries and trade seems to have halted. As a result of the boom in consumer expenditure, retailers have built up their stocks again.

Not only has public consumption increased substantially : the expansion of expenditure on private consumption was also very strong again in 1962, although in the second half of the year a certain tendency to slow down became evident. The year-to-year growth rate of retail trade turnover fell from 10 % in value and almost 6 % by volume in the first six months to 6.5 % in value and 2.5 % by volume in the third quarter, when, however, a particularly important part was played by consumer expenditure not included in retail trade statistics—particularly that connected with holiday traffic, which is increasing from year to year. In October the corresponding growth rates, partly owing to the Cuba crisis, recovered to 10 % and 7 % respectively. The overall increase of private consumption in 1962 will probably be between 5.5 % and 6 % in real terms (in 1961 it was 7.3 %).

The main reason for this vigorous expansion of private consumption, apart from a slight reduction in savings, was the continuing sharp rise in disposable household income. The level of wages under collective agreements in the third quarter was 8 % higher than in the third quarter of 1961; in the first six months of 1962 the growth rate was 9.7 %. Effective earnings went up even faster, although the difference between that increase and the increase of those under collective agreements will certainly not have been as big as in the two previous years. The wage and salary bill also went up because of the rise in the number of persons employed. Finally, transfer incomes also rose appreciably once more.

At the end of September the number in paid employment (21.3 million) was almost 2 % higher than the year before, mainly because of the recruitment of foreign labour. There were more than 700 000 foreign workers employed in the Federal Republic, as against some 540 000 at the end of September 1961. In spite of the rise in the numbers employed, tightness on the labour market continued almost unabated during the whole year, owing partly to shorter working hours. The number of vacancies reported at labour exchanges at the end of October (537 000) was still almost six times that of the unemployed.

Although the numbers employed in industry rose scarcely at all, industrial production in general made good progress. Productivity therefore improved considerably. In the first quarter, however, the year-to-year growth rate of industrial production⁽¹⁾ was only 1.7 % because of the very bad weather. But it moved up to more than 5 % in the second and third quarters and in October, and will probably be between 4 % and 5 % for the whole year (1961 : 6 %).

Agricultural production, which rose by only 0.5 % in 1961, showed a more marked increase in 1962. Not only did livestock products rise again, but harvests were also better (in some cases much better) than in 1961.

If the rise in services is also taken into account, there will be an increase in GNP in 1962 of some 4 % at constant prices (1961 : 5.3 %; 1960 : 8.8 %); this would coincide exactly with the Commission's estimate published in this report at the beginning of the year.

The expansion of imports continued at a faster pace in 1962. According to foreign trade statistics the value of goods imported was more than 10.5 % higher than in 1961 for the first ten months of the year. However, growth in the first half-year was faster than in the second, mainly because imports of farm produce went up very sharply until the middle of the year as a result of moderate harvests in 1961 and the introduction of the common agricultural policy. Whereas the trend of raw-material imports was rather slack on the whole, imports of finished goods again rose perceptibly. Once again, expenditure on services abroad also grew considerably in 1962. The overall volume of imports of goods and services in terms of national accounting, i.e. including imports from West Berlin and the Soviet Zone of Germany, will probably have increased by some 10 % in 1962 (8.4 % in 1961).

In spite of this vigorous growth of imports, prices continued to rise; however, the upward trend flattened out somewhat towards the end of the year, not least because of a drop in farm prices and increasing foreign competition. In September agricultural producer prices were the same as in September 1961, while in the middle of the year they had been almost 6 % above the 1961 level. Industrial producer prices in September were 1.2 % above the 1961 level. Prices of capital goods and consumer goods, however, rose more markedly (4.2 % and 2.4 % respectively). The return to normal food prices finally caused the consumer price level to become steadier in the course of the year. In October the cost-of-living index was only 2.9 % higher than in the same month of 1961, as against 4 % in June.

The rise of imports—sharp in comparison with that of exports—led to a distinct reduction of the surplus on trade in goods and services. According to balance-of-payments

⁽¹⁾ According to the index of the Federal Statistical Office (output per working day).

statistics ⁽¹⁾ the balance on current account, which includes unrequited payments, fell from a surplus of DM 2 900 million over the first nine months of 1961 to a deficit of almost DM 1 000 million in the corresponding months of 1962. The balance of trade alone over the same period of 1962 showed a surplus of only DM 2 500 million (1961 : DM 5 300 million). In the third quarter alone, the surplus was barely DM 1 000 million (DM 1 700 million in the third quarter of 1961). While the gold and foreign-currency reserves of the banking system (Bundesbank and other banks) in the first nine months of 1961 had fallen by about DM 200 million, in the corresponding period of 1962 they rose by DM 700 million in spite of the deficit on current account. The balance of capital movements, including "residual items", was therefore favourable at almost DM 1 700 million, as against a deficit of DM 3 100 million in the first nine months of 1961. Extraordinary Government payments to abroad, however, in the first nine months of 1961 amounted to DM 5 100 million, whereas in the same period of 1962 extraordinary transactions showed a surplus of DM 400 million. Leaving aside extraordinary payments, therefore, the balance of payments deteriorated considerably. Foreign trade in the first half of 1962 had a much less expansive effect on domestic liquidity than in 1961, when more capital exports were financed from sources other than the internal monetary flow (special payments by the Federal Government). Consequently, although the public authorities' internally effective cash surpluses dwindled, bank liquidity came under some pressure, which the Bundesbank did not counter by credit-easing measures as it had done in 1961. The banks therefore had greater recourse to their internal liquidity reserves and were more sparing in the grant of short-term credits to trade and industry. On the other hand, many more medium- and long-term advances were made in 1962.

2. Outlook for 1963

The calmer tempo which became increasingly evident in 1962, is likely to continue in 1963, with consequently improved prospects for balanced economic growth. Production and incomes will rise again, but there is much to suggest a further slight decline in the pace of growth and a more marked differentiation of development from sector to sector.

Exports are again likely to expand less than in the previous year, since the growth prospects—particularly as regards investment—in many importing countries are not particularly favourable and Germany's competitive position on world markets has deteriorated in certain sectors because of the revaluation and the relatively rapid rise in costs.

⁽¹⁾ The balance of payments has not been adjusted by the amount resulting from the inclusion in foreign trade statistics of goods held in bond (first quarter 1962 : DM 411 million, second quarter 1962 : DM 54 million).

The situation as regards new orders from abroad in recent months points in this direction. In the third quarter new orders were 1.3 % below the corresponding level of 1961 and almost 7 % below export sales over the same period. However, there are still a good number of foreign orders in hand, although the EEC business survey suggests that businessmen were less optimistic on this point than they had been at the beginning of the year. Furthermore, if the expansion of internal demand continues to slacken, industry may exert itself more to penetrate export markets than it did in the years of domestic boom. Lastly, some influence on exports could be exerted by German aid to developing countries, which is mainly tied to specific projects. If a further rise in earnings from services is taken into account, an increase of about 3 % in the volume of exports of goods and services (as defined in terms of national accounting) can be forecast for 1963.

The growth of equipment investment, which was much slower in 1962, is likely to fall off still more in 1963. Industrial investment is at present relatively weak, despite the fact that in recent months the profit situation does not seem to have deteriorated as much as formerly. New home orders for capital goods in the third quarter of 1962 were only 1 % above the third quarter of 1961 and more than 6 % below domestic sales over the same period. In engineering alone, domestic orders received were 1.4 % less than in the year before and 9 % less than turnover during the same period. The number of permits granted for industrial and commercial building hardly indicates that the propensity to invest is growing : in the third quarter they were 3.6 % below the figure for the same period of 1961, in terms of space enclosed.

However, total building investment in 1963 is likely to increase to a considerable extent—probably even more than in 1962. True, housing permits in the third quarter of 1962 were only slightly higher than in 1961, in terms of space enclosed, but the backlog of unfinished projects from the previous year (more than 800 000 houses at the end of the year) itself ensures the full use of building capacity. In addition, public building will probably increase again: in spite of restrictive measures, permits issued for public buildings in the third quarter of 1962 were 10.5 % by volume above the 1961 level. A further expansion of building in connection with transport—particularly road works—can be expected in 1963.

Provided that building is not held up by abnormal weather, the increase of total gross fixed investment at constant prices may, despite the assumed slower growth of equipment investment, be about the same in 1963 as in 1962, i.e. between 4 and 5 %.

In spite of various efforts to check the expansion in spending, expenditure on public consumption in the coming year will again rise appreciably—at any rate more substantially than the real GNP.

Expenditure on private consumption in 1963 will again go up appreciably. Disposable household incomes will continue to rise, though probably not as rapidly as in 1962. The trade unions are still making high wage claims, but on the employers' side

resistance has evidently hardened. The salaries of federal civil servants have been effectively raised by 5 % - 6 % from 1 January 1963. Transfer incomes will also increase substantially, particularly if the "Sozialpaket"—a body of legislation intended to better the lot of the workers—should be put through Parliament in the course of the year. In national insurance, existing pensions have been increased by 6.6 % with effect from 1 January 1963; the future pensions, calculated on a new basis, will go up even more (over 8 %).

Despite some easing of the situation, there can be little expectation that the labour market will return to normal in 1963, particularly as the natural population trend (despite an estimated rise of more than 40 000 in the number of school-leavers) will result in a drop in the number of persons employed, and average working hours will probably be reduced still further. The difficulty in recruiting supplementary foreign labour will in all likelihood increase, since manpower reserves are becoming more and more exhausted even abroad—at least in neighbouring countries. The increase in the number of wage-earners is likely therefore to be fractional—less than 1 %.

The growth of output will therefore depend mainly on higher productivity. Total industrial production may go up 3.5 % to 4 %. The growth-rate of real GNP will probably be nearer 3.5 %.

The expansion of imports will continue, but presumably at a much slower pace than in 1962, if only because the better harvests of 1962 will doubtless keep farm imports in the first half of 1963 below the level for the corresponding period of 1962. However, the surplus on foreign transactions is again expected to shrink—though not as much as in 1962.

Although the general outlook thus points to a further slowdown in the growth of demand, and a more satisfactory market equilibrium than in recent years, prices will still go up slightly in 1963. The increases will mainly be accounted for by costs—except in building—and for the most part will represent only the after effects of the recent boom in demand. This also means that they virtually cannot be combated by general measures to restrain demand, which in certain circumstances might even aggravate the rise in costs, since they are likely to result in a lower utilization of productive capacity. The control of demand will have to be differentiated according to the state of imbalance of the markets in sectors where demand is strongest.

The stabilization programme announced by the Federal Government in the Bundestag on 9 October 1962 is intended to take this into account: in the first place, it provides for measures (such as suspension of tax concessions) to put a brake on the expansion of demand in building; secondly, it aims at ensuring that total federal expenditure in 1963 will rise only by about the same percentage as real GNP, by keeping a tight rein on public consumption and building expenditure in particular.

In fact, however, Government spending will rise more sharply than the real GNP, since a number of additional items of expenditure already seem to be regarded as unavoidable. It is all the more necessary, therefore, that care must be taken to see that additional public expenditure does not cause a heavy increase in demand in the very sectors in which further strain is to be expected—particularly building. This calls for better co-ordination of spending between public authorities, based possibly on an economic budget.

If there is to be some falling-off in demand, it will probably occur mainly in the equipment investment of firms. Economic and financial policy should avoid everything that might impede industrial investment—particularly the financing of investments. This applies also to credit and interest-rate policy, which should, where possible, counter any tendency towards dearer money.

Here considerable significance also attaches to wages policy, the scope for which is to be indicated in the economic report for 1963 announced by the Federal Government; the report will also show what opportunities exist to cope with the demands made by the various sectors of the population and the Government on the GNP. An attempt should be made in discussions between interested circles and the Government on this economic report (which practically constitutes an economic budget) to ensure that the rise of wage costs per unit of output does not persist indefinitely.

It will then be possible, and indeed essential, for the Government to intensify its efforts in competition and price policies and exert more influence on the incomes of persons not in paid employment. Certain measures to encourage competition are announced in the stabilization programme; they should be put into effect as quickly as possible. In addition, however, the rise in prices can be effectively combated by steps to increase supply by way of imports : this can be done mainly by means of the Rome Treaty's provisions for voluntary advance tariff cuts on imports from other Member States. It need not be stressed that measures (such as increases in turnover equalization tax) which have the same effect as increased customs duties and therefore react on prices are incompatible with the requirements of short-term economic policy and price policy for the coming year.

B. France

Economic growth has been somewhat faster in 1962. To judge by the INSEE index, industrial production was most likely up about 7 % over 1961 and, since agricultural output picked up again, the national product may have risen about 5 %, as against 4.4 % between 1960 and 1961.

External demand contributed only very little to this expansion. As a result of the political and economic situation in North Africa, exports of goods and services for the whole year were no more than about 3 % higher in value than in 1961. The decisive impulse came from internal demand—in the first half-year still mainly from investment, but increasingly from private consumers' expenditure in the second. There was a substantial rise in private household incomes, not least as a result of sharp wage increases, subsistence grants to Algerian repatriates, and certain capital transfers from Algeria.

Nevertheless, the expansion of real private consumption was again adversely affected by rising prices: the annual average cost of living was probably up a good 4 % over 1961.

As imports of goods and services advanced more strongly than exports, there was a fall in the surplus on external account (in national accounts terms). On the other hand, the current payments balance for the franc area as a whole with countries outside probably showed a surplus of about the same order of magnitude as in 1961. Despite higher public exports of capital, the gold and foreign exchange reserves of the monetary authorities went up a further 677 million dollars in the first ten months of 1962.

The upswing can be expected to continue in 1963. Industrial output might rise by about 6 % or 7 % and the real gross national product by about 5 %.

In fact external demand is expected to provide somewhat greater stimulus all round than in 1962—particularly in the event of a gradual return to normal in the North African economy. The growth of capital investment should only slow down a little: businessmen will probably still show a comparatively high propensity to invest, public spending particularly on construction will again increase sharply, and, finally, house building is likely to expand faster to provide accommodation for persons repatriated from Algeria. Private consumption will no doubt also continue to follow

a vigorous upward trend, since consumer incomes will again grow very appreciably as a result of increasing employment, rising salaries and wages and larger social benefits.

As and when trade relations with the franc area revert to normal the surplus on the external account should again increase. However, there might be a slight fall in the high surpluses on the balance of payments with countries outside the franc area.

Prices will probably continue to climb in 1963, with rising trends to be expected mainly in services and building. But for industrial products also the upward trend seems to be continuing. It is favoured by the relatively sturdy growth of consumer income, which will probably again exert some pull on unit costs.

In view of this prospect, overall measures to stimulate the economy are scarcely called for. The more important task of economic policy seems to be to keep the upward push of incomes within limits compatible with balanced economic growth. At the same time care should be taken that the expansion of productive investment does not slow down too much.

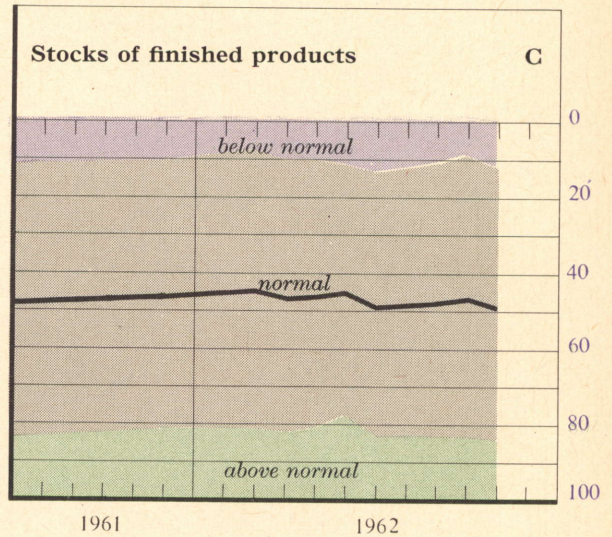
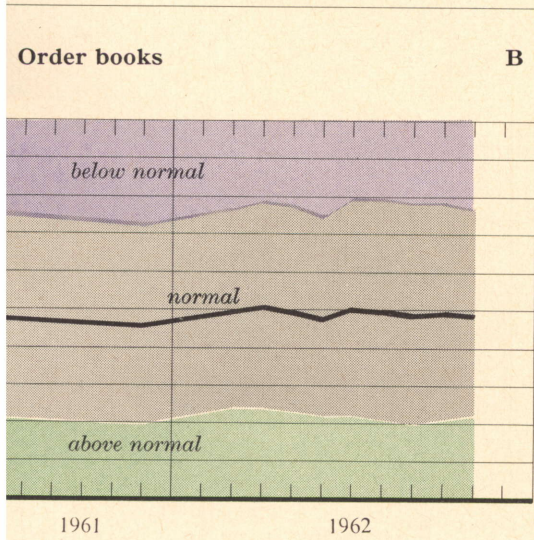
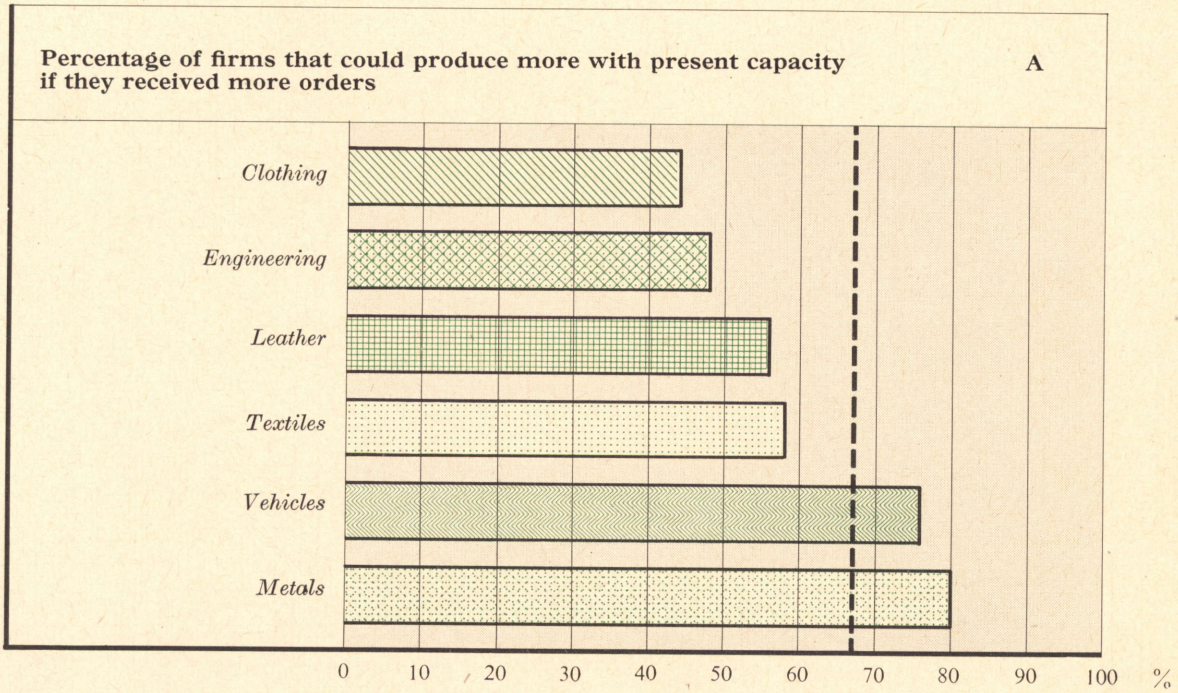
1. Balance-sheet for 1962

There was a clear shift in the pattern of growth factors in 1962 as overall demand quickened.

External demand for goods and services practically ceased to provide any new stimulus after the spring. Exports of goods (as defined in customs statistics) sometimes even showed a slight tendency to sag. While the growth rate in the first quarter—in terms of value—had been + 6.1 %, exports in the second quarter just equalled the corresponding level a year ago and in the third quarter fell 2.7 % short of it. Even assuming that they picked up somewhat in the fourth quarter, the figure for the full year is not likely to be more than about 2.5 % higher than in 1961.

The modesty of this overall result is however solely attributable to the steep drop (more than 20 %) in deliveries to the franc area, caused chiefly by the political events in Algeria and the precarious economic situation of Tunisia and Morocco. Exports to countries outside the franc area on the other hand probably achieved almost the same high average growth rate as in the previous year (+ 11 %), although they clearly flattened out during the summer months.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION

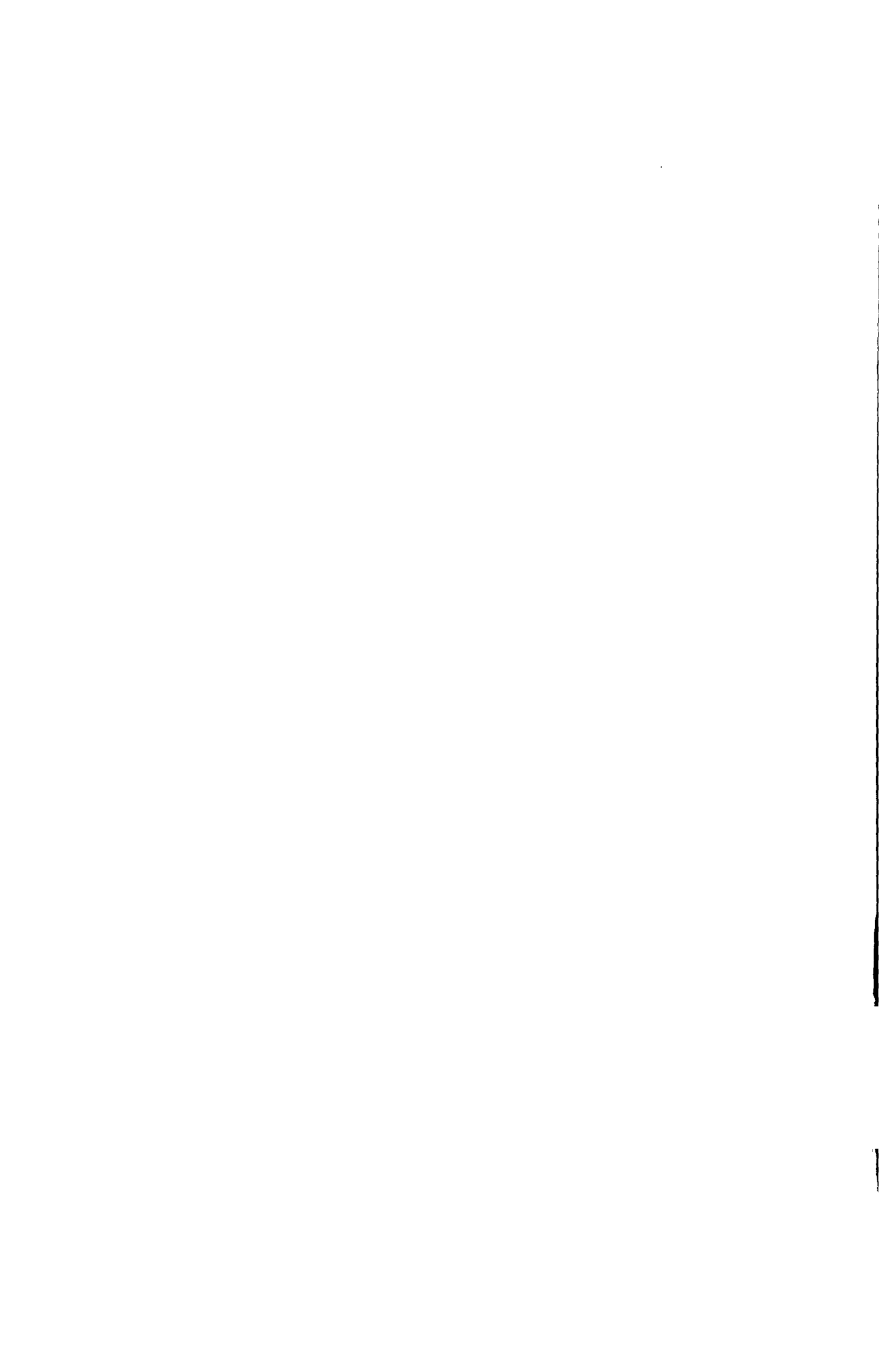


Answers to questions of the EEC business survey, carried out in France by INSEE.

GRAPH A : Answers to this question (from the survey made at the end of October 1962) are given for six branches of industry. The percentage for industry as a whole is shown by the dotted vertical line.

GRAPHS B and C : The three colours (green, grey and violet) show the percentages of the three different answers. The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

- by 0.03 for the answer "above normal";
- by 0.02 for the answer "normal";
- by 0.01 for the answer "below normal".



Exports of services also weakened as compared with 1961. The decisive factor here was undoubtedly the effects of the North African situation, while foreign exchange earnings, particularly from transport, insurance and tourism, probably again forged ahead very strongly.

On the whole exports of goods and services—in national accounts terms, including factor income from abroad—will probably only show a growth rate of barely 3 % in value and of about 2.5 % by volume in 1962 (1961: 5.8 % and 5.4 % respectively).

The higher output and employment were almost wholly attributable to internal demand. The annual average growth rate of fixed investment and of public and private consumers' expenditure was practically the same. In the course of the year, however, the emphasis gradually shifted from investment to consumption.

Nevertheless, the growth of capital investment by enterprises slowed down less than was at first feared in many quarters. The nominal growth rate will probably reach about 10 %, as against 11.5 % in 1961. Not only did incentives continue to be adequate, in particular for rationalization investments, but finance was also relatively easy to come by. The economy as a whole seems to have been able to offset part of the load imposed upon it by the spurt in wages by stepping up productivity or saving on other costs, and in some cases by passing it on in the form of higher prices to the consumer. Non-distributed profits of both self-employed persons and corporations definitely rose again, after slipping backwards in 1961. Enterprises should therefore have been in a position to finance a rather greater share of investment from their own resources.

Public investment also expanded slightly more slowly in 1962, although the annual average growth-rate remained relatively high at about 12 % (1961: 15 %). On the other hand, expenditure on house building rose faster than a year ago. Sundry improved incentives offered by the Government and above all the extra demand from people returning from Algeria, may well have given a substantial boost in the latter half-year.

All in all, gross capital investment, with a nominal growth-rate in 1962 of about 10 %, probably increased at almost the same speed as in the previous year (10.5 %). As a result of a sharper rise in prices for equipment and especially for buildings, the growth in volume will, however, have been somewhat smaller (6.5 % to 7 %) than in 1961, when it was 8 %.

Investment in stocks gave a lift to the economy, particularly in the second half-year. On the one hand more plentiful supplies on certain agricultural markets led to greater stocking, while on the other livelier industrial activity meant more work in progress. But raw material stocks should not have risen greatly, and under the pressure of heavy consumer demand, stocks of finished goods in industry and commerce probably even showed a slight downward tendency.

Expenditure on private consumption actually increased a little faster in 1962: it was probably about 10 % higher than the year before (1961: + 9.0 %). As in 1961 the increase in volume was about 5.5 %. The extra demand was chiefly for motor vehicles (new registrations were up 23 % in the first half-year and 30 % in the third quarter) furniture, household appliances and services. Against this the rise in expenditure on food and clothing was below average. A sizeable rise in consumption was doubtless triggered off by the massive repatriation, which began in the second quarter, of Europeans from Algeria—over 600 000 or 1.3 % of the total population—who spent not only their subsistence grants from the State but some of the funds they had brought with them. Later in the year the speedier rise of other disposable household incomes as well was reflected in increased consumer expenditure. With hourly wages and employment rising faster than in the previous year, wage and salary incomes were probably up about 11 % on 1961. In addition, various social security benefits, in particular family allowances, were raised several times during the year. Finally, drawings of self-employed persons and income from property of wage and salary earners again rose, although rather more slowly. On the whole, with a comparatively smaller burden of direct taxes and social security contributions, private individuals probably had nearly 11 % more spending money available in 1962 than in 1961.

The rise in public consumption was also somewhat faster over the whole year, owing mainly to the sharp increase in wages and salaries. On average, public consumer expenditure probably went up by about 11 % (1961: 10.1 %) although the increase by volume was smaller than in the previous year (about 3 %, as against 4.7 % in 1961).

Supply did not advance as strongly as demand, but here too the pace was somewhat faster than in 1961. Despite very unfavourable weather conditions at times, total agricultural output was up a good 5 % on the relatively low level of the previous year. Harvests, however, varied greatly: they were outstandingly good only for wheat and wine, middling for fodder grains, and bad—particularly in the first six months—for fruit and vegetables. For livestock products also the growth-rate was small compared with 1961.

Industrial production showed a notably strong and steady growth throughout the whole year. According to the INSEE index, it was 7 % above the corresponding 1961 level in the first half-year and 8 % in the third quarter. Since the EEC business survey shows that output is expected to shape fairly well in the fourth quarter also, everything points to a year-to-year growth-rate for 1962 as a whole of about 7 % (1961: 5.7 %). Most branches have made their contribution to this expansion, with motor vehicles, petroleum refining and chemicals in the lead. The growth of output in the capital goods sector was by comparison smaller. In the first six months this was attributable mainly to capacity bottlenecks and manpower shortages, while in the second it was also due to some extent to firms adapting themselves to the sometimes rather hesitant inflow of new

orders. Developments in coal mining and iron and steel continued unsatisfactorily, although signs of improvement were discernible in the summer months. The loss of markets in North Africa made itself felt in textiles.

Building output in 1962 was probably up about 5.5 %—a somewhat smaller increase than in 1961. There was a further sharp rise in public building, which probably even gathered speed in the second half of the year under the influence of low-cost housing schemes—but building on private account definitely slackened.

The services industry stepped up supply to a noteworthy extent, mainly because a bigger share of rising consumer expenditure was allocated to it.

On the whole the real gross national product may have grown about 5 % in 1962, as against 4.4 % in 1961. Once again higher productivity was a decisive growth factor.

Employment, however, also went up rather more than in the previous year. The number of hours worked was practically the same as in 1961, but there was a marked increase in the number of persons employed—about 1.5 % on a full-year average in industry and commerce, as compared with only 0.7 % in 1961. In the first half of the year this was mainly a result of the natural growth of the working population and the greatly increased recruitment of foreign workers; in the second six months, shorter military service and Europeans repatriated from Algeria also played a part. Despite all this, labour shortages continued to be fairly severe in important branches, even though the statistical picture of the labour market changed completely in the autumn. The registration of the Algerian repatriates led to a big jump in the number of persons seeking jobs, which until then had been falling almost continuously, while the increase in vacancies slowed down noticeably.

After a very hesitant start during the early months, imports of goods and services went up strongly as the year advanced. The volume of goods imported, reckoned on the basis of foreign trade returns and weighted for ascertainment errors, showed a growth rate of 7.5 % in the first half-year and about 16 % in the third quarter. Taking into consideration the development expected in the fourth quarter the annual average should thus show a higher increase than in 1961 (8 %). The structure of these imports has somewhat altered, however: whereas the proportion of foodstuffs to total imports rose very considerably owing to what was in some cases inadequate domestic output, and the share of finished goods rose sharply, raw material imports declined further, proportionately.

Although the events in Algeria probably prevented imports of services from rising as strongly as in the previous year, total imports of goods and services—in national accounts terms and including income payments to abroad—probably expanded at a rather higher rate than in 1961 (6.9 %).

Despite the powerful increase in total supply, prices continued to rise. Bad weather conditions, combined with the effect of agricultural policy measures and other administrative action, contributed notably to the steady rise in the cost of living, which was about 1 % a quarter or an annual average of more than 4 %, but a further factor was that the market situation was favourable for passing on rising costs or widening profit margins. In October 1962 food prices were 5.5 % higher, industrial consumer goods about 3 %, and services 5 %, than for the same period in 1961. Investment goods and especially building prices also rose more sharply than in the previous year.

As imports of goods and services increased much more than exports, the surplus on external account—in national accounts terms and at 1961 prices—dwindled very considerably—from 3 100 million NF to 1 000 million NF. At current prices the decline was almost as marked. The terms of trade developed only slightly more favourable than in 1961.

On the other hand, the payments balance, which does not cover all dealings in goods and services but only operations with countries outside the franc area, will probably close in the current account, including unrequited services with a surplus roughly as high as in 1961 (\$ 928 million). However, the result in the second half-year might have been less favourable than in the first, which, at \$ 483 million, had an even larger surplus than a year ago.

The rise in the net foreign exchange holdings of the monetary authorities, running at more than \$ 1 000 million in 1961, will however probably have been somewhat smaller in 1962. Net private capital imports definitely slackened, while higher debt pre-payments were a feature of public capital exports. The official gold and foreign exchange reserves rose by \$ 677 million in the first ten months of 1962, compared with \$ 759 million in the corresponding period of the previous year. Total reserves at the end of October were over \$ 3 600 million.

The net inflow of foreign exchange and the probably very heavy repatriation of funds from the franc area considerably added to the liquidity of the money and capital markets in the course of the year. Furthermore, cash operations by the Treasury, after showing a surplus in the first quarter, had a rapidly growing deficit, mainly as a result of subsistence grants to repatriates from Algeria. This deficit was already over 4 800 million NF at the end of August—without counting debt re-payments—compared with only 2 100 million at the end of August 1961. Contrary to what happened in the two previous budget years it must therefore be expected that the estimated budget deficit—again about 7 000 million NF—will in fact occur. So far this year the Treasury has made considerable calls on the Bank of France to finance this surplus expenditure, leaving the capital market to enterprises and public authorities. Issues were on a larger scale in the first ten months of 1962 than in the corresponding period of 1961. In addition, borrowing from the commercial banks by industry increased very strongly.

2. Outlook for 1963

Everything points to 1963 as being another year of expansion for the French economy.

On the whole foreign demand is likely to stimulate output and employment rather more than was the case in 1962. The volume of exports of goods and services—in national accounts terms—could well increase by about 4 % to 5 %, compared with 2.5 % between 1961 and 1962. However, this slight recovery would be attributable solely to the expected development of exports to the franc area: these should no longer act as a brake, at any rate when the year is viewed as a whole. If the economic situation in Algeria returns progressively to normal, some degree of recovery is possible compared with 1962. Against this, however, the none too brilliant business outlook in certain leading industrial countries, and the limited foreign exchange availabilities of the primary producer countries, throw a rather less rosy light on prospects for enlarged sales of French products outside the franc area. In trade with these countries a repetition of the high 1962 growth rate will hardly be feasible.

Internal demand will continue to rise briskly. Capital investment should on the whole lose only a little momentum. It is true that investment plans in private industry for 1963 seem at the moment to lack boldness, although the pressure on enterprises to offset rising costs by rationalization investments, and thus keep competitive, continues to be very strong, and although the sales outlook in a few branches producing mainly consumer goods might engender efforts to step up capacity. On the other hand, the programmes drawn up by public undertakings already make it possible to predict an appreciable increase in their investment outlay.

Housing construction will be given a fillip by the need to find accommodation for persons returning from Algeria. The number of building permits shot up already in the latter half of 1962. Finally, as direct investment by the State will also increase somewhat faster than hitherto, the nominal growth rate of gross capital investment can, by and large, certainly—in spite of one or two signs of weakness in investment projects by private enterprises—be expected to be only slightly lower than in 1962. The actual growth in real terms may well be of the order of 6 % (1962: 6.5 - 7 % approximately).

Private consumption will again rise substantially: by volume at about the same rate as between 1961 and 1962 (5.5 %). In fact the growth of private individuals' disposable incomes is unlikely to slacken. There must, of course, be expected to be a slower increase in grants to repatriates from Algeria, but incomes of employed persons should again climb appreciably as a result of further wage rises and the expected expansion of employment. In addition, notable improvements in social security benefits have already been decided for 1963. Finally, the self-employed, especially farmers, might well consume a somewhat greater share of their income than in 1962.

Public consumption will probably expand less vigorously than between 1961 and 1962. True, purchases of goods are likely to give another slight spurt, but the changed structure of outlay on wages and salaries resulting from the return of officials and employees from Algeria will begin to have its full effect. The real growth rate might therefore fall in the year-to-year comparison from 3 % in 1962 to about 1 % in 1963.

With this outlook for demand it can be expected that industrial production will again rise—at a year-to-year rate of 6 % to 7 % over 1962. This is all the more on the cards as strains in the labour market, which were still a prominent feature in 1962 and which, according to entrepreneurs, hampered the optimum use of available technical capacity in important branches, will probably increasingly tend to ease. In fact the natural growth of population and shorter military service are likely to result in a marked rise in the civilian labour force—already swollen by the repatriates from Algeria. As against this, however, there might be a fall in the employment rate mainly due to the higher school-leaving age and earlier retirement and, for the first time, a sizeable shortening of working hours.

Taking into consideration the possible increase in agricultural output, given normal weather conditions and the steady expansion to be expected in the services sector, the gross national product could increase by about 5 % between 1962 and 1963.

Imports should also rise further. The increase will, it is true, be adversely affected by the notable reduction in purchases of farm products, but higher imports of industrial products are to be expected, so that total imports of goods could therefore probably grow 7 % by volume. However, since in the year-to-year comparison imports of services will decline as a result of the altered situation in Algeria, the volume of total imports of goods and services in national accounts terms will probably only rise by about 3 %.

The price level will be up again in 1963. As the EEC business survey shows, entrepreneurs at the end of 1962 felt in any case as strongly as they had done at the end of 1961 that prices would continue to rise. In addition, tariffs for public services (gas, electricity, transport), which had been held down in 1962, must be expected to rise in 1963. Finally, rents might go up more quickly, as a result both of administrative decisions and higher building costs. On the other hand assuming normal weather the cost of food should hardly exert any upward push on prices during the year.

The current payments balance will probably continue to show quite high surpluses, although with some tendency to decline.

On the whole therefore the French economy still seems sufficiently buoyant, so that general measures to stimulate it would appear neither necessary nor opportune. Nevertheless, those responsible for short-term economic policy would be well advised to keep the structure of expanding demand under review: on the one hand, the fact should be

borne in mind that private consumer expenditure is tending possibly to expand too fast, and that this is due to a development of income exerting an upward pressure on unit costs; on the other, one or two signs that investment by enterprises may nevertheless be flagging should be noted.

Precisely because it affects costs, the first of these phenomena in particular might warrant some anxiety, the more so as the way demand is shaping permits certain price increases. Great importance therefore attaches to income policy. An agreement to harmonize competing claims of various population groups for shares in the growing national product should therefore be an aim of income policy, not only in the longer term, but also in the short run for the current year or the year immediately following. It must be admitted however that income policy is fraught with great difficulties, mainly statistical. The first steps in this direction—the 1962 “Autumn rendez-vous”—proved this clearly. However, there seem to be good auguries of success in the rather longer view.

In connection with income policy it will also be necessary to give some attention to saving by private individuals, not only because it provides an essential point of leverage for adjusting the distribution of incomes and wealth but because, in the short run, increased savings could at the present cyclical phase combat rising consumer prices and at the same time help to finance investment. If advantage is also taken of the possibilities of increased supplies afforded by external trade—in particular by advance tariff reductions—and if the rationalization of distribution circuits is also energetically pursued, the prospects for greater price stability should vastly improve.

C. Italy

Economic expansion continued in 1962. The growth rates from 1961 to 1962 were again appreciable and again higher than in the other Member States. (These rates were, however, affected by the particularly brisk expansion in the last quarter of 1961: the cyclical growth in fact slowed down in the course of the year). Nevertheless the increase in the gross national product—estimated at 5.5 %—was well below the figure for 1961 (8 %). This decline is, however, due in no small part to the fact that in farming and to a lesser extent in building and construction, owing to unfavourable weather, production for 1962 was only slightly up on the 1961 figure. On the other hand the index of industrial production rose, despite the summer and autumn strikes, by upwards of 8.5 % i.e. almost as much as for 1961 (9.1 %).

On the demand side, exports and fixed capital investment suffered from the general slowdown of expansion. On the other hand private consumption rose substantially in terms of value, even more so than in the previous year; in terms of volume the growth rate shows a slight decline (6 % as against 7 %), due to a more rapid increase in consumer prices.

For despite higher industrial production and a further substantial expansion of imports, the price trend continued upwards. Higher food prices, owing to disappointing harvests of certain produce, were partly to blame. But the fact that from 1961 to 1962 the average wage rose faster than productivity was another factor, because firms were able to pass on part of the increased costs in higher prices.

The deficit on trade widened, all the more since percentage-wise imports appear to have increased somewhat more than exports. But net income from services has certainly risen once more. The overall balance of payments, owing particularly to changes in the balance of capital transactions, will show a markedly smaller surplus.

The balance of payments situation, treasury surpluses, certain psychological factors and a keener demand of industry for credit, all these combined to produce tighter credit conditions, despite the remedial measures brought to bear by the monetary authorities.

Business may be expected to expand at an appreciable rate in 1963; subject to certain conditions, it seems quite possible that the tempo may even be speeded up. Though by and large the stimulus from foreign demand will probably be rather weak,

home demand should again forge ahead faster. This, it is true, will require a substantial growth in public investment, which, combined with the more confident mood of private industry and the prospects of a further rapid increase of consumer spending, may engender a faster growth of industrial investment.

In these circumstances, industrial production and—assuming normal harvests—the gross national product at constant prices may well exceed the 1962 figures by about 6 % and fully 5.5 % respectively.

It would seem, moreover, that an increase of this order at least is required if employment is to be again improved (the number of persons employed rose by about 1 % in 1962). This will be impossible without a monetary and credit policy designed to allay the tightness on the credit market, and particularly a financial and investment policy advancing from the preparation of major public investment projects and the provision of funds to the active stage and the consequent increase in expenditure.

1. Balance-sheet for 1962

For the full year, foreign demand was once again the most lively factor in the expansion of overall demand; the year-to-year growth rate proved, however, a little weaker than in 1961, mainly because of a slowdown in the growth of exports of goods. This item, according to customs returns, probably exceeded by some 12 % in value and 13 % by volume the figures for 1961, which had represented an advance on the previous year of 14.8 % and about 19 % respectively.

To a large extent the rise in the year-to-year export figures is still a consequence of the boom in business in the last quarter of 1961; in the course of the year itself, development, on a seasonally adjusted basis, was distinctly less brisk, doubtless partly reflecting cyclical factors, in particular a weakening of foreign demand for investment goods. But special factors, such as losses due to strikes and also bad harvests, hampered the development of exports; the seasonally-adjusted figures showed an actual decline for the third quarter, though this was probably more than offset towards the end of the year.

The year-to-year growth rates for exports to the other countries of the Community were again particularly high. To the United States also, exports rose sharply, after a lull from 1960 to 1961. As for the breakdown of exports by category of product, Italian sales of consumer goods were obviously strongly placed since in important purchasing countries

business activity centred mainly on consumption; for exports of investment goods, the growth rates, though high, are tending to sag.

Exports of services again, it would seem, increased a little more rapidly than exports of goods, largely owing to the tourist boom. All in all, exports of goods and services, in terms of national accounting, were probably up by a good 12 % in value and more than 13 % by volume on the figures for 1961; in that year the growth rates had been 15.1 % and 16.9 % respectively.

Home demand continued to rise, but the expansion of gross fixed investment slowed down in the course of the year, and also the final growth rate was lower than for 1961. This was true, in the first place, of investment by enterprises. Purchases of equipment goods probably further increased, but they were far from reaching the high growth rate of 1961. Investment in building, i.e. outlay on building for trade and industry, which was still growing very vigorously in 1961, seems to have made only modest progress. Housing also advanced more slowly than in 1961, and in fact was sluggish. Lastly, in the public investment sector, a decline at least in public works was recorded for the first time for many months. The slack development of the building and construction sector as a whole was doubtless due partly to unusually bad weather, in contrast to 1961, in the early months of the year.

A rough general estimate for the expansion of gross fixed investment for this year as compared with 1961 would put the increase at a full 10 % in value and 6.5 % by volume as against 13.9 % and 11.5 % for 1961 over 1960.

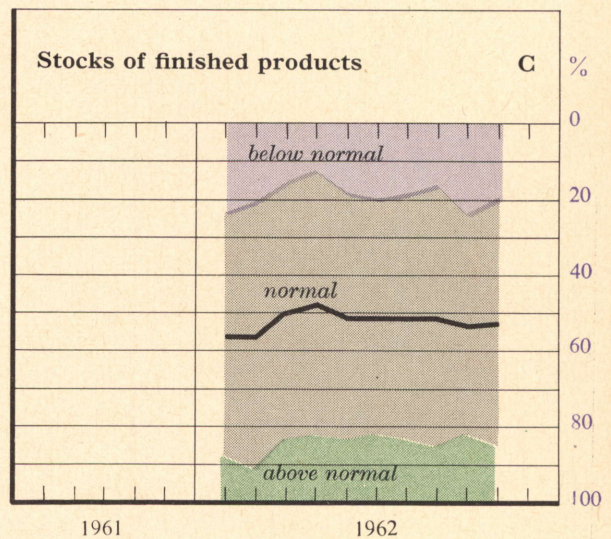
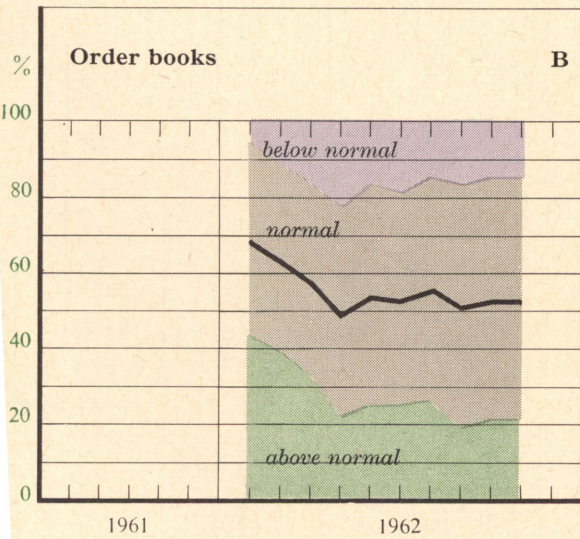
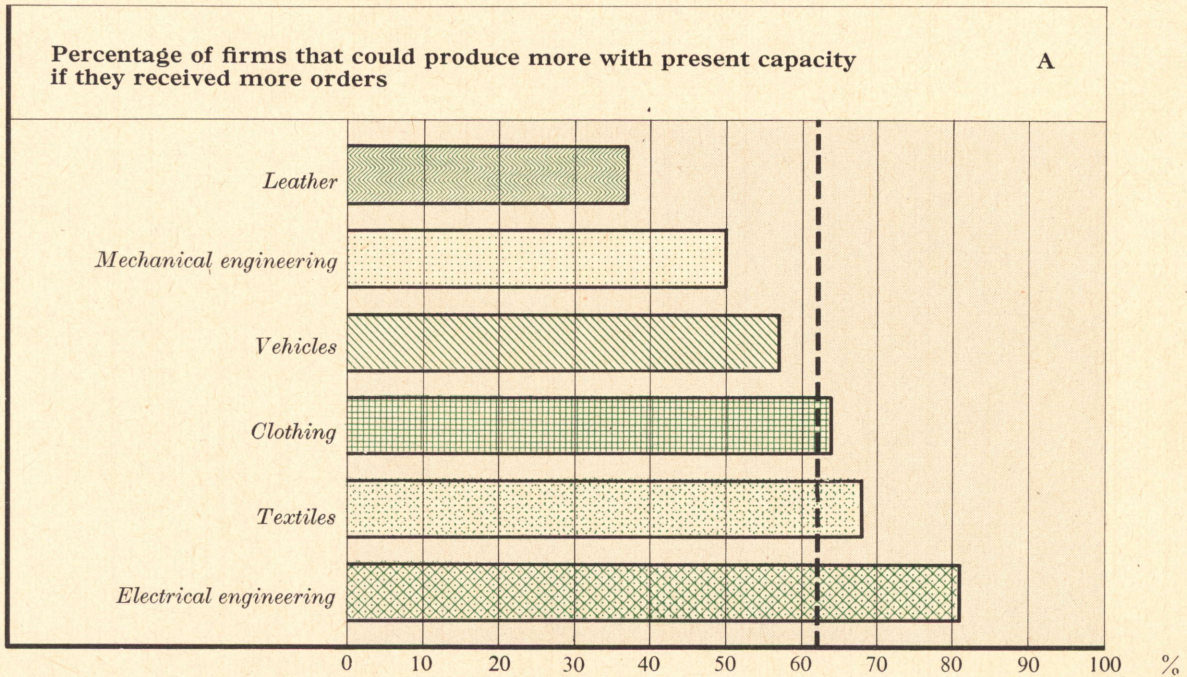
As for the seasonally adjusted trend in fixed investment during the year, the slowdown in growth already noted last year persisted at least until the middle of 1962. At any rate, the EEC business surveys carried out by ISCO-Mondo Economico suggest that in private firms the propensity to invest continued to decline until the autumn.

Trends in stock-building would seem, if anything, to have had slightly moderating effects on the business situation in 1962.

In contrast with investment, consumer expenditure gathered momentum: consumption may be considered as the most important growth factor in 1962. In the public sector it increased considerably, probably by more than 10 % in value and some 7 % by volume, rates which had been 10.1 % and 5.5 % for 1961 over 1960. Substantial improvements in the salaries of Government employees were a major factor in this vigorous increase in value terms.

The increase in private consumer expenditure was probably about 10 %. But since, at the same time, consumer prices increased substantially, the rise in terms of volume is not likely to have been more than 6 %. The shift in consumption towards more

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to the questions of the EEC business survey, carried out in Italy by ISCO-Mondo Economico.

GRAPH A : Answers to this question (from the survey made at the end of July 1962) are given for six branches of industry. The percentage for industry as a whole is shown by the dotted vertical line.

GRAPHS B and C : The three colours (green, grey and violet) show the percentages of the three different answers. The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

- by 0.03 for the answer "above normal";
- by 0.02 for the answer "normal";
- by 0.01 for the answer "below normal".

expensive goods continued, as can be seen from the rising year-to-year growth rate of home sales of luxuries and semi-luxuries: 22 % for the first ten months of 1962.

Total disposable income has certainly increased substantially. The incomes of those in paid employment account mainly for this development, not only because of a fresh increase in numbers but above all because of a sharp rise in income per head. This was due mainly to considerable wage increases and the continuing drift from the land into industry and certain types of services. As for the wage trend, the conclusion of fresh collective agreements in the first ten months of the year was enough to step up wages, on a year-to-year basis, by fully 8 % in industry, 10 % in transport and no less than 18 % in farming. The figures for wages actually paid would almost certainly show even larger margins. The sharp rise in the prices of farm produce also meant higher average incomes in agriculture. Lastly, transfer incomes were substantially improved about the middle of the year.

On the supply side, agricultural output fell short of the expectations of mid-1962. It is true that the wheat harvest was 15 % up on that for 1961; but severe drought in certain areas prevented maize, rice, olives and certain fruits and vegetables from reaching the 1961 level. Livestock production seems to have declined slightly. By and large, it would seem, then, that agricultural production (value added) did not expand to any noteworthy extent.

Industrial production on the other hand again appreciably surpassed the previous year's figures. The ISTAT index suggests that growth from 1961 to 1962 was more than 8.5 %, which would make it almost as large as that for 1961 over 1960 (9.1 %). However, this constitutes in part only the arithmetical expression of the particularly sharp rise in the conjunctural trend recorded at the end of 1961. Subsequent development in the course of 1962 was less lively, although unquestionably stronger than the seasonally adjusted June, July, September and October indices would suggest: in these months strikes caused heavy losses of output, which are not eliminated in correcting for seasonal variations. The autumn recovery was apparently fairly brisk.

As was to be expected from the fact that demand was centred mainly on consumption—the salient feature of the economic situation in Italy, as indeed to a great extent in other countries—higher growth rates were recorded in 1962 for the production of consumer goods than of investment goods.

The volume of output in building and construction (value added) was only slightly up on that for 1961, when the year-to-year growth rate was 7.5 %. On the other hand, the value added by the services sector seems to have again expanded, by 5.5 % at constant prices as against 7.3 % in 1961.

Broadly speaking, the growth of the gross national product at constant prices in 1962 may be put at a good 5.5 % as against 8 % for 1961.

The expansion of production was accompanied by only a moderate growth in the number of persons employed. Sample surveys carried out up to now by ISTAT suggest that this was probably about 1 %, as against more than 1.5 % in 1961. The growth of production therefore reflects once more, for the greater part, an improvement of productivity. The unemployment figures fell more sharply than usual: Ministry of Labour returns show that they were about 17.5 % down in the first nine months on the corresponding 1961 figures. Conditions on the labour market in Northern Italy again tightened.

In contrast with 1961 the utilization of production capacity as revealed by the EEC business survey mentioned above was on the decline, the total increase in output being slightly lower.

Heavier imports again swelled overall supply. Customs returns suggest that imports of goods increased by about 14 % by volume and slightly more in value as against 14.3 % and 10.5 % in 1961. The growth of imports from other Community countries accelerated, stimulated mainly by the two cuts in internal customs duties, of 1 January and 1 July, made in accordance with the EEC customs disarmament plan, and by a cut made at the end of August for reasons of price policy. These reductions lowered the basic Italian tariff (i.e. the tariff on 1 January 1957) once more very considerably, this time by no less than a quarter. Imports from the developing countries also moved up again after declining in 1961. Imports of consumer goods expanded particularly vigorously. In the course of the year, and more especially in the third quarter, the trend was more strongly expansive than in 1961.

Imports of services almost certainly increased also. If all, imports of goods and services, in terms of national accounting, may well have advanced by 15 % for 1962 both in volume and in value, the corresponding figures for 1961 being 11.9 % and 15.2 %.

Despite the considerable increase in supply, the price level continued to rise, sometimes at a distinctly faster tempo. In October 1962, wholesale prices and consumer prices were 3.7 % and 5.2 % up respectively on the figures for a year earlier. The unfavourable influence of the weather on the supply of foodstuffs mainly accounted for this development, but regular increases in controlled rents, and certain increases in industrial products and above all in services also made their contribution. Wage increases were doubtless a significant factor, since the resultant rise in costs per unit of output was passed on to the customer.

The deficit on trade may well have increased in comparison with 1961 (\$1 035 million) and may reach a figure of about \$1 200 to \$1 300 million. However, a further substantial increase in net income from services may be expected. Despite the recurrence of a fairly favourable trend in the balance on current account, the surplus on the balance of payments will almost certainly have declined substantially, since the balance of capital transactions is now showing a deficit.

Official gold and foreign exchange reserves fell by \$137 million in the first 10 months of 1962, but it should be remembered that Italy made an advance repayment of its external debt of nearly \$180 million. Other reserves of foreign exchange grew over the same period by nearly \$350 million.

Developments on the credit market in 1962 were rather unfavourable. In the first place, the converging trends in prices and wage costs again restricted margins for the self-financing of investments, causing a more rapid expansion of the demand for credit. Secondly, the movement of official foreign exchange reserves raised the level of domestic liquidity much less than in the previous year. Lastly, further Treasury surpluses and an increase of notes and coin in circulation due to higher wages and sales restrained to a certain extent the internal liquidity of the banks. To facilitate the financing of investments, the compulsory reserve rate was reduced at the end of January 1962 from 25 % to 22.5 %, and recently the banks have once again been authorized to increase their liquidity by borrowing abroad. Moreover, since November 1962, issues of Treasury bills are to be adapted, in volume and in interest rates, to the current situation of the money market. Not least, psychological factors have increasingly unsettled the Italian Bourses in the course of the year; the net yield on Government bonds increased substantially, rising from 4.8 % in April to 5.4 % in October.

2. Outlook for 1963

There is every indication that economic expansion will continue in 1963; and certain factors suggest that it may even gather more momentum. It is true that the not very encouraging outlook for world business hardly justifies the expectation of exports benefiting from any major stimulus; however, if certain assumptions are correct, the development of home demand might well be more rapid than in 1962.

The growth rate of foreign demand for goods and services should, then, decline. In terms of national accounting, it might none the less reach at least 7 % by volume. The competitive position of Italy has remained strong, although it was certainly stronger still eighteen months ago, before the upward trend in wage costs and prices sharpened. With reserve capacity and relatively large manpower reserves, early delivery dates can still be quoted. Still in connection with export prospects, mention should be made of the forthcoming increase in resources available to the Public Guarantee Fund for export credits—the total will be raised to 270 000 million lire—and of the plan to double the subsidies granted for export credits. Similarly the new 10 % cut in customs duties in the Community on 1 July must be expected to boost trade. Moreover, assuming good harvests, exports of farm produce—an important item for Italy—will increase. Lastly, the boom in tourism will certainly continue.

The forecast of more rapid expansion in home demand is based mainly on the assumption that the growth of gross fixed investment will gain momentum. A powerful impulse here should come from public works. Large-scale projects—notably the construction of motorways, operations in Southern Italy and in the islands, and investments to rationalize the railways and farming—are now, it seems, about to be launched or pressed forward more rapidly. Similarly new government-aided housing may again increase more rapidly, at latest by the second half of the year. These prospects, a probably more confident mood in private industry, the still very expansive prospects for private and public consumption, and lastly the growing need for rationalization in industry may, taken together, provide strong enough inducements for business circles to abandon the cautious investment policy they have been following in 1962. On these assumptions, the growth rate for total gross fixed investment might reach a figure of the order of 8 % for 1963.

It has already been stated that consumption is expected to increase rapidly. In 1963 it might grow in the public sector by about 7 % to 8 % at constant prices, i.e. a little more rapidly than in 1962. Similarly, private consumption will almost certainly grow by at least 5 %. The incomes of workers, in particular, will again rise substantially, although the increase per head will not be so rapid and the numbers employed will also increase a little more slowly than in 1962. The increase in retirement pensions granted in the middle of 1962 will have a particularly noteworthy effect on the growth of transfer incomes.

In these circumstances, industrial production should continue to grow, seasonally adjusted and in the course of the year, at least as rapidly as in 1962, unless it is hampered by exceptional factors such as strikes. For the full year 1963 a growth rate of about 6 % is to be expected. It is thought that the rate of expansion of output in the building and construction sector (value added) will be a little higher, i.e. 8 %, assuming that expenditure on public works and housing does in fact go up steeply. Lastly, the possible growth in the services sector (value added) is estimated at about 5.5 %.

Assuming normal weather and a corresponding improvement in the contribution from agriculture, the gross national product for 1963 at constant prices may well exceed that for 1962 by fully 5.5 %.

In view of the expected trend in overall demand and production, the year 1963 should see a further growth of imports of goods and services, which in terms of national accounting should be of the order of 9.5 % by volume.

However, the level of prices may creep up a little further. In the first place, it is likely that food prices will still for some time be pressed upwards by the factors which inflated them in 1962. Secondly, the increase in wage costs—partially reflected in higher prices—may well continue, although it may be less marked than in 1962.

On the basis of these predictions, it may be expected that the deficit on trade will continue to widen. Despite a further growth of net earnings from services, particularly on account of tourism and remittances from Italian emigrants, the surplus on current transactions may again decline or even disappear altogether. The overall balance of payments will depend essentially on capital movements.

In any case, there is little reason to expect that, for 1963, the balance of payments will inject any appreciable increase of liquidity into the economy. Similarly, internal savings are hardly likely to lead to any great easing of the capital market. But sufficiently easy money and capital markets are a vital prerequisite if the expected revival of the propensity to invest is to find practical expression in a vigorous increase of investment expenditure, the more so since a further narrowing of the margin for the ploughing back of profits by firms must be expected, although this margin is likely to remain fairly wide. Public credit policy and financial policy will therefore have to remain very flexible. It is therefore to be welcomed that the financing of public investments is now to be made first and foremost from the reserves accumulated by the public sector itself. In this connection the lifting of the reserve requirement for bank-to-bank deposits, the lowering of the minimum reserve ratio for foreigners' deposits and the repayment on 1 January 1963 of long-term Treasury bills to a total of more than 190 000 million lire are also to be noted. In addition, the new regulations concerning rates of interest paid on bank-to-bank deposits and the change mentioned above in arrangements for issuing short-term Treasury bills have created further important conditions enabling open-market operations to be carried out in future in Italy as well as in the other member countries.

It is essential that the Government should increase its investment expenditure in 1963 under the numerous projects which have been approved for public works designed to improve structures. The budget proposals for the financial year 1962/63 already provide for such long-term expenditure to a total of about 1 200 000 million lire, or about 15 % more than for the financial year 1961/62. In general, however, there were no signs of an expansion of this order in 1962. If it were not to reach the scale planned in 1963, special measures would certainly have to be taken.

An expansionary credit and financial policy would not involve any further danger with regard to prices, in view of the existing elasticity of production and the scope for imports. It would be desirable again to stimulate imports by consolidating the cut in customs duties made in August 1962 for reasons of conjunctural policy, i.e. by not allowing it to be absorbed in that planned for 1 July 1963. Further anticipatory cuts in duties might be made and other liberalization measures taken. Such measures still seem feasible even after the recent liberalization decisions taken with regard to the dollar area and Japan. It would also be desirable to press forward the rationalization of distribution.

D. Netherlands

Unlike the other member countries, except France, the Netherlands had a faster year-to-year economic growth-rate in 1962 than in 1961. Although the gross national product probably only rose about 2.5 % by volume, as in the previous year, the real gross domestic product went up 3.5 % as compared with 2.5 %. Industrial output will, according to the CBS index, have risen by a good 3.5 % (1961: 2 %).

The quicker real growth is mainly attributable to somewhat greater elasticity of domestic supply due to high rationalization investment in previous years and to expansion of the potential labour force caused inter alia by the advent on the labour market of young people from the post-war population bulge.

In the case of demand, the growth of exports picked up appreciably over the year as a whole. The individual components of internal demand developed along differing lines—gross fixed investment expanded somewhat less, both in value and volume, than in 1961, with equipment investment by enterprises, in particular, dragging behind. By way of contrast private consumers' expenditure gathered momentum as a result of very sizeable wage rises. However, the real increase in consumption of almost 4.5 % remained at much the same level as a year ago because consumer prices hardened somewhat.

Imports did not grow as fast as exports, and the balance of trade therefore, improved slightly; for this reason, notwithstanding distinctly higher imports of services and a substantial drop in factor income from abroad due to extraordinary circumstances, the surplus on current account should be roughly of the same order as in 1961.

Total demand can be expected to expand at about the same rate in 1963 as in 1962, probably with some easing of tension, especially on the labour market. Greater elasticity of domestic supply should boost exports but it should be borne in mind, that the extent to which the possibility is exploited also depends on the flow of orders from abroad and the competitiveness of Dutch exports.

Domestic demand is likely to climb somewhat more slowly than in 1962 because the growth of gross fixed investment may well level off again. Private consumers' expenditure should go up in about the same proportion as in 1962, especially as further substantial wage increases are likely. In view of the fact that a further

slight price rise is inevitable, real consumption is likely to expand somewhat more slowly than in 1962.

In 1963 as a whole domestic supply will advance rather more quickly than in 1962. Industrial output and, given a normal harvest, the total real gross national product will probably both go up about 4 %. This being so, imports should climb at about the same rate as in 1962. A larger surplus might again be recorded on current account.

The main tasks of economic policy will be to see that rising wage costs and their repercussions on profits do not get out of hand and at the same time to handle tools for the promotion of investment sufficiently flexibly to counter in good time any sharp fall in the growth of productive investment.

1. Balance-sheet for 1962

Despite the continued heavy potential demand in 1962, total effective demand expanded only a little faster owing to slightly slacker growth of domestic demand.

The rise in exports gathered momentum: the growth rates of merchandise exports (in national accounts terms) in value and volume were probably a clear 6 % in each case for the whole year, compared with 1.4 % and 3.1 % in 1961. Growth quickened perceptibly as the year advanced, chiefly because of greater elasticity of the production system in most sectors.

In some sectors dwindling orders clearly put a brake on exports. The increasingly greater caution displayed during the year by businessmen in assessing their order books seems, however, partly attributable to enlarged facilities for production and deliveries since the middle of the year. Whereas exports of chemicals and foodstuffs rose steeply in 1962, there was a marked drop in metal products and some textiles.

The greatest increase was once again in exports to Community countries, not counting Belgium; deliveries to non-member countries, especially EFTA, fell back again in the third quarter after appreciable progress between May and July.

Revenue from services increased on about the same scale as exports of goods in contrast to factor income from abroad which, partly owing to casual factors, fell appre-

ciably after having made vigorous progress in the previous year. In national accounts terms therefore, total exports may well have been some 5 % up on the year before, compared with an increase of 3.5 % in 1961.

The individual components of internal demand developed along differing lines in 1962.

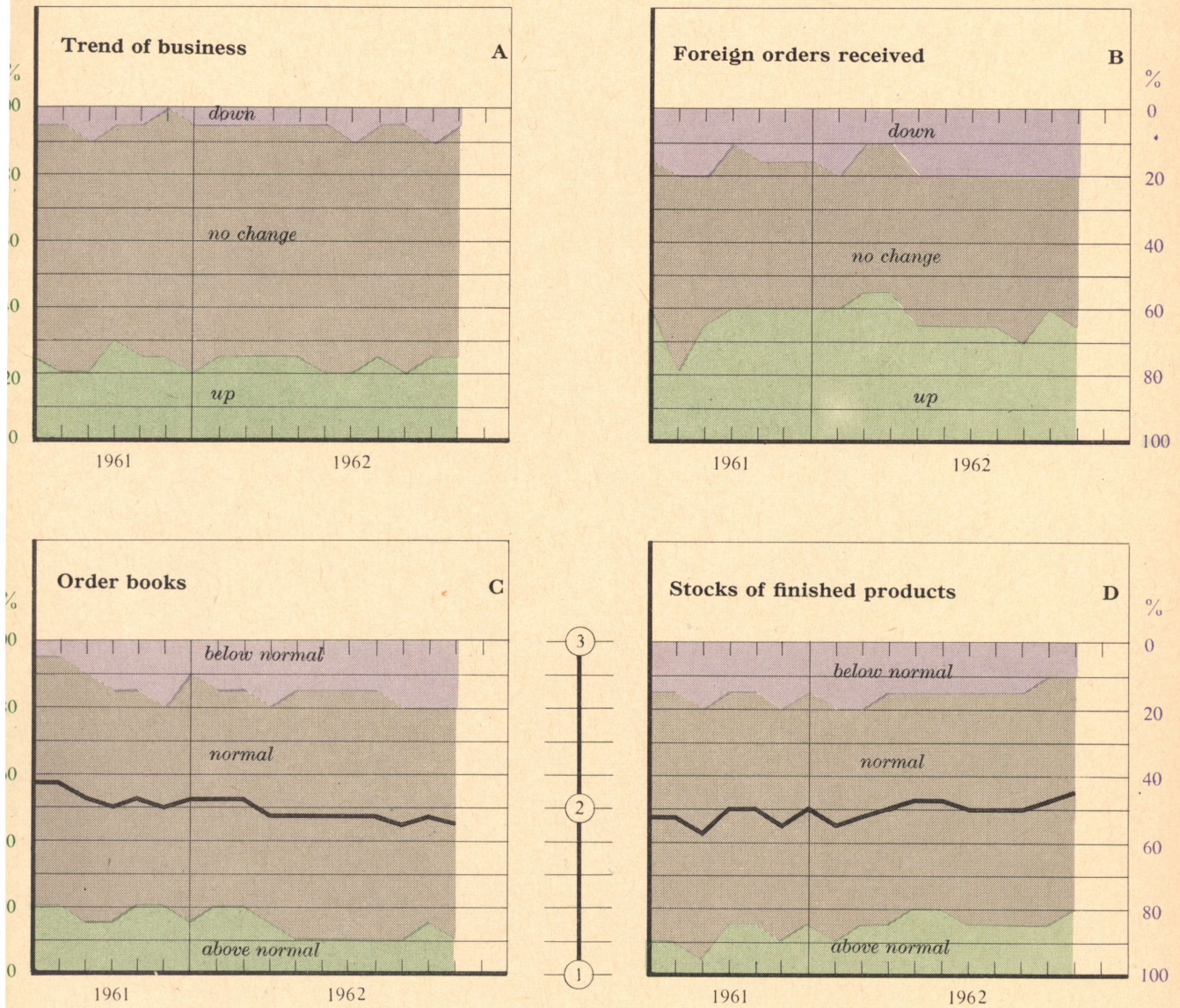
Gross fixed investment, which had expanded rather briskly in 1961, slowed down somewhat in 1962 and its year-to-year growth rates probably dropped from 8.5 % (in value) and 7 % (by volume) to 7 % and 4.5 %. Fixed investment by enterprises did in fact expand less than in 1961 and, in addition, the tendency for growth to flag seems to have become more pronounced in the course of the year. A number of factors accounted, to a greater or lesser extent, for this trend in investment: the comparatively substantial enlargement of productive capacity and a less favourable business outlook abroad—especially in non-member countries—the anti-cyclical measures taken in 1960, the policy of restraint in the issue of industrial and commercial building permits, the restrictions on lending by the banks, slightly higher interest rates, the narrowing of profit margins in recent years. Growth was particularly slow in equipment investment, where already in the first six months the year-to-year growth rate was only 12 % by value compared with 18 % a year earlier. All the available partial indicators suggest that the trend continued in the second half-year.

There was also a slowdown in the growth of public gross fixed investment, which was probably only 12 % in value and 9 % by volume compared with 14 % and 11 % in 1961. The situation remained strained in the building sector. On the whole, effective demand for building probably went up again, albeit more slowly than in 1961. This also applies to house building, although the authorities continued to keep a tight rein on permits for certain types of housing, as well as for non-residential construction.

Unlike investment, private consumers' expenditure expanded more rapidly in the course of the year, probably running at an annual rate of 7 % as opposed to 6 % in 1961. However, a definite rise in consumer prices meant that real growth was much the same as the year before—about 4.5 %. The income of private households made great strides, for various reasons: higher employment, substantial pay increases, especially in the first six months, the lowering of wages and income tax on 1 July and larger old-age pensions. Gross wages per person employed in the private sector were up by about 8 % on 1961 (when a 5 % increase was recorded) despite the fact that at the beginning of the year the economic plan had recommended a ceiling of roughly 6 %. Average hourly wages even went up by as much as 9 %, compared with 8 % in 1961, owing to the adjustment of the 1962 rates to compensate for further cuts in the working week.

The very sharp rise in value of public consumption—about 13 %—is mainly due to the substantial salary increases for civil servants (13 % per head). In terms of volume, growth was about 4 %.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Source : Business survey of the Centraal Bureau voor de Statistiek.

Note : The survey includes construction but not paper, petroleum, non-metallic minerals.

GRAPHS A, B, C and D : The three colours (green, grey and violet) show the percentages of the three different answers.

GRAPHS C and D : The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

- by 0.03 for the answer "above normal";
- by 0.02 for the answer "normal";
- by 0.01 for the answer "below normal".

As already mentioned, the employment figures went up; the increase of about 2 % was chiefly accounted for by the extra numbers reaching the labour market due to the post-war population bulge and this in turn did a good deal to prevent strain on the market from becoming more acute. Average monthly unemployment figures in 1962, although still very low, no longer fell below the corresponding level of the previous year; furthermore, the number of vacancies, whilst still extremely high, did not become any higher.

The increase in employment (about 2 % in industry) helped to increase the elasticity of internal supply to some extent, although the total number of man-hours worked suffered as a result of the further cuts in the working week decided in 1961, even though these were less drastic than in 1961.

Mainly as a result of enlarged material facilities and labour resources, industrial production, which, according to the CBS index, went up only about 2 % in 1961, expanded faster again in 1962. True, growth was very slow in the early months of the year, but it picked up after June and in the third quarter was 5 % higher than a year ago. This build up doubtless continued during the rest of the year. All in all, output probably rose by a good 3.5 % in 1962.

There appears to have been hardly any noteworthy expansion in the building sector during the year, mainly because of the severe setback caused by the extremely bad weather in the first quarter. In September 1962 the number of dwellings under construction was again 10 % higher than a year earlier, whereas the number of completed units from January to September was 7.3 % lower than for the first nine months of 1961.

Agricultural production appears to have made hardly any advance on 1961. Services, on the other hand, probably again expanded at much the same rate as industry.

All told, the growth of real gross national product was probably about 2.5 % in 1962—virtually the same as in 1961. It should not be forgotten, however, that the gross national product for 1962 was influenced by the unfavourable trend in net factor income from abroad due to exceptional factors. The development of internal activity is better reflected in gross domestic product, which went up by 3.3 % by volume in 1962, as against 2.5 % in 1961. Hence, if the increased employment figures are taken into account, productivity (per person in paid employment) rose about 1.5 % in 1962.

Although imports were up once more, the annual figures reveal that growth was again slower than in the previous year. In national accounts terms, imports of goods were probably up by 4.5 % in value and 5 % by volume on 1961, when increases of 5.5 % and 7.5 % were recorded.

This slowdown seems to have set in after the middle of 1962. True, imports of raw materials which were comparatively slack in the first half-year were given a fillip by faster production. Imports of consumer goods, too, expanded vigorously, but purchases of investment goods sagged visibly during the year.

Imports of services will have expanded somewhat faster than imports of goods. On the whole the increase in total imports of goods and services from 1961 to 1962 in national accounts terms might well amount to 5 % in value and 5.5 % by volume, compared with 5.5 % and 7 % in 1961.

The price level inched up again, despite a slight expansion of domestic supply and continually rising imports. More particularly, it proved impossible to prevent the index of consumer prices from rising in 1962 (about 2.5 % as compared with 1961). Temporary exceptionally high prices fetched by some farm produce were partly responsible for this : but above all, services, especially rents, rose and some industrial products showed a similar upward tendency. By way of contrast, the wholesale price index remained stable, owing mainly to a drop in prices of imported raw materials.

The serious deterioration in the balance of trade recorded in 1961 did not continue in 1962. Since imports and exports of goods developed on more or less the same lines and import prices fell slightly—this was still partly an after-effect of the revaluation of the guilder—customs returns show a somewhat smaller deficit on the balance of trade than in 1961 (about Fl. 3 000 million). Nevertheless, there was no further worsening of the current balance of payments despite much heavier calls on foreign services and a substantial fall in factor income from abroad. The 1962 current surplus should be about Fl. 500 million compared with Fl. 520 million in 1961. There is likely to be a surplus on the overall balance of payments, which registered a deficit in 1961 following heavy exports of private and public capital. In the first six months of 1962 long-term private capital transactions already showed a surplus of Fl. 300 million. Moreover, in 1962 probably no more than Fl. 80 million went to repayment of Government indebtedness abroad, the corresponding figure in 1961 having been Fl. 280 million. Finally, the ceiling for authorized foreign issues on the Dutch capital market was set at only Fl. 180 million as against 550 million in 1961. Consequently the Central Bank's gold and foreign exchange reserves will no doubt have risen: in any case they went up by Fl. 150 million from January to October 1962. The commercial banks' foreign exchange reserves are likely to have risen only slightly.

On the whole, although the money and capital markets enjoyed relatively high liquidity in 1962, it was lower than in 1961, one reason being the tightening up of restrictive policy. The agreement between the Central and other banks to limit the expansion of credit to industry was extended several times and Bank rate was raised at the end of April from 3.5 % to 4 % to check borrowing. Yet the agreed ceiling was exceeded at times and the non-interest-bearing deposits which the commercial banks were therefore required as a disciplinary measure to lodge with the Central Bank, amounted to Fl. 180 million in June. Expansion of credit kept within the prescribed limits for the rest of the year.

Business demand on the capital market was heavier than in 1961 owing to the decline in scope for self-financing. At the end of September, the number of Dutch in-

dustrial bonds on the market was already more than three times what it had been in 1961. This may also have had something to do with the slight increase in long-term interest rates since the beginning of the year.

Preliminary data on how the budget was implemented suggest that the deficit will come to Fl. 1 180 million and not Fl. 311 million as was first estimated. This higher figure can mainly be put down to the fact that revenue fell short of estimates by Fl. 600 million owing chiefly to lower yield from corporation and income tax. Leaving out items that have no influence on the internal monetary flow, the cash deficit may well have been about 850 million as against Fl. 625 million in 1961. However, the direct effects of the budget on the economy, in terms of the percentage increase in expenditure over the previous year, were less pronounced than in 1961 even regarding lower taxes as tantamount to higher expenditure.

2. Outlook for 1963

For 1963 as a whole the increase in economic activity and employment can be expected to continue. There is also likely to be some easing of the strain which has been a feature of the economic situation in recent years; domestic supply will expand more rapidly whereas domestic demand may well slacken off a little, thus leaving a greater margin for increased exports.

Despite the fact that economic expansion is expected to be slower in many industrialized countries and that there are no indications that demand from the developing countries will quicken, exports can be expected to expand more vigorously than in 1962. True, in view of the weaker growth of demand, expanded capacity in several sectors will mean keener competition on foreign markets. Nevertheless, the Netherlands should still be in quite a good competitive position, since production costs have also been soaring for its main competitors in the past two years. It must also be borne in mind that the Netherlands had a comparatively strong foothold on world markets at the beginning of the current trade cycle.

The flow of new foreign orders, particularly for consumer goods, will probably continue at a relatively satisfactory rate. Finally, 1963 should see the delivery of military equipment on a larger scale. Altogether, exports of goods in 1963 might well be 7 % above the 1962 level by volume. Exports of services will likewise probably climb somewhat more steeply than in 1962.

On the other hand, internal demand is likely to expand somewhat less than in 1962, chiefly because the demand of fixed investment will continue to slow down. Actu-

ally, equipment investment by enterprises will probably show hardly any further increase since from now on the decline in the propensity to invest will be affecting effective outlay on equipment to an increasing extent. Firstly, the propensity to invest is affected by the way in which profit margins have been shrinking and will probably go on doing so, thus restricting the scope for self-financing; the cut in corporation tax on 1 January 1963 will probably only really take effect on profits at the beginning of 1964. Secondly, the credit restriction policy has of course also to be reckoned with. Moreover, businessmen no longer expect demand to expand in a number of sectors as it has done from time to time in recent years. Since, broadly speaking, the labour situation is likely to ease slightly, there will probably be less incentive to make investments designed to economize on manpower. Investment in rationalization will, nevertheless, continue at a very high level.

Expenditure on industrial and commercial building will go on rising in any case. As the housing demand will in particular still be very brisk, building demand as a whole can be expected to increase and this should make possible a further increase in the volume of investment in the sector.

Public investment will act as an additional factor. Generally speaking, it will again mount steeply in 1963 and a real growth of about 9 % can be expected.

On these hypotheses for the various components of investment, total gross fixed investment could have a year-to-year growth rate of 3 % by volume in 1963. The stimulus to the economy provided by fixed investment will therefore be feebler than in 1962.

Investment in stocks, on the other hand, may do somewhat more to stimulate the economy than in 1962 since there are signs that stocking is being adjusted to the increase in sales.

Private consumers' expenditure should expand vigorously once again, to about the same extent as in 1962. Since the price rise will probably be at least as pronounced as in 1962, it will again put a brake on the real increase in private consumption, although it will probably amount to at least 4 %.

In the first place, the number of persons in paid employment will go up again and secondly, wages will continue to rise. Thirdly, the income of self-employed persons is also expected to increase, although if pay rises are not kept within bounds, the increase will be somewhat threatened. Fourthly, the disposable income of private households will benefit from the cuts made in 1962 in income and wages tax and from the higher rates of old-age pension.

According to the guiding principles of wages policy for 1963, provisionally agreed upon by the leading workers' and employers' associations in the Labour Foundation (Stichting van de Arbeid), wage increases to be granted in the 1963 renewals of collective bargaining agreements should not exceed 2.7 % per head on average for workers covered

by them. This includes workers in the particularly important metal-sector. These wage rises, together with higher social security charges, the effects of agreements already concluded in 1962 (increased rates in many branches and a general increase to compensate for higher rents) and, finally, the wage drift, already mean that wage costs per person employed in the private sector will be at least 7 % higher in 1963 than in 1962.

Wages and salaries will also continue to mount in the public sector, albeit more slowly—at an average of at least 6 % per person employed—than in 1962. On this assumption the total payroll would be 8 % bigger in 1963 than in the previous year, when it must have gone up by 10 %.

In public consumption, on the other hand, growth will become perceptibly slower. According to the budget estimates, expenditure on goods and services will grow more slowly than in 1962 when expenditure on defence rose steeply. Secondly, the level of wages and salaries in the public sector will, as already mentioned, advance more slowly. Broadly speaking, public consumption is likely to have a year-to-year growth rate in 1963 of about 5 % in value and 2 % by volume.

Mainly because of increasingly elastic production, domestic supply should expand more than in 1962. This is expected not only as a result of the heavy investment in rationalization in recent years but also because another jump in the number of school-leavers coupled with the fact that no further shortening of working hours is planned; the cuts made hitherto will have practically ceased to affect the situation by 1963. Since demand is losing ground in some branches of industry and advancing less rapidly in several others, the labour market will probably ease slightly. Labour reserves could become somewhat larger. Employment will probably go up by about 1.5 %.

In view of these prospects, industrial production, as well as building construction, is expected to register a good 4 % increase in volume. The services sector can also be counted on to expand vigorously again and some slight growth is expected in agriculture. In these circumstances, the gross national product at constant prices might well be upward of 4 % larger than in 1962.

There will also be a marked rise in imports but, despite the fresh Common Market tariff cuts due on 1 July 1963, faster growth is unlikely. A limited rise in imports of consumer goods and a perceptible one in raw material imports are anticipated. Imports of capital goods, on the other hand, will probably continue to slacken. Taken all in all, imports of goods could be about 6 % higher by volume than in 1962. Imports of services, however, will in all probability expand at a rather weaker rate.

The predicted trend in imports and exports of goods and services might produce a higher surplus on current account in 1963 than in 1962. While it is not possible to foresee what changes the balance of capital transactions may undergo, there is little likelihood of capital imports on the same scale as in 1962.

Consequently, transactions with abroad cannot be expected to bring about any significant increase in internal liquidity. Nor do the budget estimates for 1963 hold out any prospect in this respect. The cash deficit which admittedly should be somewhat higher than in 1962 (Fl. 930 million as against Fl. 850 million) could be covered by advance subscriptions by the pension fund and by borrowing on the capital market, although this latter will amount to less than the gross amortization payments on the consolidated internal debt (Fl. 470 million).

These forecasts for 1963 depend essentially on whether it proves possible in fact to keep the development of wages within the required limits. In any case, these allow for a further rise in wage costs albeit at a slower rate than in 1961 or 1962. If costs actually climbed more steeply, there would be a risk of further adverse effects on investment by enterprises. In addition the competitiveness of the Netherlands economy would deteriorate to an extent that could create problems in the longer term.

Economic policy-makers have to face two requirements: they must keep wage trends within the limits that are desirable or acceptable in the light of economic and growth policy, and they must also maintain sufficient flexibility in handling the instruments available for countering the decline in investment demand. This is especially true of credit policy, which needs to be eased up at the appropriate time. Public finance policy has already once more been given a greater bias towards expansion. The budget estimates are intended to give the economy a boost by a more vigorous increase in expenditure than in 1962.

E. Belgo-Luxembourg Economic Union

Belgium

A comparison of the annual figures shows that economic growth was almost the same in 1962 as in 1961. In fact the gross national product in real terms appears to have risen to the same extent (about 3.5 %). Industrial production may have increased by more than 5 % compared with 4.5 % from 1960 to 1961.

However, if the adverse effect on the 1961 figures of the strike at the beginning of the year is discounted, output appears to have expanded somewhat more slowly in 1962. The main reasons for this lie in the disparity between the trends in demand: external demand advanced somewhat more rapidly than in 1961—although here too the figure for that year was doubtless influenced by the strike—whereas internal demand increased less than in 1961, the reason for this being that gross fixed investment grew appreciably more slowly; private consumer expenditure at constant prices seems to have risen almost as rapidly as in 1961.

The price level rose rather sharply at times, owing mainly to temporarily higher food prices, bringing the sliding wage scale into operation in many sectors. This accentuated the upward trend of wages, which even without this factor was more pronounced than in 1961. In the latter part of the year prices fell again, so that in the autumn the price level was only slightly higher than a year earlier.

Since imports showed a slightly smaller growth-rate than in 1961 and exports expanded faster, the balance of trade improved. The overall balance of payments probably closed with a surplus. This, together with increased savings and the reform of the money market, contributed to the relatively liquid state of the money and capital markets, although the Treasury made heavier calls on these markets.

There are many indications that economic growth will continue in 1963. The tempo may, however, be slower. Firstly, prospects for a further expansion of exports are less encouraging and, secondly, it seems likely that the growth of investment will again decline. Private consumption, on the other hand, may advance somewhat faster than in 1962, but without entirely counterbalancing the damping effect of the trend in the other components of demand.

Production will probably make further strides; the growth rates of industrial production and of the gross national product in real terms may be about 3 %. In view of this, the situation on the labour market in 1962, which could almost be described as one of full employment, is unlikely to show any further improvement.

Should exports and investment lose momentum more rapidly, it would certainly be advisable to take fresh measures, especially to give a further boost to investment growth. Some intensification of Government efforts to promote investment will be needed in any case, otherwise it may be virtually impossible for Belgium to attain the long-term objectives of its policy of economic expansion.

1. Balance-sheet for 1962

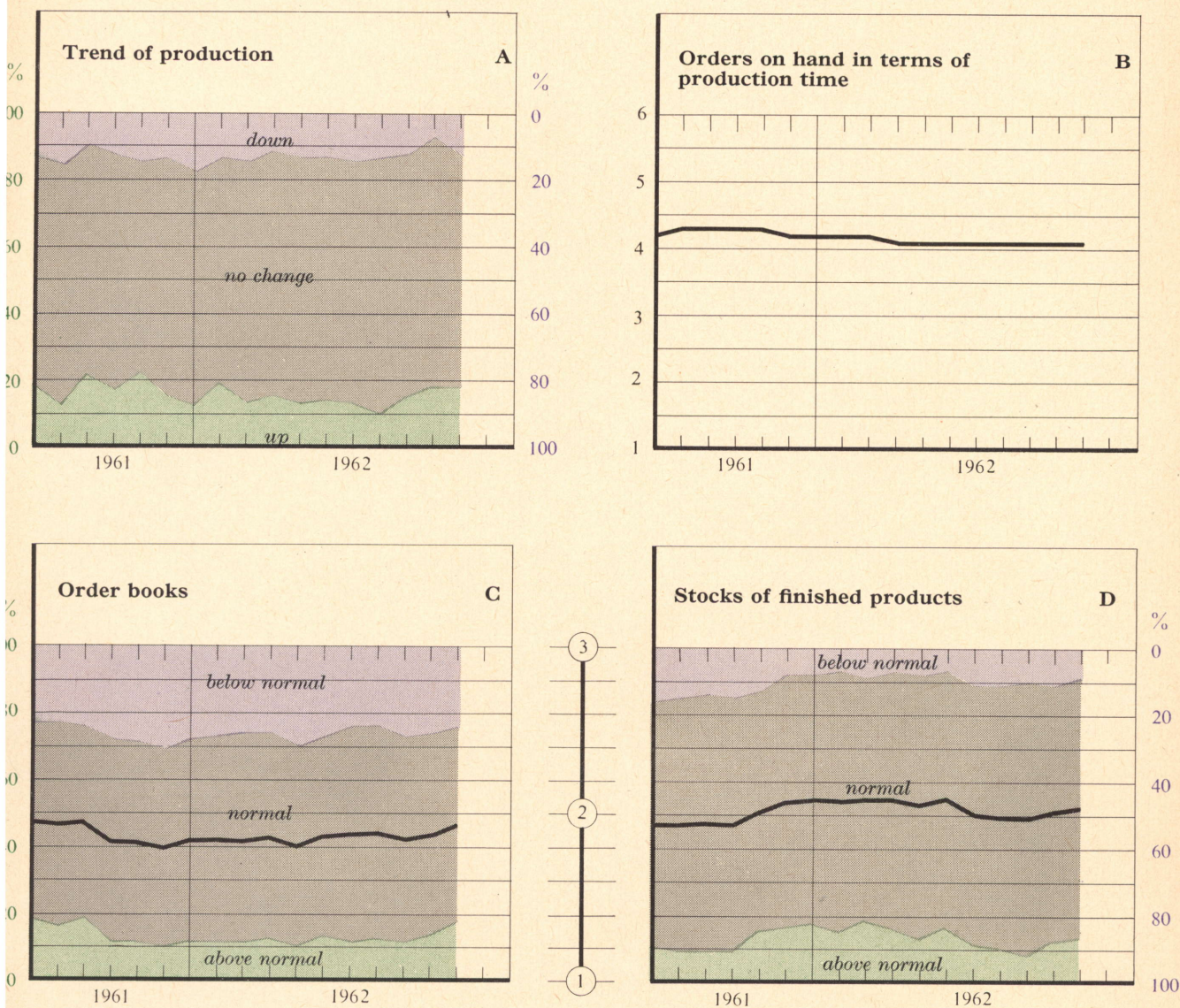
In 1962 the growth of overall demand was sustained mainly by external demand. Exports of goods, according to customs returns, were up by more than 9.5 % in value. In 1961 the growth rate was lower, but if the effects of the strike at the beginning of that year are discounted both years are seen to have much the same growth-rate (about 6.5 % by value and 7.5 % by volume). Export prices again fell slightly.

The growth of exports, however, showed a slight tendency to lose momentum in the course of the year and the year-to-year growth rate fell from an average of 7.2 % in the period from February to June to about 6.5 % in the third quarter. One reason for this may well have been slower expansion in exports of certain items, such as machinery, appliances and textiles, which had given the greatest impetus in the first six months. Falling external demand, compared with 1961, for metals and mineral products was more than outweighed, particularly in the third quarter, by a recovery in exports of transport equipment and chemical products.

In 1962 as a whole, exports to EEC countries increased substantially and, except to the Netherlands, at a faster rate than in 1961. Exports to other industrialized countries also rose but solely because of a notable increase in exports to North America, and these moreover showed no signs of any further increase in the third quarter. Deliveries to developing countries were practically unchanged.

Exports of services also went up in 1962, but the incomplete information available suggests that the growth rate will be substantially lower than that for goods.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Source : Business survey of the National Bank.

Note : The survey does not include all branches of industry; for instance, fuel, chemicals, non-ferrous metals and foodstuffs are not included.

GRAPHS A, C and D : The three colours (green, grey and violet) show the percentages of the three different answers.

GRAPH B : The curve shows the average of answers, expressed in months of production.

GRAPHS C and D : The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

- by 0.03 for the answer "above normal";
- by 0.02 for the answer "normal";
- by 0.01 for the answer "below normal".

In contrast to external demand, internal demand rose less rapidly in 1962 than in the previous year. This can mainly be attributed to the slower growth of investment, whereas private consumer expenditure went ahead at about the same rate as in 1961.

The growth of gross fixed investment appears to have declined by about a third in comparison with 1961. Latest estimates put the growth rate at some 4 % by volume, as against about 10 % in 1961.

Gross fixed investment by firms, which was already at a very high level, advanced only slightly. The data available (particularly on home sales of machinery and apparatus) indicate that equipment investment virtually marked time at the level reached in the last quarter of 1961. True, investment in the form of industrial and commercial buildings showed a further rise, but probably at a growth rate considerably lower than in 1961. Housing construction showed a slight decline in 1962, whereas in 1961 it had remained more or less stable.

On the other hand, public investment rose considerably, although the pace tended to slacken in the third quarter.

Public consumption increased considerably more than in 1961, mainly owing to an increase in civil servants' salaries.

Private consumer expenditure appears to have increased on about the same scale as in 1961 but, since prices rose somewhat more steeply, private consumption in real terms probably advanced somewhat more slowly than in 1961, when an increase of about 3 % was recorded. The increase in the first quarter was only moderate, but the pace quickened later in the year.

The increase in the total wage and salary bill in 1962 may be put at more than 7 % for the full year, as against 6 % in 1961. This is due not so much to a higher level of employment as to substantial wage and salary increases, which in many sectors were accentuated by the operation of the sliding scale in the middle of the year. It is possible that the proportion saved of disposable household income went up slightly.

There was in fact hardly any change in the number of persons in paid employment during the year; in industry and transport, employment remained more or less at the high level reached at the end of 1961. Comparison of the average annual figures for 1961 and 1962 shows an increase of less than 1 % in 1962 as compared with about 1.5 % in 1961. The situation on the labour market remained substantially the same: almost full employment, with shortages in a few trades and sectors and reserves of labour in others. Unemployment figures stood at 77 400 in October as against 92 600 a year earlier.

The production trend suffered only slightly from these labour shortages; generally speaking it was still determined by the development of demand.

According to the IRESP index the growth rate of industrial production may be more than 5 % in 1962 as against 4.5 % in 1961. These figures are, however, affected by the repercussions of the strike at the beginning of 1961. If these are discounted, expansion appears to have fallen off slightly owing to trade-cycle developments: firstly, internal demand, especially for investment, advanced at a slower rate and secondly, external demand in some sectors declined in absolute terms or lost momentum (iron and steel, non-ferrous metals and capital goods). In coal-mining, however, the further drop in output was probably caused mainly by the labour shortage. Finally, the supply of imported goods again increased considerably.

These factors tending to restrain the growth of industrial production were offset by a revival of demand for consumer goods, on export and particularly on home markets. This probably explains to a large extent the slight spurt in industrial production in the third quarter, when the year-to-year growth rate was 5.3 %, after a rate of only 2 % in the second quarter. The level of activity in the second quarter of 1961 was, however, particularly high, because the backlog in production caused by the strike was partly made up by overtime working.

The information available suggests that agricultural production made only moderate progress in 1962. It also seems that the product of the services sector expanded only slightly. All in all, the provisional estimates of the Commission's staff put the growth of the gross national product in 1962 at about 3.5 % in terms of volume. In view of the trend in employment described above, this increase is mainly the result of higher productivity.

Supply was again swollen by a fairly marked increase in imports. Despite the slight slackening in the growth of overall demand, imports of goods (according to customs returns) went up by more than 5.5 % by value in 1962. True, this was somewhat less than the increase recorded in 1961 (6.5 %), but import prices tended to ease in 1962, contrasting with developments in 1961. There does not seem to have been any significant change in comparison with the previous year in the growth of imports by volume. Heavier purchases of certain farm produce following the poor harvests in 1961 doubtless helped to swell total imports in 1962; however, this expansion is also due to a large extent to a fresh increase in imports of capital and consumer goods. But it may be noted that the growth rate of imports of capital goods and vehicles fell away during the year while that of certain imported consumer goods was maintained or even increased. For imports of raw materials and semi-finished goods the trend was rather hesitant.

Prices rose slightly. Retail prices moved up more rapidly in the first half of 1962, mainly owing to temporarily higher prices for some agricultural products, so that the sliding wage scale came into operation towards the middle of the year. After July food prices eased and in the third quarter the retail price index stood only 1.1 % higher than a

year earlier, after exceeding the 1961 level by 2.3 % in the second quarter. Wholesale prices remained virtually stable, thanks partly to lower prices for a large number of imported raw materials and some semi-finished products.

The balance of trade probably improved appreciably in 1962. This impression is confirmed by the encouraging trend in the third quarter and the improvement will doubtless still be apparent in the annual figures even after the effects of special factors which widened the deficit in 1961 have been discounted.

By and large the deficit on trade in goods, according to customs statistics, may be around Bfrs. 7 500 million in 1962 compared with 14 500 million in 1961 and 9 000 million in 1960. Despite an expected slight deterioration in the net position on services, there may well have been an improvement on current account. Capital transactions, on the other hand, may well show a net outflow of foreign exchange, due to a deficit on public capital transactions arising from repayments of short-term foreign debts and transactions with the International Monetary Fund.

The overall-balance of payments should close with the same surplus in 1961 (Bfrs. 600 million). Although the official gold and foreign exchange reserves fell by \$5 million from January to November 1962, after rising by \$235 million in 1961, the net foreign exchange position of the banks has probably improved considerably.

Public finance was a little better situated in 1962 although it failed to reach the targets set for it in the budget-equilibrium in current transactions and an overall deficit not exceeding Bfrs. 15 000 million. According to the latest information, the budget deficit will probably amount to Bfrs. 18 500 million, compared with 19 800 million in 1961 and 26 500 million in 1960. Probably the cash deficit will largely be financed by long-term borrowing. The total foreign debt, which reached its peak in May 1961, was reduced by Bfrs. 13 700 million between May and October 1962. The fall of Bfrs. 9 500 million in the short-term foreign debt between December 1961 and October 1962 was accompanied by a relatively faster rise in internal short-term indebtedness. But thanks to the reform of the money market at the end of 1961, the banks' holdings of Treasury bills increased only moderately. A substantial part of the increase in the public debt was in fact taken over by semi-official institutions.

Interest rates tended to be brought down by the abundant liquidity on the money and capital markets, which can be attributed to the monetary reform measures introduced at the end of 1961, to the surplus on transactions with abroad and also to caution in the use of private savings for investment purposes. This trend in interest rates was also encouraged by the monetary authorities who, in December 1962, lowered bank rate (by 0.25 %) for the sixth time since August 1961. In the middle of October the interest rate on Treasury bills was 4.28 % compared with 5.16 % a year earlier.

2. Outlook for 1963

The trends in the Belgian economy in the latter part of 1962, the outlook for business abroad and the available indications as to the possible further growth of internal demand all point to a continued expansion in 1963 as a whole. Growth, however, might be somewhat less vigorous than in 1962.

External demand is hardly likely to keep on growing as briskly as in 1962. Replies to the questions put to businessmen by the National Bank as part of the joint EEC business survey indicate that foreign orders were tending to fall off in the second half of 1962.

True, exports of goods to the other Community countries should increase in 1963. But at this phase of the business cycle, which is marked almost everywhere by a weaker propensity to invest and a cautious policy as regards the stocking of semi-finished and intermediate products, the corresponding Belgian exports will only be able to make rather meagre progress. In fact it is not impossible that these products, which still make up a large proportion of total exports, will tend to stagnate. However, sales of highly specialized products of the mechanical engineering industry and certain finished products of the chemical and textile industries may well continue to enjoy relatively high growth-rates.

The outlook for world economic activity, and particularly the prospect of a lull in North American business, hold out no hope of an improvement in demand from non-member countries.

As strain eases in the industries of Belgium's main competitors, Belgium stands to lose the advantage it has had hitherto where delivery dates are concerned. This introduces a further element of uncertainty into the export trend, even for products which in the last two years have contributed much to the growth of total exports.

This being so, it may be estimated that exports will increase by 4 %-4.5 % by volume. The growth rate for exports of services will probably decline slightly.

Internal demand is likely to advance in 1963 at about the same rate as in 1962, a slight speeding-up of private consumption being possibly offset by a further slackening in the growth of investment.

Public investment, however, will in all probability rise somewhat faster than in 1962. Fixed investment by firms may well show further distinct signs of a decline in expansion, particularly where equipment investment is concerned. Investment is in fact being adversely affected in several large sectors by the discouraging outlook for external demand and the pressure on profit margins—though this is much less severe than in the other member countries—due to low export prices and higher production costs. However, this trend will help to boost rationalization investment, which is tending to

become general in most sectors. The overall level of investment by firms will also be sustained by the progress of extensive investment programmes set on foot mainly by foreign firms.

Housing construction may well tend to stagnate or even decline. In 1963 overall gross fixed investment can be estimated roughly to show a growth rate over 1962 of 3 % in real terms.

Private consumption may expand rather more than in 1962. True, the total wages bill will rise somewhat less rapidly than in 1962, but the factors which in that year appear to have restrained consumption (bad weather, expectation of effects of tax reform), and hence increased the rate of savings, should figure less prominently in 1963. Moreover, the expansion of private consumption in real terms might also be encouraged by greater price stability.

Judging from the budget estimates, public consumption will expand less rapidly than in 1962.

The main feature of the trend in domestic supply in 1963 will probably again be a virtual absence of strain. Industrial production, according to the IRESP index, may well have a lower growth rate (about 3 %) than in 1962: in the most dynamic sectors of industry, particularly mechanical engineering, expansion will be held back as investment becomes slacker both at home and in Belgium's principal markets abroad. In the basic materials industries (iron and steel, non-ferrous metals and building materials) there is even a likelihood that output will not advance beyond its present level. On the other hand, the output of certain consumer durables and even of some traditional consumer goods will probably again expand quite fast despite keen foreign competition.

Assuming that agricultural production develops normally and that expansion in the services sector is somewhat slower in 1963, the gross national product may rise by about 3 % in real terms. Employment is likely to remain at the same high level as in 1962.

The supply of consumer goods from abroad might be slightly up on 1962. Total imports, however, will advance less rapidly than in 1962, mainly because of falling purchases of investment goods, but they may well have more or less the same growth rate as exports. In these circumstances, the balance of trade should show little change on 1962.

The expected results for 1963 will probably be achieved without much threat to internal equilibrium. Any increase in production costs resulting from the trend in wages and productivity will probably affect the margin for self-financing rather than the price level. Moreover, the Government has brought in a Bill to improve the scope for price policy and stimulate competition, affording wider possibilities for measures to promote expansion without endangering internal equilibrium. Internal liquidity will certainly

remain at an adequate level. Consequently a higher rate of public investment than is foreseen would not pose any special problems. Furthermore, new measures calculated to render the capital market more elastic may encourage firms to make more calls on long-term credit.

Moreover, this does not perhaps exhaust the possibilities open to the authorities for applying anti-cyclical policy in order to maintain a satisfactory rate of growth. It may be advisable to take further measures, especially if exports and more particularly industrial investment—for which forecasts are always more or less speculative—develop unfavourably.

In any event the situation may call for more vigorous measures to stimulate the growth of investment; otherwise it will be difficult to achieve long-term objectives. Here considerations of structural policy and the requirements of rationalization should be paramount. The establishment of the final version of the five-year programme (1961-1965) by the “Bureau de Programmation” should make it possible for both the public and private sectors to co-ordinate their activities more effectively in order to meet the targets set. If economic planning is supported by the principle of medium-term agreements between workers and employers, the authorities will possess the basic data to assist them in adjusting their growth policy measures to suit actual cyclical trends.

Grand Duchy of Luxembourg

In 1962 the Luxembourg economy failed to show any advance on 1961. The index of industrial production may well have remained some 5 % below the 1961 level. Agricultural production may have declined slightly but there was some degree of expansion in the services sector. On the whole the real gross domestic product may be said to be fractionally smaller than in 1961.

This development can be mainly attributed to the fact that overall demand failed to provide any stimulus to growth, and this was largely because foreign demand for iron and steel products was appreciably less than in 1961. Internal demand continued to rise but at a distinctly slower pace as the year went by.

Since the Luxembourg economy is dependent to such a great extent on trends in foreign steel markets, the outlook for 1963 is rather uncertain. At the moment there is no reason to expect a very sizeable recovery in steel exports. The growth of internal demand—which is likely to be slower—will probably hardly suffice to boost economic activity to any appreciable extent.

In these circumstances it would seem advisable to pursue a rather more vigorous expansionary policy. An important task for public finance is to maintain a sufficient increase in expenditure, irrespective of the trend in revenue, which will probably suffer as a result of the cyclical situation.

1. Balance-sheet for 1962

Exports, which are the vital factor in Luxembourg's economic development, made in general no further progress in 1962 and appear even to have dropped below the 1961 level. Deliveries of iron and steel products probably fell by about 4 % by volume after a slight increase of 2 % from 1960 to 1961. Exports of iron ore also dropped appreciably. Export prices continued to weaken, although not to the same extent as in 1961.

However, the annual figures obscure the way the economy has developed over the past two years. In fact the contraction of foreign demand for iron and steel had already begun in the second half of 1961; it continued in the first quarter of 1962 but then this trend came to a halt. In the first quarter of 1962 exports had quite an appreciable leeway.

to make up on 1961 but the gap narrowed in the course of the year and in the last quarter both sales and order books were probably at about the same level as a year earlier. It is significant that this recovery can be put down to a slightly more buoyant demand from the member countries of the Community, exports to non-member countries having remained at the 1961 level.

The year-to-year growth of internal demand was more favourable but nevertheless it showed a certain tendency to lose momentum in the course of 1962; particularly as regards gross fixed investment. True, equipment investment by firms for 1962 as a whole was again well in excess of the previous year but the propensity to invest steadily declined. In building, too, expansion lost momentum. Although public investment increased once more, to judge from the level of expenditure under the extraordinary budget, housing appears to have advanced less briskly. For the building sector as a whole growth was only about 4 % for 1962, compared with 11 % in 1961.

Despite an apparent recovery in the middle of the year, the growth rate of private consumption may well also have been less for 1962 than for the previous year. True, the income of persons in paid employment again increased, after moving up about 6 % in 1961. The rise in the numbers employed in industry and in building and construction was substantially greater than in 1961. However, about half the increase in the working population—a greater proportion than in 1961—can be attributed to the employment of foreign workers, who probably tend to save more than local workers. Moreover, wage rises in 1962 were not higher than in the previous year and in the steel industry bonuses even suffered a 10 % cut. Transfer expenditure by the public authorities does not appear to have grown as appreciably as in 1961 either. Finally, rising prices curtailed the real expansion of private consumption to a greater extent than in 1961.

In contrast with 1961, sales of consumer durables remained almost unchanged in 1962; purchases of motor-cars and radio receivers even failed to reach the 1961 level. On the other hand, expenditure on services was, if anything, higher.

Public consumption appears to have increased only slightly, i.e. at the same rate as in 1961.

Despite the slight fall in overall demand there was no easing of the tightness on the labour market. Firstly, there were fewer frontier and seasonal workers available, and secondly branches of industry whose output declined laid off hardly any of their workers. Finally, several new industrial firms began operations. By and large the number of persons employed in industry and building probably went up by over 2.5 %, as compared with only 1 % in 1961. Despite this increase which was accounted for solely by foreign workers, labour shortages continued, particularly in the building sector.

Mainly owing to the unfavourable trend in the steel industry, industrial production for 1962 appears to have been about 5 % below the level for 1961—when an increase of 3 % was still recorded. Here again the figures for the year do not entirely reflect the

general trend during the year; after falling in the second half of 1961 and the first quarter of 1962 output largely levelled off at the lower figure it had reached.

The output of crude steel was about 4 million metric tons in 1962 compared with 4.1 million in 1961. Few branches of industry raised their output in 1962 (January-October)—and then only moderately (e.g. non-metallic ores 3 %). By contrast in most sectors of the economy, output was in part well below the 1961 level (mining 13 %, food-stuffs, beverages and tobacco 7 %, textiles 5.5 %), as a result of generally weak demand and, in some cases, more for structural reasons.

Information on the trend in other sectors is still incomplete. Agricultural production in general, however, was almost certainly rather lower than in 1961. Services, on the other hand, may well have expanded, despite a decline in railway transport.

All in all the gross domestic product, at constant prices, was probably slightly lower in 1962, as against an increase of 3 % in 1961. The gross national product—which in Luxembourg is very strongly influenced by external factors (particularly the trend in the terms of trade and in factor income from abroad) is therefore a poorer guide to economic activity than the gross domestic product. This may have remained unchanged in 1962 or even have made a little progress.

Import trends, which were probably affected by certain special factors such as the growing tendency to purchase iron ore from abroad, also reflect the decline in economic activity.

The price level rose somewhat more rapidly than hitherto; the official retail price index, which had remained practically stable in 1961, rose about 1 point in 1962, mainly owing to an increase in the cost of household coal. However, the actual price rise may well have been appreciably steeper, though it can be considered moderate in comparison with the other member countries.

The cash position of the Treasury continued to be comparatively easy in 1962. True, the business trend was already having an unfavourable effect on current revenue, but in its expenditure the Government was very cautious. The national debt increased slightly in the first nine months of the year. A public loan for 500 million Luxembourg francs was issued in October—after being postponed owing to the satisfactory state of public finance—in particular to consolidate part of the floating debt.

2. Outlook for 1963

The outlook for international business and the foreseeable trend in internal demand—of which the growth rate will probably again decline—hold out little hope of a revival of economic expansion in 1963.

It is obviously difficult to forecast the development of foreign demand for iron and steel products, except to say that it is rather unlikely to increase very substantially in 1963. Firstly, a number of steel-using industries in the Community countries—particularly in the capital goods sector—will have to reckon on a fall in the growth rate of their production in 1963; consequently their policy on stocks, if not actually restrictive, is nevertheless likely to remain cautious. This will hinder the expansion of Luxembourg's steel exports within the Community. A certain increase can nevertheless be expected, but this may be partly or wholly offset by a continuing weakness in the growth of exports to non-member countries.

This situation may of course change in the course of 1963 especially if a business recovery in the United States in the autumn, as predicted by American experts, boosts world economic activity. But even if this does happen the figures for Luxembourg's steel exports in 1963 are hardly likely to improve very substantially.

However, the fall in prices for iron and steel products can scarcely continue much longer; some degree of stabilization or even improvement during 1963 would be quite conceivable.

Gross fixed investment may remain at a high level in 1963, but will not gain much more momentum. Investments designed to streamline the steel industry will be carried through as part of the expansion programme already embarked upon, but a decline in this sector in comparison with 1962 is not entirely impossible. In the other sectors of the economy the propensity to invest will be stimulated by the inflow of foreign capital and by public expenditure designed to improve economic structure. In building and construction a higher level of activity in the public sector—as a result of the extensive work now being carried out on infrastructure and of a recent decision to carry out a long-term programme of public building—will probably be accompanied by a slight decline in housing.

Private consumer expenditure should show a further, though only slight, increase. The effect of a rise in the total wage bill in the steel industry may be mitigated by a slight fall in employment and a further cut in bonuses. Furthermore, the increase in the total number of persons in paid employment will probably be smaller than in 1962.

Public consumption will probably increase very little, apart from the rise in civil servants' salaries.

The growth of internal demand being slight and the trend in external demand hesitant, no substantial expansion of industrial production can be expected in 1963 as against 1962. The same can be said of the gross domestic product as a whole. Nor is there likely to be any significant change in the state of the labour market, despite the fact that industrial expansion has virtually ceased and growth in the building sector has slackened, because, for one reason, the difficulty in obtaining foreign workers will persist.

Given these rather discouraging prospects for a further increase of production and income it may be advisable to intensify anti-cyclical policy and, in particular, to stimulate investment more vigorously, so far as the labour situation will allow. In structural improvement schemes, priority should again be given to investments aimed at reducing the dependence of the economy on the international market for iron and steel. Moreover, public expenditure (including that on consumption) might be designed to give a greater fillip to the economy. At any rate it would not be advisable to tie financial policy to the cyclical trend—in other words, to align expansion of public demand on that of public revenue, which, in view of the general business situation, will be slender.