

EUROPEAN
ECONOMIC
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**THE ECONOMIC SITUATION
IN THE COMMUNITY**

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JUNE

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EUROPEAN ECONOMIC COMMUNITY

COMMISSION

The Economic Situation in the Community

JUNE 1962

Contents

	<i>Page</i>
I. The overall economic situation	3
A. Demand	7
B. Supply	10
C. The balance of the markets	12
D. Outlook	17
II. The situation in each of the Community Countries	23
A. <i>Federal Republic of Germany</i>	25
1. Recent developments	26
2. Outlook	30
B. <i>France</i>	33
1. Recent developments	34
2. Outlook	38
C. <i>Italy</i>	40
1. Recent developments	40
2. Outlook	45
D. <i>Netherlands</i>	48
1. Recent developments	49
2. Outlook	52
E. <i>B.L.E.U.</i>	55
Belgium	55
1. Recent developments	56
2. Outlook	60
Grand Duchy of Luxembourg	63
1. Recent developments	63
2. Outlook	64

Graphs

1. Community trade	13
2. Businessmen's views on the industrial situation :	
a) (F.R. Germany)	27
b) (France)	35
c) (Italy)	41
d) (Belgium)	57
3. Annex : Wages, productivity and wage costs in industry	68

I. THE OVERALL ECONOMIC SITUATION

The economic growth of the Community appears to have quickened somewhat in the first quarter, although expansion at the moment cannot be termed particularly vigorous.

True, exports to non-member countries went ahead only rather hesitantly at times—owing principally to slower expansion in most industrial countries—but demand at home continued to grow quite appreciably. Private consumption, for instance, showed a distinct increase in the early months of the year; this was chiefly a result of the steady rise in wage incomes, which in turn was largely due to higher wage rates. At the same time there was—despite forebodings at the turn of the year—no increase in the tendency noted in the second half of 1961 for total outlay on fixed investment to slow down—the one exception being building, which was adversely affected in February and March by the exceptionally bad weather. Moreover, firms in the processing industries are beginning to show a more positive attitude to investment in stocks of semi-finished goods.

In the first quarter of 1962 the growth of industrial production in the Community was slightly below that of the fourth quarter of 1961. The March figures in particular were rather discouraging as a result of certain special circumstances of a climatic and statistical nature, with the result that the year-to-year growth rate fell from 6.5 % of production in the fourth quarter of 1961 to 5.5 % in the first quarter of 1962. In April, however, there were again signs of an appreciable improvement.

The way output developed was governed by and large by the trend in demand—if the unusual influence of the weather is left out of account; in a number of industries, however, expansion continued to be restricted by the shortage of manpower. With unemployment still very low in most member countries, employment has been rising slightly again. Since at the same time further cuts in the working week were made during this period, particularly in Western Germany, the rise in the total number of hours worked was not correspondingly large. In the first quarter, imports as a whole, again rose faster than exports, causing a further deterioration in the Community's balance of trade. Once import figures had been adjusted to eliminate the effects produced by certain special factors of a purely statistical nature, the deficit comes to \$ 275 million, as against \$ 133 million in the first quarter of 1961. Since March, however, there have been signs of a slight tendency towards improvement.

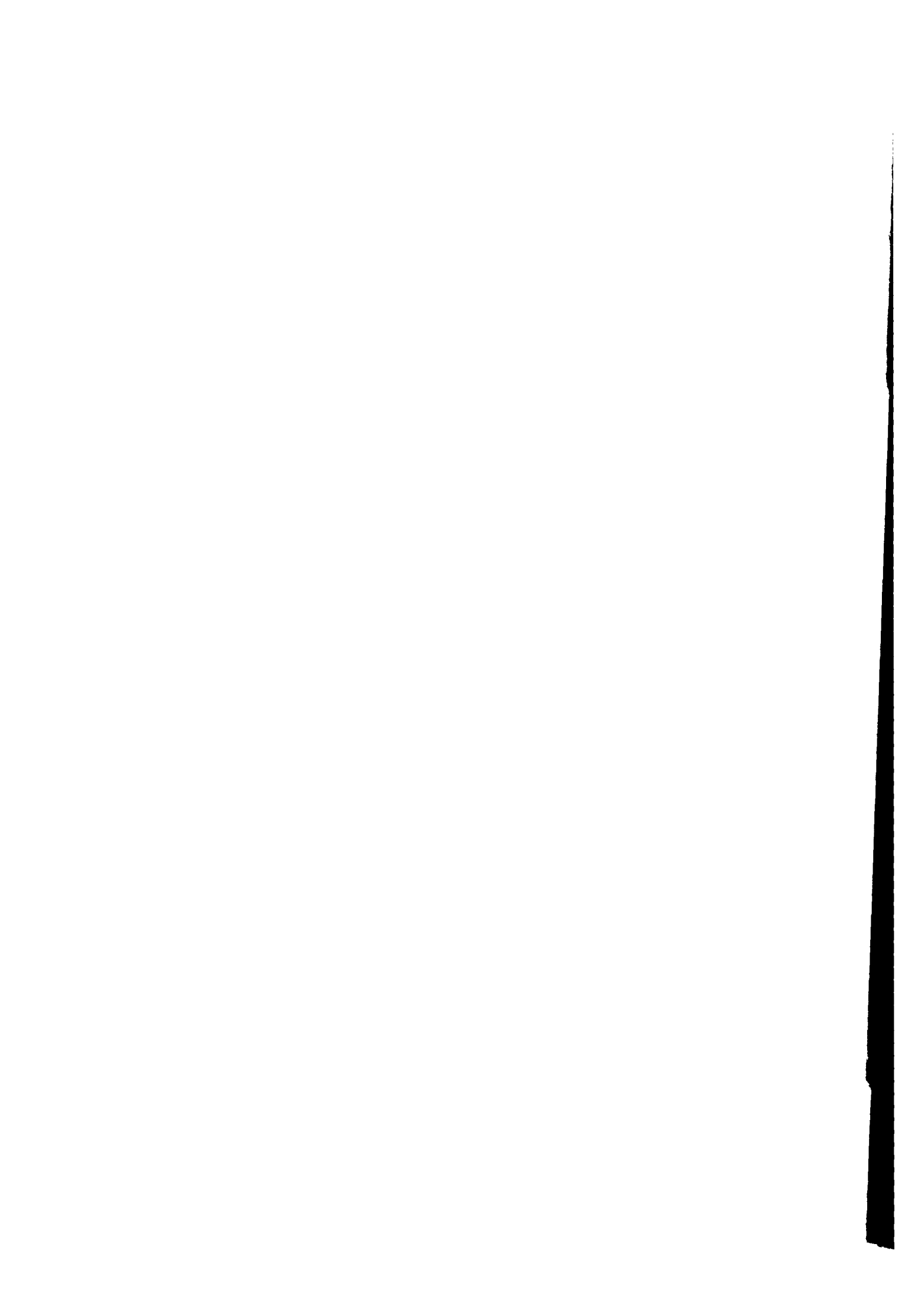
Despite the deficit on trade and renewed official exports of capital, especially in the form of advance debt repayments, the balance of payments showed a considerable surplus. True, the gold and foreign exchange reserves held by the monetary authorities in the member countries fell by \$ 300 million in the first quarter. This was however offset by a much greater improvement in the net foreign holdings of the commercial banks.

The price rises which have been going on for some time did not slacken in the early months of the year. Higher prices for some foods, due largely to poor harvests and the effects of the long cold winter, even caused the rise in the level of consumer prices to be even somewhat steeper.

The outlook for the second half of the year suggests by and large that expansion will continue. Community exports to non-member countries might even grow somewhat faster and internal demand may well keep on increasing. The rise in fixed investment is tending in general to continue but in some member countries it is still slight. Private consumption will still expand vigorously, even though in some countries a certain slackening can be expected in the pace at which wages are rising.

All in all there is no reason to make any fundamental exchange in the forecasts given at the beginning of the year; it is still reckoned that in 1962 industrial production will show an annual growth rate of 5.5-6 % and the gross product of the Community 4.5 - 5 %.

If, however, this is to occur—and especially if the trend is to continue upward in 1963, investment activity must continue to grow. The first aim of economic policy must therefore be to ensure that no further retarding influences gain a hold in this field. To achieve this, not only can measures to combat rising prices be used, but in general terms, too, workers can be encouraged to save and other measures taken to increase the chances of financing investments through borrowing on the capital markets and to improve the terms on which the funds can be borrowed.



A. Demand

The growth of overall demand may have increased its pace slightly in the first quarter of 1962 and more especially at the end of this period, although this does not mean that it could again be called rapid.

The figures for *demand from abroad*, as reflected in the Community's exports, had, after seasonal adjustment, shown an actual decline in the fourth quarter of 1961 and were rather weak in January, but in February they levelled out and showed a slight recovery in March. For the whole of the first quarter, exports to non-member countries were 4 % in value and 2 % in volume above the corresponding figures for the previous year; their rates of growth had been about 10 % in the third quarter of 1961 and had fallen to 3.7 % in the fourth.

It is obviously too soon to say to what extent this recovery will gain strength and prove lasting. In any case the Community's exports in the first quarter were still largely influenced by the distinct slackening in business expansion which was observed in many non-member countries in the second half of 1961 and the relative weakness of demand from the developing countries.

Lastly, the rise in costs in several Community countries and higher export prices following the revaluation of the mark and of the guilder may well also have had a braking effect on exports. The other factors mentioned would seem, however, to have been more important.

Exports to the United States in particular developed very favourably; in the first quarter their value was 25 % higher than a year earlier (in the last quarter of 1961 the rise had been 15 %). This growth is very remarkable, even when it is recalled that in the first quarter of 1961 there was a decided drop in the level of exports, which reached the bottom of the decline caused by the recent recession in the USA.

The expansion recorded in January to March 1962 occurred despite the loss of momentum in the American recovery. The gross national product and industrial production both showed an increase of only 1 % over the last quarter of 1961. It is true that private consumption continued to grow appreciably, but the development of fixed investment by enterprises was relatively weak. Again, exceptional weather conditions hampered business activity. From March onward the upward movement became once again more marked benefiting in particular from developments in the housing sector.

In exports from the Community to EFTA the outstanding factor was the relative weakness of demand from the United Kingdom where there was a slight recession due in part to restrictive measures taken mainly by the monetary authorities in the middle of 1961 : after seasonal adjustment, industrial production figures sank between July 1961

and January 1962 by 3 %. This trend and its effects on the United Kingdom's overall imports are reflected in the Community's exports to that country; in the first quarter of 1962 these were 4 % in value below the level reached a year previously. For this reason, sales to EFTA members as a whole showed a year-to-year improvement of only 6 % in the first quarter of 1962, although the development of exports to the United Kingdom's six EFTA partners was better than this. Despite all this the slackening in the rate of expansion observed in the second half of 1961 did not persist.

By and large, the Community's exports to the developing countries remained very slightly below the corresponding figure of the previous year, but there does not seem to have been any further downward trend. Exports to Latin America have, however, been strikingly weak; they were, it is true, about 7 % up on the figure for the first quarter of 1961, but in the previous quarter the year-to-year growth rate had been 17 %. This development is an obvious reflection of the shortage of foreign currency in the Argentine and in Brazil. By contrast, exports to the Commonwealth countries seemed to be resuming an upward trend, even if they were still below the 1961 figures. Exports to overseas countries associated with the Community, except Algeria, continued to grow, though more slowly than in the past.

While in the first quarter overall demand from abroad lost no ground—nor did it show any advance on the last quarter of 1961—domestic demand seems to have had a quite definite tendency to improve.

For example, the distinct tendency for *fixed capital asset* formation in the Community to slow down in the second half of 1961 does not seem to have become more marked. In some member countries, there may even have been some slight recovery. It is true that so far there is no sign, judging from the plans of enterprises in the private sector, of any noteworthy quickening in their propensity to invest. An increase in the delivery capacity of the capital goods industries has led to a higher rate of expenditure in connection with existing programmes and orders although in certain member countries it is becoming increasingly difficult for firms to finance growing investments from their own resources. For this reason among others there has been a general increase in calls on the capital market—although there are still structural difficulties which limit the offer of funds and although the terms available, in particular the cost of credit are not very attractive. In addition the growth of investments in some member countries is now being reflected increasingly in the expansion of (nominally) short-term credit.

In the construction sector, however, the slight upward trend in fixed investment was masked for a time in the first quarter by the effects of exceptionally unfavourable weather. On the other hand, potential demand, to which public investment projects made a considerable contribution, was at a very high level and was slowly rising. In some Community countries the total demand was again well in excess of the available supplies. For the reasons mentioned, completions in the first quarter were lower than in the same period of 1961. This applies in particular to the number of dwellings completed, which were down 7 %.

Investment in stocks seems to have begun a distinct recovery after the decline recorded during 1961 (stocks of some raw materials and semi-finished products had even been cut in certain processing industries). In the fourth quarter of 1961, there had already been signs of improvement in the stocks of imported raw materials, but here the trend was not maintained in the first quarter of 1962. There was however much less readiness in the first quarter to run down stocks of semi-finished goods and basic products, particularly with steel and steel products; purchases began once more to keep in step with current output.

The upward trend in *public expenditure on investment and consumption* continued in all member countries and even gathered pace in some. Mention has already been made of the part played by this factor in investment, once allowance is made for the spells of unusually bad weather. At the same time, public expenditure on consumption, especially in the form of increased expenditure on employees was also higher.

In the first four months of 1962 ⁽¹⁾ *private consumers' expenditure* went ahead at the same fast rate as in the last quarter of 1961 in all member countries, except Belgium and the Netherlands. Expansion in real terms, however, suffered somewhat from the more rapid rise in the level of consumer prices. The main factors in the expansion of consumption were once again wages, salaries and transfer incomes, while the contribution made by the expansion of employment was, partly for seasonal reasons, of less importance. Wages in the three larger member countries went up rather fast—the steepest rise was recorded in Western Germany; the increase in France was a little less rapid, and in Italy it was still very considerable. In Belgium the rise in wages speeded up, but did not become as rapid as in the other countries. Some wage increases also took place in Luxembourg, while in the Netherlands wage rates remained unchanged in the first quarter, due to delays in renewing and implementing collective agreements.

The structure of consumption expenditure was distorted somewhat by higher prices for foods—where demand is relatively inelastic in relation to prices—and this meant the outlay on perishable consumer goods suffered, though expenditure on consumer durables, particularly motor cars, even went up on the whole (except in Belgium) faster than overall expenditure on private consumption.

(1) The different dates of Easter in 1961 and 1962 mean that April should be included in this comparison.

B. Supply

According to the information available total domestic supply in the early months of 1962 increased at much the same pace as in the last quarter of 1961.

In the *agricultural sector*, however, crops suffered as a result of the bad weather and, as early as March, but more particularly in April/May, this was reflected in higher prices, especially for vegetables. Livestock production, on the other hand, showed a further distinct rise in the Community, even though dairy products were rather badly affected by the cold weather and the exhaustion of fodder supplies coupled with the lateness of the fresh crop.

The growth rate of *industrial output* in the Community, according to the indices available, was slightly weaker in the first quarter of 1962 than in the last quarter of 1961. The March figures in particular were unfavourable in almost all member countries, but this can largely be put down to special factors of a climate and statistical nature. In April an appreciable recovery was already apparent. According to the index of the Statistical Office of the European Communities the level of production in the first quarter was 5.5 % up on the corresponding period of 1961—after a year-to-year growth rate of 6.5 % had been recorded in the fourth quarter of 1961.

In most branches of industry the trend of production remained essentially the same as in the last months of 1961. For example, the investment goods industry, chemicals and foodstuffs continued to expand production quite appreciably. The motor car industry continued to expand production after the recovery which occurred at the end of 1961 through the Community and more especially in France, although sales of utility vehicles were still slack, owing mainly to the weakness of exports. There was some improvement in the situation in the iron and steel industry, where the downward trend in output seems to have been overcome with the volume of sales to non-member countries also developing satisfactorily. In most sectors of the textile and clothing industries output was at a low level but continued to develop. In coal mining the production trend was still downwards while in some countries specific measures to rationalize and restrict output assumed greater importance. The general expansion of economic activity failed to stimulate production, as the continued replacement of coal by other forms of energy has exerted a greater effect on output than the general economic trend. The exceptional weather in the first quarter, however, led to a temporary recovery in consumption and this was reflected in most member countries by a reduction in pithead stocks.

In the *services sector* expansion continued unabated. The wholesale and retail trades and the tourist industry benefited in particular from increased private consumption. In the transport sector a slight year-to-year increase was recorded in the first quarter by the railways and by shipping.

The number of persons in paid employment went up again in all member countries, though the rise was—partly for seasonal reasons—smaller than in the second half of 1961. The rise was largely brought about by migration within the Community, particularly to Western Germany, but greater recruitment of manpower from non-member countries also played a part. Except in Italy, where the trend was naturally influenced by the heavier emigration which helped to raise the employment figure in the other countries of the Community, the fall in unemployment did little to raise the number of those in employment. True, seasonally adjusted unemployment figures continued to fall, even in those countries where labour reserves were already very low indeed; but the resulting rise in the number of employed is relatively unimportant. The increase in the volume of labour (number of employed multiplied by the number of hours worked per person employed) was again less than the increase in employment, since in Western Germany and—to a smaller extent—in the Netherlands there were further cuts in the working week—and once again these cuts were made not because of any change in the economic situation, but as a direct result of collective agreements.

C. The balance of the markets

The trend in the Community's *imports* was the reverse of that in exports, but not quite so distinct. In January and in some countries still in February imports increased substantially, while in March and again—so far as can be judged from incomplete figures—in April they went ahead somewhat more haltingly. Total imports from non-member countries in the first quarter were about 7 % ⁽¹⁾ in value above the corresponding period of the previous year, producing practically the same year-to-year growth rate as in the fourth quarter of 1961.

Community imports continued to expand under the influence of the rather poor harvests in 1961. In addition, further expansion of demand for investment goods brought with it a decided increase in imports of engineering and electrotechnical products, especially since some branches of the investment goods industry in several member countries were still only able to make limited deliveries. While the growth of imports of semi-finished goods gathered some momentum, mainly because some branches of the processing industries were no longer trying to run down stocks, the expansion of industrial production in the Community was not sufficient to provide any very large fresh stimulus to imports of raw materials.

The trends outlined above are reflected in the breakdown of imports by areas of origin. Imports from the United States still showed a slight tendency to rise, and in the first quarter were up by about 7 % on the 1961 level.

The increase in imports from EFTA was somewhat sharper (some 13 % above the 1961 level), with purchases from the United Kingdom showing a special recovery (with a year-to-year growth figure of about 24 %), due in no small measure to the difference between the economic situation in the United Kingdom and in the Community. Imports by the Community from the developing countries and other producers of raw materials were again, as in the last quarter of 1961, about 5 % higher than a year earlier.

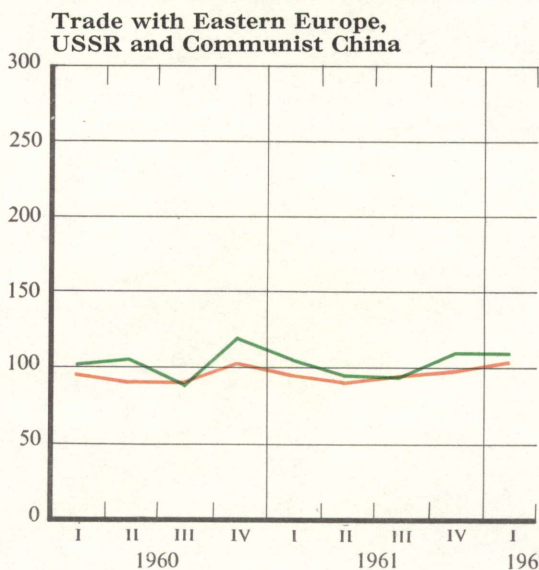
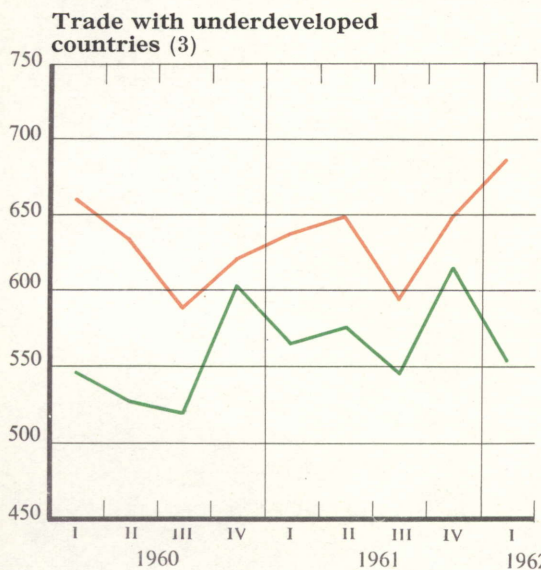
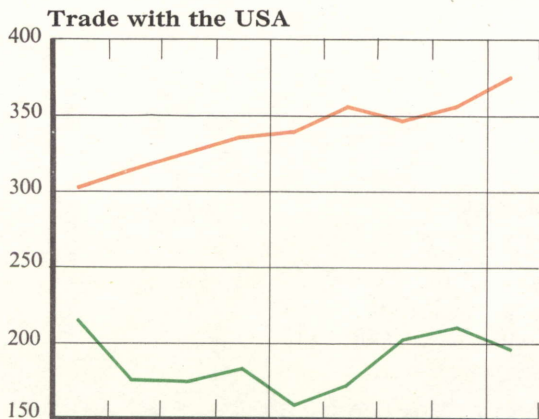
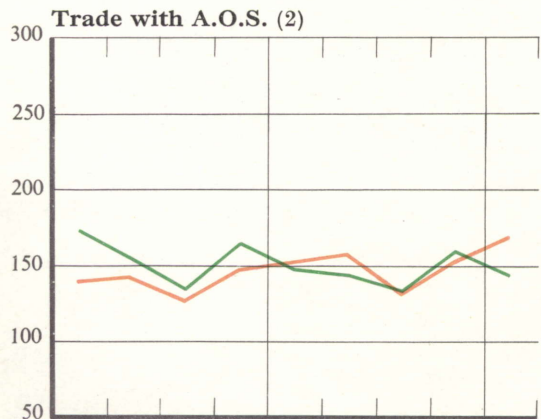
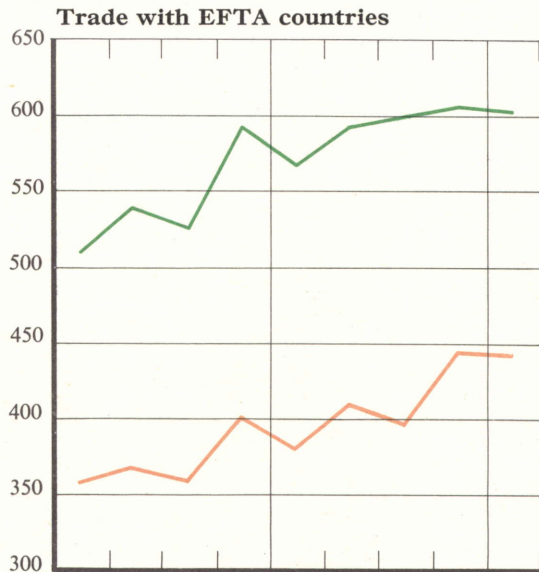
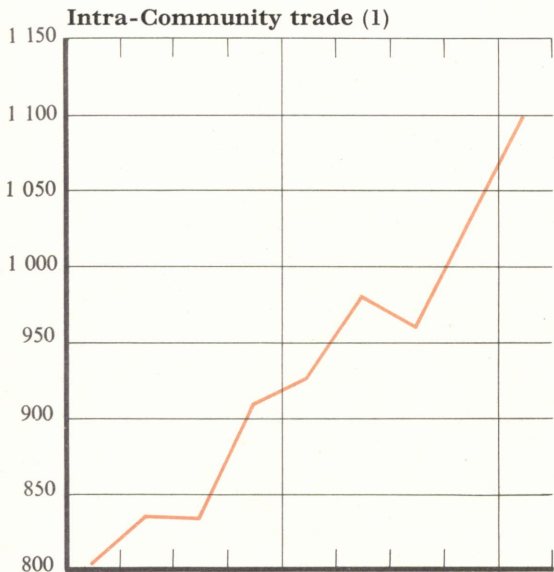
The growth of *trade between Community countries* once again gathered momentum in the first three months of 1962. In terms of value a year-to-year growth rate of some 16 % ⁽¹⁾ was recorded after a figure of almost 14 % in the fourth quarter of 1961. This spurt is partly explained by the 10 % cut in tariffs within the Community which came into effect on 1 January 1962; in anticipation of the cut importers were holding back in the last months of 1961 and imports from member countries were correspondingly higher in the first weeks of 1962. This was in addition to the long-term basic effect of the tariff cuts, which will intensify trade between Community countries. Furthermore the factors which

⁽¹⁾ Adjusted on the basis of estimates to eliminate purely statistical increases, affecting in particular the figures for January; in France there were certain changes in the method of collecting statistics, and in Western Germany goods stored in bonded warehouses were brought into the import figures, though they belong economically to 1961 or even earlier periods.

COMMUNITY TRADE

Monthly averages

In millions of dollars



— Exports

— Imports

(1) According to import returns.

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

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

exerted an influence on the Community's external trade in general, of course affected trade between Community countries as well : trade in agricultural products was heavier as a result of poor crops in the second half of 1961 and in spring of 1962 (although the degree to which each country was affected varied) and trade in investment goods, transport equipment and consumer goods continued to rise steeply, while semi-finished goods experienced a slight recovery.

The balances of the various member countries on their trade within the Community showed no great tendency to change. Western Germany continued to have the largest surplus—almost as large as in the first quarter of 1961 once allowance is made for special statistical factors—and the Netherlands the heaviest deficit, which was also on practically the same scale as in the first quarter of 1961. This means that Western Germany's imports went up faster than exports, while just the opposite happened in the Netherlands. Italy not only had the highest year-to-year growth rate for exports (about 30 %), but imports also went up almost as steeply, so that the Italian deficit on trade with EEC increased slightly. In France, too, imports from other EEC countries tended to rise steeply and as this rise was steeper than the rise in exports, the surplus fell slightly. A surplus was recorded in the Belgo-Luxembourg Economic Union, contrasting with the first quarter of 1961 when trade had suffered from the effects of the strikes.

Even though trade between the member countries and imports from non-member countries had a certain stabilizing effect on *prices*, in the early months of 1962 there was still no slackening in the price rise which had been gathering pace since the middle of 1960. Except in France consumer prices in general rose even a little faster than in the last quarter of 1961. In Western Germany, France, Italy and the Netherlands they were in April on average about 5 % higher than a year earlier. Much of this increase was due to the higher cost of certain foods for which the poor harvest in 1961 and the bad weather at the beginning of 1962 were chiefly to blame. Services continued to cost more and more, with a fresh rise in controlled rents in France and Italy adding some impetus to the general trend.

Furthermore, the price of a number of industrial products rose more rapidly than before, not so much owing to any *ex ante* imbalances between supply and demand—for these have if anything been growing smaller—but rather as a result of the increase in wage costs, which has in part been passed on to the consumer. Building was the only sector where considerable excess demand continued to exert pressure in some countries.

The more rapid increase in imports than in exports is reflected in a deterioration of the Community's *balance of trade* which showed a deficit of some \$ 275 million in the first quarter, after elimination of the effects of the special statistical factors on imports. The deterioration in comparison with the last quarter of 1961 was quite considerable even though part of the fall was due to seasonal factors. In January the underlying trend was still towards a heavier deficit, but in February it levelled out and in March and April there was even a turn for the better.

The Community's *balance on current account* appears to have followed the same trend as the balance of trade but without showing a deficit. A large surplus was recorded on the overall balance of payments although once again there were considerable special transactions with non-member countries in the early months of the year, as, for example, further advance repayments of public foreign debts. Although the *gold and foreign exchange reserves* held by the monetary authorities of the Community countries fell by a total of about \$ 300 million, the net foreign exchange position of the commercial banks showed a much greater improvement than previously.

In the early months of the year the trend in the balance of payments tended to increase the level of *liquidity* in business and the banks. The current economic situation is however such that the funds available are more and more being converted into effective demand. In some member countries for example, the expansion of credit gathered momentum especially as firms were finding that they had smaller profits and less liquidity, due in no small measure to the fact that the increase in costs was greater than the rise in prices. In the early months of the year banking business showed signs of strain and at times money-market rates went up quite sharply. In Western Germany, France and the Netherlands a factor in this development was the way in which *Government cash surpluses*, due partly to seasonal influences, reduced the level of liquidity. In Italy and Belgium, on the other hand, there was a deficit, though in Belgium this was smaller than in the corresponding period of 1961.

By and large the monetary authorities of the member countries refrained from policies liable to increase liquidity and confined themselves to dealing with any strains that appeared. In some member countries the authorities even sought to put a brake on the use of liquidity to expand credit—by raising minimum reserves and Bank rate and, in the Netherlands, by retaining quantitative restrictions on the expansion of the volume of credit—or to channel short-term savings in various ways into forms of longer-term investment, as is being done in France. Bank rate was again gradually lowered in Belgium, but this was basically to adapt it to the vastly improved balance of payments.

D. Outlook

The trends which emerged in the early months of 1962 and have probably persisted in the second quarter, to judge by various indications already available, are not on the whole likely to alter very much in the second half of the year. Exports to non-member countries may speed up slightly and internal demand will probably advance somewhat more slowly. In any case there will be only minor changes in the rate of growth, so that no basic revision is required of the forecasts drawn up at the beginning of the year ⁽¹⁾ for the whole of 1962 of the trend in supply and its main outlets.

As for *exports to non-member countries*, the information available on the economic trends in those countries indicate that exports of industrial goods from the Community should increase slightly in the coming months, despite the rise in costs that has already occurred and is likely to go on in a number of member countries, where it is more serious than in some important non-member countries. Given normal harvests, agricultural exports will probably also make more rapid progress in the second half of the year.

That the trend in costs has not yet seriously jeopardized the competitive position of any member country is evident from the latest trend in the balances of transactions and the overall balances of payments. One point however must be noted : under no circumstances can the rise in costs be allowed to maintain the pace recently experienced in most member countries, for even if in important non-member countries costs should start to move up again more rapidly, the competitive position of the Community could still suffer too seriously in the long run.

At the moment, however, costs are still at a level which ensures that the Community will be able to benefit from the upsurge of economic activity in the United States by increasing its exports always assuming that an increased tendency to partial protectionism does not gain the upper hand, despite the generally very liberal commercial policy pursued by the Administration, and make it impossible for major imports from Community countries to enter the United States.

In any case such a step would not be justified by the balance of trade, since for over a year the Community has been increasing its imports from the US much more than its exports to that country. At \$ 1 800 million, the Community's deficit on trade with the United States was in 1961 considerably larger than in any of the preceding three years. Apart from this consideration, measures of a partly protectionist nature are in general unlikely to serve any useful purpose in a policy designed to improve employment, the balance of trade or even the balance of payments.

At all events the outlook for the American economy till the end of 1962 seems to be still one of expansion, even though the upsurge will probably not be strong enough

⁽¹⁾ See Quarterly Survey 1/62 "Economic situation of the Community".

for the factors of production to be employed to the full unless substantial steps to improve expansion are taken soon. It will probably fall short of this because of certain structural characteristics of the American economy and, according to many experts, of the American fiscal system, and also because of certain repercussions the latest events on Wall Street might have on the economy. Nevertheless Community exports to the United States will probably continue to show quite high growth rates.

The outlook for exports to the United Kingdom, on the other hand, is less encouraging. However, they are expected to rise slightly, since economic activity in that country is showing something of a recovery stemming chiefly from the relaxation of the credit squeeze and the end of the pay pause. Community exports to other European countries will probably continue to grow, even though perhaps at a somewhat weaker rate than previously. As for sales to the developing countries, a slight recovery may perhaps be expected, particularly since several of them appreciably improved their foreign exchange position in 1961.

By now, there can be little doubt that the internal demand of the Community will continue to rise in the second half of 1962 and that the rise will be considerable.

For instance total *fixed investment by enterprises* will continue to expand. The expansion may even be rather substantial in several countries, as for example Italy and France, where the latest figures indicate that actual investment will undoubtedly be on a larger scale than appears from the investment programmes drawn up at the end of 1961 and beginning of 1962. In Western Germany, where the number of orders received in recent months fell below the corresponding 1961 figure, and in the Netherlands, where investment was hampered by the restrictive money and credit policy and the changes made during 1960 in the regulations governing depreciation allowances, investment will, it is true, be very high but its further growth will probably be relatively slow—although in both countries the labour shortage and rising wage costs provide incentives for firms to invest in rationalization.

Public investment will continue to rise briskly, especially in Italy, France and Belgium. In the building sector there will often be manpower shortages which will set limits to the progress of output. Measures taken to restrict building demand in the Netherlands and, more recently, in Western Germany will help to restore the equilibrium of the market but will probably not fully achieve this aim in the current year.

Private consumption will again advance rather vigorously. True, Western Germany can despite everything expect to see a slight slackening in the rapid rise in wages as a result of the weakening of economic expansion, smaller profits and certain signs that the strain on the labour market is easing. In the Benelux countries, however, and more especially in the Netherlands, the upward trend in wages may well gather momentum and it will remain substantial in France and Italy. On top of this a further increase in employment can probably be expected. Finally, transfer incomes (pensions, family

allowances, etc.) are being raised considerably in most member countries; the rise will be even greater than in 1961.

According to the figures at present available *public expenditure on consumption* will continue to expand as before; in particular there are likely to be salary increases in the public service.

The prospective trend in total demand seems to allow of renewed growth in the Community's *industrial production*, although growth is still restricted by labour shortages in some sectors. By and large it seems that the estimate of an annual growth of 5.5 to 6 % in 1962 will prove to have been correct.

Naturally enough little can be said at the moment of the outlook for *agricultural production* since much depends on the weather in the coming months. The area of land under wheat has been increasing considerably and, after a drop in 1961, is now slightly above the 1960 level. In any case the supply of pigs and poultry can be counted on to show a substantial rise.

The growth of *imports* is likely to be at best rather hesitant, especially if the 1962 harvest is better than that of 1961 and if there is no marked stockpiling of raw materials—of which there is no sign in most member countries at present. Imports of industrial products at any rate will record a further advance.

In these circumstances it is quite possible that the Community's *balance of trade* will tend to show a slight improvement once again. However, the year-to-year figures suggest that the balance of trade will—if only because the rise in imports in the last quarter of 1961 and the first two months of 1962 was perceptibly greater than the rise in exports—be somewhat less favourable than it was in 1961, and will close with a modest deficit. On this point, too, and also with regard to the balance of transactions, there is no change in the outlook described in the last report. The overall balance of payments will probably continue to show a large surplus.

Prices are likely to rise more slowly once price conditions for vegetables, potatoes and fruit return to normal, while the cuts in internal tariffs on 1 January and 1 July will also have a stabilizing effect. Finally, the rise in wage costs also seems to be slowing down somewhat since the increase in productivity may recover slightly and since the upward trend in wages is—although only in the Federal Republic—losing some momentum. Prices of industrial products and services must none the less be expected to show a further rise, as firms will wish to maintain their profit margins and their scope for self-financing.

Development since the beginning of 1962 and the outlook today have made little change of substance in the problems and tasks of *economic policy* which were dealt with in detail in the last survey (Quarterly Survey 1/1962).

This applies particularly to the problems raised by the divergent developments in wages and productivity—indeed, the whole problem of the rise in costs per unit of output—and the repercussions of these problems on the price level and on the outlook for business and for economic growth.

The degree of success which will attend efforts to stabilize the trend in costs will depend upon the effectiveness of the policy followed in stabilizing prices. It is therefore to be welcomed that the authorities of the member countries are devoting more and more care to stabilization of prices.

This policy must not however overlook the problems and requirements of real economic growth—especially since it is after all just in this field that mistakes could jeopardize the success of efforts to stabilize costs.

In the endeavour to exert pressure on the level of prices and costs, every possible means of increasing supply should be tried before anything is done to limit demand, i.e. governments could do more to promote—as far as possible on a Community basis—occupational training and the occupational and geographical mobility of labour, and substantial tariff cuts could be made on trade with other member countries (under Article 15 (2) of the Treaty) and with non-member countries, provided this does not bring the duties below the level agreed in the common external tariff (less 20 %).

Here a twofold action is needed : an attempt should be made to use selective tariff cuts, as has recently been done in Western Germany, in an endeavour to influence key markets and prices which exert a significant psychological influence in the business world; at the same time since prices and costs are rising on a fairly broad front, the widest use of advance tariff cuts is desirable, as such cuts affect the economy in depth and affect semi-finished goods, which are themselves a factor in costs. All member countries where such measures would be appropriate are still in a strong enough position as regards balance of payments and reserves for tariff cuts to be perfectly feasible. In fact, some even have such large surpluses that these are precisely the type of measure called for, since they would boost imports.

On the other hand, the present economic situation calls for the exercise of some caution over measures to restrict the growth of internal demand, especially where these measures are designed to curb investment. For it must be borne in mind that the upswing of investment by private firms has already slowed down in most member countries and that some of their investment plans betray a certain flagging in the propensity to invest. At the same time this trend does not appear to have been offset in all member countries by an additional rise in public investment.

True, there can be no harm from the point of view of economic policy if in some member countries the investment boom levels off—it can even be a good thing from the price angle; however, an unduly rapid drop in investment activity while consumption was

still rising would mean a most undesirable change in the use made of the national product, and this is an important factor in the rate of real long-term growth. Economic policy should not make such an attempt to change the pattern of growth in the short term merely because private consumption is in one or other member country at the moment rising too fast for the maintenance of price stability.

By and large it does not seem that general measures to limit the growth of investment demand are today still to be recommended in most member countries. It may be true that in those countries where the balance-of-payments position is not too strong there is a better chance than in the past that such measures could bring total demand into line with total supply. But in that case the pressure on investment would have to be fairly intense if it is to offset the effect of the vigorous expansion of consumer demand on prices and/or the balance of payments, especially since in some member countries the expansion of consumer demand is being further boosted by tax reductions and substantial increases in pensions and similar payments. It must in any case be realized that the price of more rapid harvesting of the fruits of past economic expansion must be slackening in the actual growth of national income and of the standard of living in the long run and this might even lead in the direction of a recession.

Restrictions on credit and the higher cost of credit would set a special problem if they actually heavily curbed the growth of private investment, which is already labouring under certain difficulties due in no small part to the reduced possibilities of self-financing. True, the propensity of firms to invest should hardly be seriously impaired by the fall in share prices on the stock exchanges of the member countries, since longer-term expectations for the economic development of the Community are very optimistic—and with good reason. But these falls could none the less make it more of a problem to finance investment, as they upset for a while at least the floating of new issues by industry and in a number of cases may even cause the banks to exercise more caution in allowing credit.

In these conditions it is quite definitely not desirable at the present time to maintain global demand through an expansion policy. In any case, as far as financial policy is concerned, it would seem better, if anything, to hold expenditure growth on a tight rein. Again it is or would be advisable for the member countries to follow money and credit policies intended to maintain favourable financing conditions on the credit markets. Serious thoughts should also be given to doing more than has so far been done to swell the flow of funds to the capital markets by encouraging workers to save. Not only would this dampen the effect on consumer prices of greater demand stemming from the rise in consumer incomes, but it would also have favourable repercussions from the point of view of the distribution of wealth, and, even more important, it would counteract the changes noted in the relative weight of items in the national product by increasing the importance of consumption.

It would however be wise to curb demand in the building market wherever it appeared to be under considerable strain. But here too the targets set would have to be

co-ordinated and due attention paid to considerations of growth policy—and in particular to the requisite extension of the infrastructure—if there are not later to be dangerous bottlenecks in growth. From this point of view there does not seem to be much point in, for example, reducing funds for road building—especially where it is clear that capacity and labour are by no means being used to the full in this sector of construction.

This example brings out the fact that economic policy in the modern economies of the member countries, where growth tends to be rapid, needs for its guidance a medium- and long-term growth policy which would co-ordinate developments in the economic, financial, agricultural, transport, social and other fields in the light of forecasts covering the economy as a whole. Only with the aid of such a growth policy will it be possible to see which points of attack and margins for manoeuvres must, and can, be decisive for economic policy today. The need for this will soon be evident from the decision, taken by the representatives of the member countries in the Economic Policy Committee, under which the practice of making annual general economic forecasts is to be generalized. The fact that it is also precisely medium- and long-term policy that must be co-ordinated in the framework of the Community and be merged increasingly in a common policy is self-evident, since this development lies at the heart of the economic union and is its *conditio sine qua non*. It seems, too, that it is on the basis of these long-term forecasting methods that a judicious income policy and policy with regard to the distribution of the increase in national wealth can be framed and best achieved.

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

A. Federal Republic of Germany

Economic expansion was maintained in the first quarter and probably also in the following months, although in the building and allied sectors particularly growth suffered from the bad weather experienced in February and March. Exports made some progress and the slackening, noted during the second half of 1961, in the rate at which investment was expanding hardly seems so far to have gone any further. The steady vigorous rise in incomes, and especially in wages, boosted the expansion of private consumption.

By and large the labour market remained under strain. Nevertheless industrial output, apart from seasonal factors, advanced slightly, especially as demand due to stock-building was no longer on the decline. Imports increased substantially. For the first time in many years a deficit was recorded on current account. Prices went up again, owing in no small measure to rising costs.

On the whole the outlook for the second half of the year is by no means unfavourable, even though it contains some elements of uncertainty. Exports may well make further progress but their expansion may be relatively slow, partly as a result of the deterioration in Germany's competitive position. Investment expenditure will also keep on growing; as yet, however, there is no evidence of a recovery in the propensity to invest. Such a recovery will probably be needed if in the long term the optimum use of productive capacity in the investment goods industries is to be ensured through follow-up orders. Private and public demand for building and construction, on the other hand, will probably remain so high for the time being, despite the recent measures to curb building activity, that no decisive easing of the strain on the building market can be expected. Private consumption, too, will again rise appreciably.

The upward trend of production will probably continue, although it may well be hampered by the labour shortage and the weakening of demand in some sectors. Imports will continue to increase but possibly at a slower rate. The tendency for wages and costs to rise will persist, but the pace of the rise may slacken somewhat.

Both the developments observed so far and the outlook for the second half of the year are on the whole in line with the general forecasts given for the full year 1962 in the first quarterly survey of 1962, so that no revision of these forecasts is called for.

1. Recent developments

Exports of goods and services may have picked up again somewhat in the first months of 1962. The foreign trade statistics show that in the first quarter of 1962 the year-to-year growth rate for goods exported (in terms of value) was 3.2 %, whereas in the last quarter of the old year it had shown a slight decline. In April, however, exports advanced rather weakly, but this is probably largely because Easter fell late this year. The trend in earnings from services may also have been somewhat better in the first quarter than in previous months.

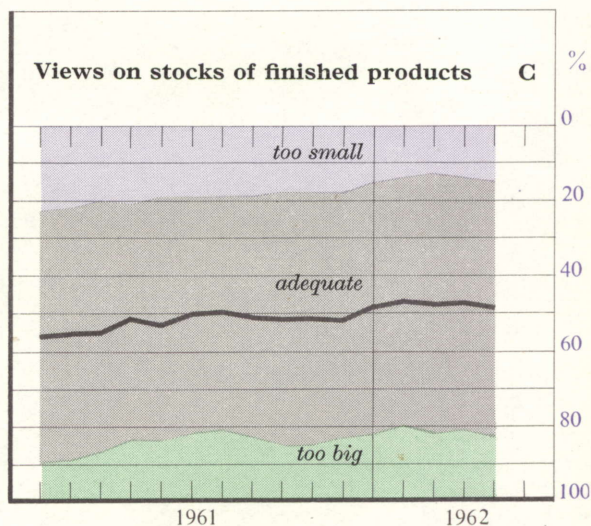
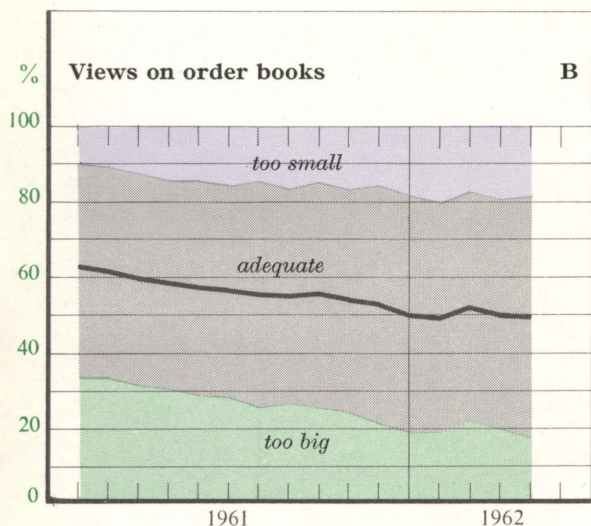
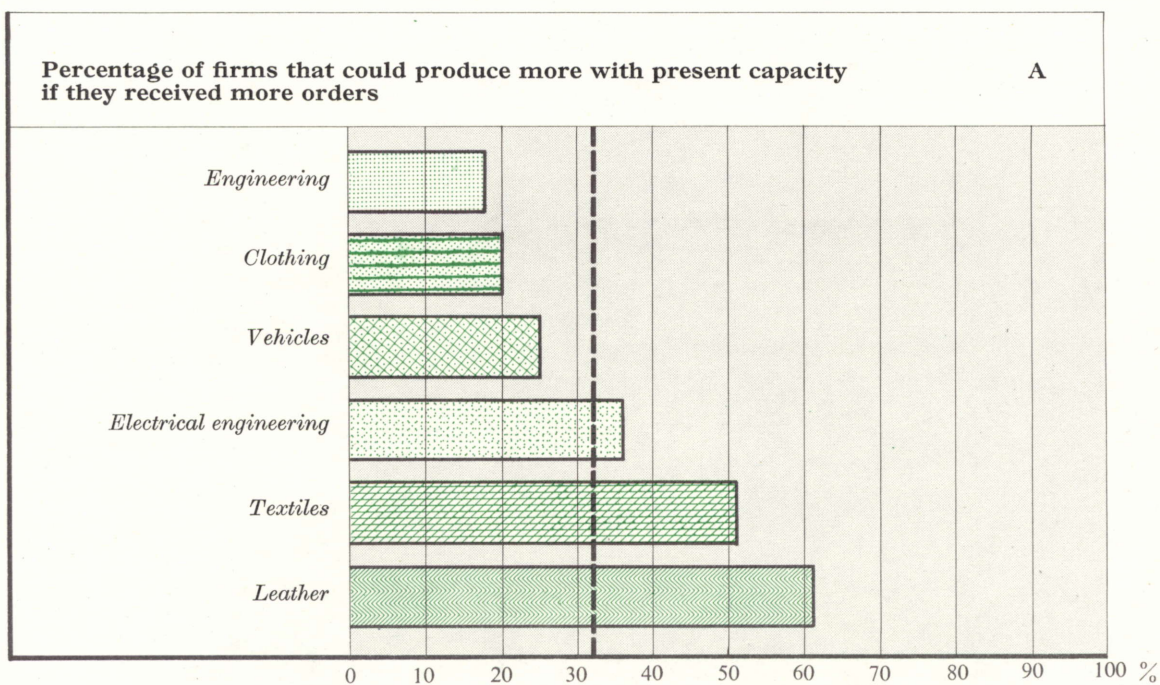
There was no further slackening in the expansion of internal expenditure. The increase in *investment* activity, in particular, appears to have been only very little less than in the fourth quarter. Investment in equipment again rose very vigorously to judge by the way sales shaped in the typical investment goods industries and by imports of capital goods. Building investment, on the other hand, where demand is substantially in excess of real supply, suffered appreciably from the bad weather in February and March; it seems, however, to have gathered momentum again in the following months.

In the first months of 1962 investment in *stocks* was still markedly influenced by the cautious policy of industry. Nevertheless in a few sectors, especially steel, there seems to have been less keenness on the part of manufacturers and dealers to run down their stocks. Steadily growing consumer expenditure induced those dealing in consumer goods trade to replenish stocks.

Private expenditure on consumption did in fact continue to expand vigorously. True, retail sales in the first quarter were up by only 7.2 % in value and 3.1 % by volume on the corresponding level of the previous year—as against 10.0 % and 6.5 % in the fourth quarter of 1961—but the drop in sales is almost wholly attributable to the relatively low turnover in March, when sales were affected by the late date of Easter and the bad weather. Retail sales in April were 18.6 % in value and 13.7 % by volume above those of April 1961.

The main factor in the expansion of consumer expenditure was that the disposable incomes of private households continued to increase steeply, while the rate of saving remained more or less unchanged. Although the resistance of businessmen to wage claims has been hardening, wages under collective agreements again rose appreciably the year-to-year rate of almost 9 % recorded in the first quarter, being even higher than the 8 % in the last quarter of 1961. By contrast to the earlier trend, however, the gap between the increase in actual earnings and the increase in minimum wages under collective agreements does not appear to have widened. Moreover, the total amount of wages and salaries went up again because of an increase in employment. Since transfer income also rose appreciably, mass incomes may well have been substantially—about 10 %—above the level for the corresponding period of the previous year; the rate of growth was thus more or less the same as in the fourth quarter.

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, iron and metal production.

GRAPH A : Answers to this question (put during the survey at the end of April 1962) were given for six branches of industry. The percentage for industry as a whole is indicated by the dotted vertical line.

GRAPHS B and C : The three colours (green, grey and violet) indicate the percentages of the three different answers in the total number of answers.

The black curves, the scale for which is between the graphs, indicate the figures obtained by adding the percentages together if the latter are weighted as follows :

- by 0.03 for the answers "too big";
- by 0.02 for the answers "adequate";
- by 0.01 for the answers "too small".



The tightness on the *labour market* has not eased appreciably in recent months despite the increased numbers in paid employment—2.2 % more at the end of March 1962 than a year previously. Greater use of foreign manpower contributed considerably to this expansion; at the end of March 566 000 foreign workers were employed in the Federal Republic, i.e. 157 000 more than at the end of March 1961. The number of unemployed was again unusually low at the end of May (about 98 000, i.e. 0.5 % of all persons in paid employment), especially in view of the fact that six times that number of vacancies was registered.

Although the increase in the numbers employed in industry was substantially less than in the economy as a whole, *industrial production* tended to keep on moving slightly upwards. In the first quarter the index of production ⁽¹⁾ was only 1.7 % above the corresponding period of the previous year, but this was solely due to the fact that building and allied sectors were hard hit by the unusually bad weather. For March in particular, therefore, the index does not clearly bring out the underlying economic trends. The way the index of industrial production developed in April—the growth rate was again 3.9 %—clearly confirms that the slight expansion of industrial output noted since the end of the second quarter of 1961 is continuing.

Imports of goods and services rose steeply in the first quarter. According to customs figures the year-to-year growth rate of goods imported went up from 3.5 % (7.1 % by volume) in the fourth quarter of 1961 to 16.5 % (21.5 % by volume) in the first quarter of 1962. This was in any case largely due to the fact that goods stored in bonded warehouses have now been included in the import figures, but even without this special factor the growth rate in value was 12.5 %. The April figures, however, were only about 3 % above those for the corresponding period of a year earlier. The poor harvests last year led to a particularly steep rise in imports of foodstuffs, but imports of finished industrial goods also continued to rise considerably. Expenditure on services made further progress, largely because more payments were made to foreigners on capital yields and more foreign exchange was being spent on tourism.

Despite the vigorous growth of imports, *prices* continued to move upwards. This is partly attributable—as for example in the building sector—to the continuance of a heavy excess demand. But the steady rise in wage costs per unit of output, combined with a tendency for profits to fall, led businessmen to raise prices where the market situation, and not least foreign competition, still seemed to allow them to do this. For investment goods producer prices in April were 5 % higher than a year earlier, and for consumer goods the rise amounted to 2.7 %. Finally, as a result of poor crops in the 1961/62 farming year agricultural prices again went up. The cost-of-living index in April was 4.6 % higher than in April 1961.

As imports tended to expand more than exports there was a reduction in the surplus on *current transactions*. If unrequited payments are included in the first quarter of 1962,

(1) Index of output per working day — “Statistisches Bundesamt”.

there was even a deficit on current account—the first since 1950—of DM 190 million as against surpluses of DM 80 million in the last and almost DM 1 900 million in the first quarter of 1961. The surplus on *trade* alone fell from DM 1 300 million in the fourth quarter of 1961 to DM 600 million in the first quarter of this year. This was, it is true, partly due to the decision that goods held in bond (about DM 400 million) would be included in the import statistics. The overall balance of payments, however, showed a surplus; the total *gold and foreign exchange reserves* of the banking system (Deutsche Bundesbank and other banks) went up by about DM 1 300 million in the first quarter. Here a fall of about DM 2 000 million in the Central Bank's reserves of foreign exchange was offset by an improvement in the foreign exchange position of the banks to the tune of about DM 3 400 million. There was in fact evidence of a net inflow of capital, both long-term (about DM 400 million) and short-term (improvement in the terms of payment including errors and omissions to the tune of some DM 700 million) and the balance of trade, on a cash basis, was DM 400 million more favourable than would appear from the customs returns, for the sole reason that no payment abroad was involved when the goods held in bond were added to the import figures.

If the internal *liquidity* of the banks dropped in the first quarter despite the balance-of-payments surplus, this was due not so much to heavy money exports but rather to the cash transactions of the central authorities which normally result in considerable funds being withdrawn from circulation at this season; this year the amount withdrawn was around DM 2 750 million. The banks therefore had recourse on a larger scale to Central Bank credit and returned more "mobilization paper" ⁽¹⁾. Advances to industry went ahead at a slower rate than in the previous quarter, following a seasonal trend, and were also less than in the first quarter of 1961. This, however, is partly explained by the fact that at that time firms were subscribing to the development loan, and they obtained part of the money by borrowing.

2. Outlook

The outlook for economic development in the coming months is on the whole rather favourable, despite a number of factors causing uncertainty. The prospect of a continuance of the slight economic growth is more or less borne out by business surveys including the recent EEC inquiry into economic trends.

Since the second quarter of 1961 the *flow of orders abroad* was regularly lower than for the corresponding period a year earlier—the difference in the first quarter of 1962 being 2.5 %; since the fourth quarter of 1961 however the trend has been unmistakably upward. Many factors suggest that this trend will continue in the immediate future,

⁽¹⁾ "Mobilization paper" = Federal Treasury bills and non-interest-bearing Treasury bonds resulting from the exchange from the corresponding partial amount of the Deutsche Bundesbank's equalization claim on the Federal Government.

especially the shorter delivery dates in important export industries, the tariff cuts likely to be made in the middle of the year on trade between the EEC countries and in the United States, and the increase in German payments for development aid which are largely tied to specific projects. On the other hand, a continuation of the steep upward trend in wages appreciably in excess of the simultaneous advance in productivity could cause a further deterioration in Germany's competitive position, and in the end the expansion of exports would again be considerably hampered. As for exports of services in the next few months, particularly services in connection with tourism, the available information, such as bookings with travel agencies abroad, indicates that these will probably be brisker than last year.

The expansion of *gross investment in fixed assets* will continue, although perhaps once more at a somewhat slower rate. Investment in equipment by enterprises may well increase still further in the coming months, mainly because of deliveries of orders already placed quite some time ago. At the same time the trend in new orders for investment goods does not suggest any upturn in the propensity to invest. If in the long run domestic demand is to provide the guarantee that optimum use is made of production capacity, it seems essential that the propensity to invest should increase. In fact domestic orders received by the mechanical engineering industry in the first quarter were 2 % below sales in the same period and almost 10 % below orders received in the first three months of 1961. Against this, the number of building permits issued for commercial and industrial buildings, in terms of space enclosed, was again 2 % above the very high figure recorded for the first three months of 1961; in the last quarter of 1961 there had been a 5 % drop on the figure recorded a year earlier.

By and large, the present pattern of supply and demand holds out no hope of any early easing of the severe strain on the building market, particularly if the very large backlog in building is also taken into account. In housing the present trend of demand is even upward. During the first quarter the volume of newly authorized building in this sector was 6 % (in terms of space enclosed) higher than a year earlier, whereas for the last quarter of 1961 the corresponding figure was only 1 %. The only class of permits to show a reduction was for the erection of public buildings; here the figure was 14.5 % less than in the first quarter of 1961 when, however, a very high figure had been recorded.

In order to ease the strain on the building market it has been decided in settling the Federal budget to block 20 % of the funds allocated to building and construction, although the Minister of Finance is authorized to make exceptions to this rule. But this measure cannot be expected to give any appreciable relief to the building market unless the other public bodies follow the Federal Government's lead. Parliament has also passed a law "restricting building activity"; this forbids certain types of building, but the volume affected is relatively small.

The growth of mass incomes will continue in the second half of the year. But the rate of growth is likely to decline, particularly if there is further hardening of the resistance

offered by employers to large wage rises. The increase in *private consumption* might slow down correspondingly. *Public consumption*, on the other hand, may well again rise steeply.

On the supply side, there is likely to be a continuation of the considerable differences in trend between the various branches of industry; in some sectors, for instance, the growth of *output* will continue to be hampered by severe labour shortages, while in others it will be limited by demand. On the whole, however, there is likely to be a slight expansion, especially if it is no longer slowed down so much by the influence of the stock cycle.

Imports will go up once more; but it appears doubtful whether, despite the tariff cuts in trade with EEC countries expected in the middle of the year, imports of goods will keep up until the end of the year the rate of expansion maintained so far. There will however be further vigorous growth in expenditure on foreign services, especially on tourism.

There is much to be said for keeping up a vigorous rate of expansion in imports, particularly as this can temper the *rise in prices*. If there is no effective policy to curb the trend in prices—which as things are cannot (except in the building sector) be done by restricting demand but must be achieved mainly by obtaining larger and cheaper supplies from abroad—it will be difficult to induce employers and workers to follow a wages policy which will not entail further increases in costs. Serious thought should be therefore given to the possibility that the Federal Republic might take action under Article 15(2) of the Treaty and make reductions in its rates of duty not only where these help to maintain target prices, but quite generally on its trade with other member countries in the Community, especially as these reductions will have to be made anyhow within a few years.

B. France

Economic expansion continued in the early months of this year with external demand providing on the whole a somewhat greater stimulus than previously. Home demand remained very lively, investment again increased, and private consumption was favoured by the continuing rise in incomes.

Supply increased still further. The seasonally-adjusted index of industrial production was up about 2 % on the fourth quarter and by about 7 % on the first quarter of 1961. Despite a slight decline at the beginning of the year, the volume of imports was about 8 % higher than in the first three months of 1961.

Prices continued to rise and the cost of living went up 1.1 % between December 1961 and April 1962.

The balance of payments again closed with considerable surpluses. Despite further repayment of external debts, gold and foreign currency reserves increased by \$ 380 million in the first four months of the year.

The outlook for further growth of production and employment remains favourable and a business survey suggests that sales prospects on world markets are good. Investment in general should again rise, and on the income side all the conditions are present for a strong and lasting expansion of private consumption.

The authorities responsible for economic policy will still, however, have to keep a wary eye on the trend of prices.

Keener competition, brought about if necessary by a further anticipatory cut in customs duties (the balance-of-payments situation seems to call for such action in any case), could contribute to more stable costs and prices. Finance for the high investments needed to carry out the Fourth Plan should be found primarily by further encouraging the formation of long-term savings and channelling them to capital markets.

It would seem inadvisable from the standpoint of economic policy to attempt to improve the self-financing possibilities of firms by increasing prices, the more so as this might finally lead to a steeper upward trend in wage costs.

The development of the economy so far and the outlook for the rest of the year do not call for any material change in the estimates for 1962 published early this year in Quarterly Survey 1/1962.

1. Recent developments

At the beginning of 1962 the development of *exports* of goods and services, which for a time had been hesitant in the fourth quarter of 1961, again made a definite contribution to economic expansion. According to external trade statistics, total exports in the first quarter were up 6.3 % in value and about 4 % by volume on the corresponding period of the previous year. In April the rate of growth by value rose to 7 %. The value of deliveries to the franc area in the first four months was, however, 13 % lower than in the corresponding period of the previous year, mainly as a result of a further sharp shrinkage of outlets in Algeria. On the other hand, exports outside the franc area showed a growth rate of 14.4 %. In the early months of this year the receipts from services also would seem to have been higher.

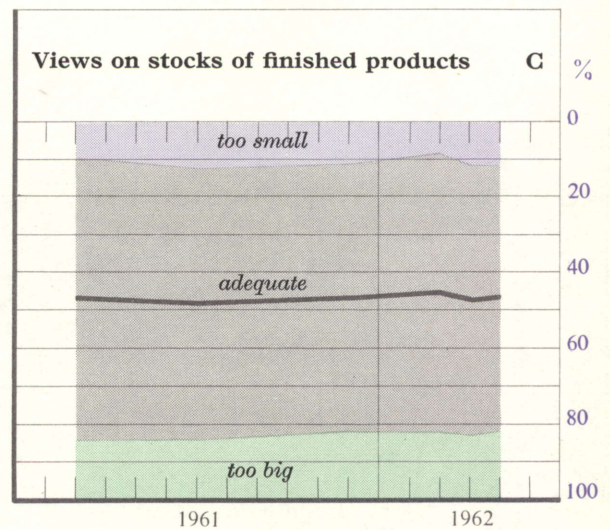
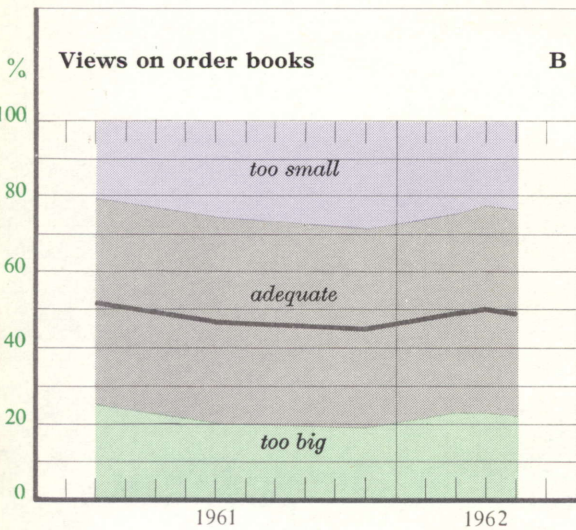
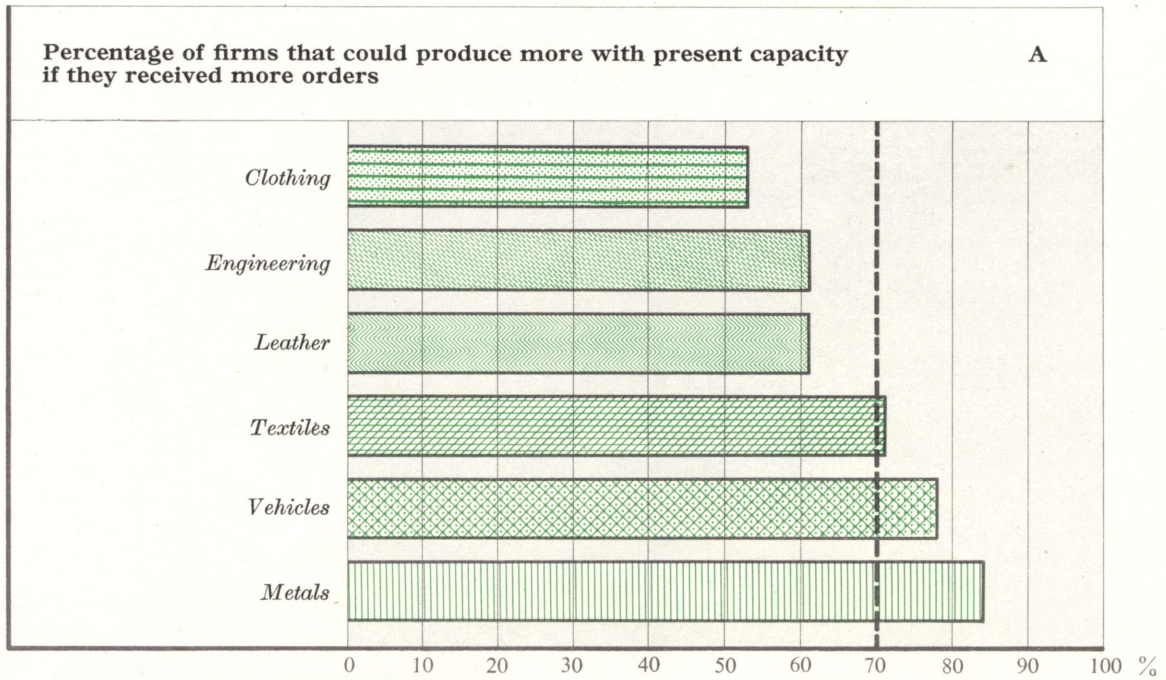
Internal demand continued to rise. The development of *fixed investment* was again the most important factor in expansion. Though private industry did not increase its outlay on buildings and equipment quite as much as a year earlier, the beginnings of a definite increase were to be noted in fixed investment of public undertakings. The direct investments of the State, mainly building and public works, have also increased further, if seasonal factors are left out of account, although the unusually cold weather in the first months of the year may have had a retarding effect at times. The same is true for housing, where the number of dwellings completed was in fact lower than a year earlier. *Investments in stocks* again probably made a somewhat larger contribution to economic growth in the early months of 1962.

The continuing expansion of income of households as a consequence of rising employment, further wage increases and improved social benefits, was reflected in higher expenditure on *private consumption*, although demand for textiles and other traditional consumer goods seems to have been curbed at times by the abnormal weather. Demand for consumer durables, in particular motor cars, was on the other hand very lively. The rise in public consumption may have been somewhat more pronounced than hitherto, not least because of the considerable increases in wages and salaries in the public services and higher disbursements for persons returning from North Africa.

There was no notable strain between demand and supply in the first months of 1962, except in agricultural markets. Because of the weather, *agricultural output* was in fact so delayed that consumers could not be supplied at the prices previously obtaining, despite a greater release of stocks and issue of import licences.

Industrial production on the contrary was again able to meet rising demand with relative elasticity. The slight slowdown in the growth rate revealed by the seasonally-adjusted INSEE-index—from 3.2 % in the first quarter of 1962 to 2.1 % in the first quarter of 1962 (in each case compared with the previous quarter)—was probably wholly attributable to the fact that the motor car industry had reached the planned rate of output of new models. In general, however, the earlier trends persisted into the first months of

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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the year : continued expansion of production in the capital goods industries; further recovery in consumer durables and chemicals; hesitant trends in textiles, clothing and leather. However, there was a reversal of the trend in coal-mining, where after the upward trend observed in the fourth quarter of 1961, output declined, and in steel where, on the contrary, production went up somewhat in recent months. Industrial production as a whole in the first quarter of 1962 was up 6.9 % on the corresponding level of the previous year.

Advances in productivity probably played a decisive part in the expansion of production. However, in industry the number of hours worked, seasonally corrected, rose, owing in particular to the recruitment of extra labour. *Labour shortages* seem to have grown no worse in the first months of 1962, but the possibility may not be entirely ruled out that the unusually cold weather or other random factors have temporarily distorted the statistical picture.

Disregarding seasonal factors, *imports* of goods and services may well have fallen somewhat during the first months of 1962 after the strong rise towards the end of 1961. Customs statistics nevertheless show that—even if allowance is made for the exaggerated January figures due solely to a change in accounting technique—imports of goods in the first quarter were still up 8 % in volume and 7.6 % by value on the corresponding level of the previous year. In April, on the other hand, the trend seems to have again been upward. There was probably somewhat less recourse to external services in the first quarter than in the last quarter of 1961, at least to the extent that these services are linked with the import of goods.

The rising *price* trend continued. According to information supplied by businessmen industrial producer prices continued to climb. Retail prices for manufactured consumer goods rose—sometimes at a clearly faster pace—in the first four months of the year. In the services sector not only did rents rise considerably, as is usual at the beginning of the half-year, but the prices of other services also rose. Contrary to the normal seasonal movement, food prices went up this year, chiefly because of inadequate supply as a result of weather conditions. The index of consumer prices as a whole thus rose 1.1 % between December and April, when it was 5.1 % above the corresponding level of the previous year. Building costs, too, have shown a distinct upward trend for some time now. In the first quarter of 1962 they were 3.5 % higher than in the corresponding quarter of 1961.

If seasonal factors are left out of account, the deterioration of the *trade balance* did not continue in the early months of this year. True, the traditional surplus in trade with the franc area has almost disappeared following the sharp decline in exports to Algeria. But in trade with countries outside the franc area the surplus again showed a definite rise. The *balance of payments* again closed with considerable surpluses. Official gold and foreign exchange reserves increased in the first four months of the year by nearly \$ 380 million, and thus totalled about \$ 3 300 million. Advance repayments of foreign debt totalled \$ 120 million, a sum comparable to the exceptional inflow in foreign exchange which was

mainly due to a purchase of francs by the Federal Reserve Bank worth \$ 50 million. The net currency position of the banks probably did not change to any important extent.

However, the inflow of funds from abroad did not contribute to the liquidity of the *money and capital markets* quite as much as a year earlier. As the cash transactions of the Treasury probably also showed a surplus, and since demand for credit from industry remained quite lively and, in particular, large loans were floated by public undertakings, signs of strain were apparent at times. At the end of February the monetary authorities raised the banks' special minimum reserve ratio (*coefficient de trésorerie*) from 30 to 32 %. At the same time the statutory minimum holding of Treasury bills was lowered and the interest on them reduced. Liquidities were thus channelled away from short-term to medium-term credit business.

2. Outlook

So far this year the economy has developed as forecast at the beginning of 1962 for the year as a whole. Available advance indicators do not point to any significant divergence of general economic activity from the estimated growth trend in the months ahead. Businessmen are thus fairly optimistic about future sales on world markets and even count on a slight speed-up in exports. In the EEC trend check at the end of March, the capital goods industry in particular reported relatively heavy backlogs of external orders. Exports of industrial products will also be favoured by the anticipatory reduction in customs duties between the EEC countries decided on for 1 July. After a normal harvest the export of agricultural produce should also advance somewhat more sharply, the more so as the first measures for the creation of the common agricultural market might simultaneously provide an added stimulus. However, it cannot be excluded that these expected export successes outside the franc area may be to some extent offset by a further shrinking of sales opportunities in the franc area.

Internal demand should continue to afford a relatively strong stimulus for production and employment. There are signs that private industry is regarding its initial 1962 investment programmes, which looked to an increase in *real fixed investment* of 7 % over 1961, as over-cautious. In the coming months medium-sized concerns in particular will be carrying out certain projects which originally were merely tentative. Nevertheless, the weight of increased investment during the second half of the year may be more clearly in the public undertaking sector for which much bigger programmes have been approved in 1962 than in 1961. Investments by public administrations will also continue to advance strongly. On the other hand, there are still no signs of any particularly expansive development in housing.

The growth of *private consumer expenditure* should continue at the pace expected. From the income side the conditions for such growth are present—the more so as note-

worthy increases (old-age pensions, minimum wages, salaries of certain grades in the civil service) and certain tax reliefs have been decided on or planned for the lower income groups, whose propensity to consume is relatively high.

In view of the continuing expansion of demand, a further rise in *industrial production* is to be expected. However, this may be a little slower than in the six winter months of 1961 to 1962, when the pace of growth was greatly influenced by the rapid recovery of motor car production. Shortages of equipment and, in particular of labour continue to be serious bottlenecks, even though the shortening of military service and repatriation from Algeria promise to ease the situation before the end of the year.

The outlook for *agricultural production* is at present somewhat depressed by the unusually cold spring weather. Nevertheless, a much larger area than in the previous year has been put under grain. Stockraising should further increase.

If harvests are normal the need to import agricultural produce should decline. Nevertheless, the trend of *overall imports* should remain upward, since a further increase of imports of manufactured goods is to be expected.

It would greatly help price stabilization if these imports were facilitated, if necessary by special measures. Not only would this directly increase supplies on home markets, but on the demand side also the conditions for curbing the rise of prices would in the long run be improved in so far as the rise is caused by the large liquidity of business and the banking system, which is still being fed by the very high surpluses of foreign currency.

It cannot be denied, however, that with rising wage costs a further limitation of the freedom of enterprises to increase prices would erode their profit margins and impair their self-financing capacity at a time when the implementation of the Fourth Plan demands a continuing high growth of investment. For this reason even greater efforts should be brought to bear to prevent further cost increases. Along with the fair sharing of improved prosperity this is an important task for a national income policy which the Government is now considering. Finally, it would be very welcome if the policy of facilitating finance from outside for business concerns, already initiated by certain measures on liquidity and interest, were consistently pursued. Tax reliefs for long-term saving by private households would perhaps be worth considering in this connection.

C. Italy

Economic growth was maintained in the early months of 1962, although at a more moderate pace than in the fourth quarter of 1961, when expansion had been exceptionally rapid. Demand from abroad and, to an even greater degree, investment and private consumption continued to grow. The seasonally adjusted index of industrial production went up by 1.3 % in the first three months, a very sharp rise. Supply was boosted by imports, but the trade deficit for the first quarter was a little lower, at \$ 321 million, than it had been a year previously. Since exports of services grew once again, the seasonal deficit on the overall current account was lower than the corresponding figure for 1961. As is normal at this time of the year gold and foreign exchange reserves declined ; they were, in fact, \$ 140 million down.

The upward trend in prices, which had become distinctly more rapid since the autumn of 1961, persisted in the first quarter ; this was due mainly to higher prices for food and services. In March the cost of living was no less than 4.9 % up on the figure for 1961. Wages, however, again increased appreciably. In February, and more especially in May, cost-of-living allowances were raised through the operation of the sliding scale.

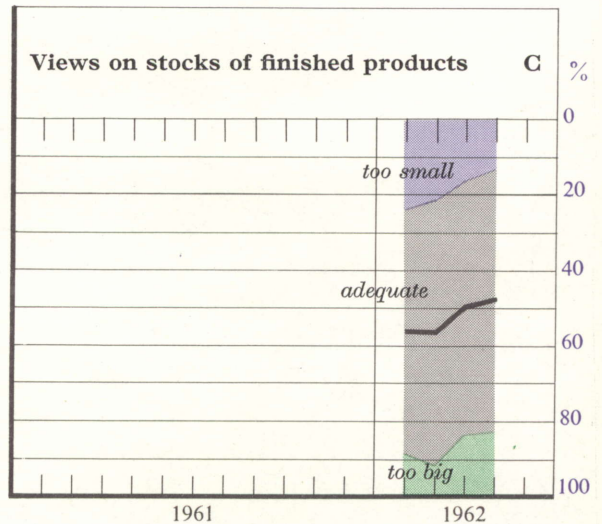
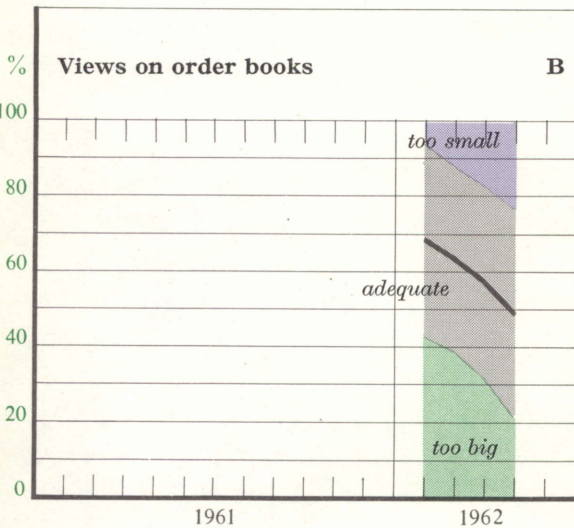
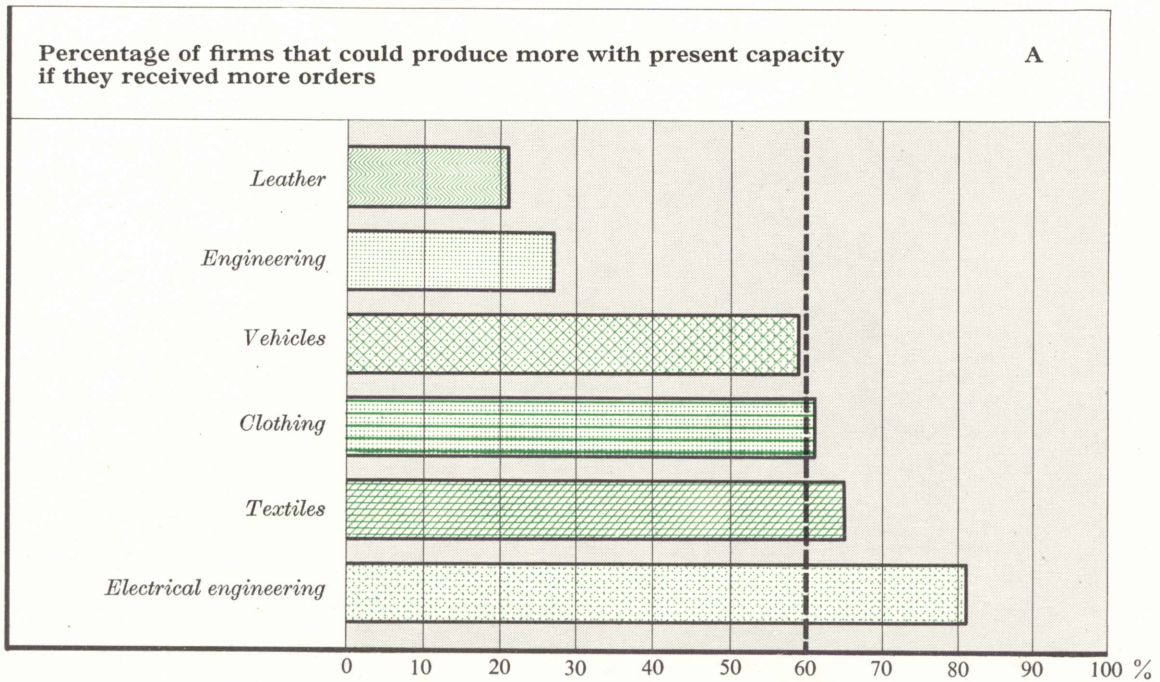
The remaining months of 1962 hold out every promise of continued expansion. It is true that the growth of exports might once again lose a little of its vigour ; growth ought, however, to remain substantial and greater than in the other member countries. Equipment investment in particular will grow, as will construction investment, especially if more public schemes for structural improvement are now put in hand. Private consumption will go ahead vigorously, encouraged by the current wave of wage increases, which is likely to continue, and by a substantial improvement in pensions.

Production is elastic enough to keep pace with demand. Developments in the first months of the year and the present outlook do not warrant any change in the estimates for the full year published in the last quarterly survey.

1. Recent developments

Demand from abroad for goods and services grew once more in the first three months of 1962, though rather less vigorously than in the fourth quarter of 1961. The growth rate for goods exported (external trade figures in terms of value) fell from 22.6 % in the last quarter of 1961 to 16 % in the first quarter of 1962, export prices remaining practically unchanged. However, it must be remembered that the expansion at the end of last year was extraordinarily rapid and substantially more vigorous than in the rest of the year.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



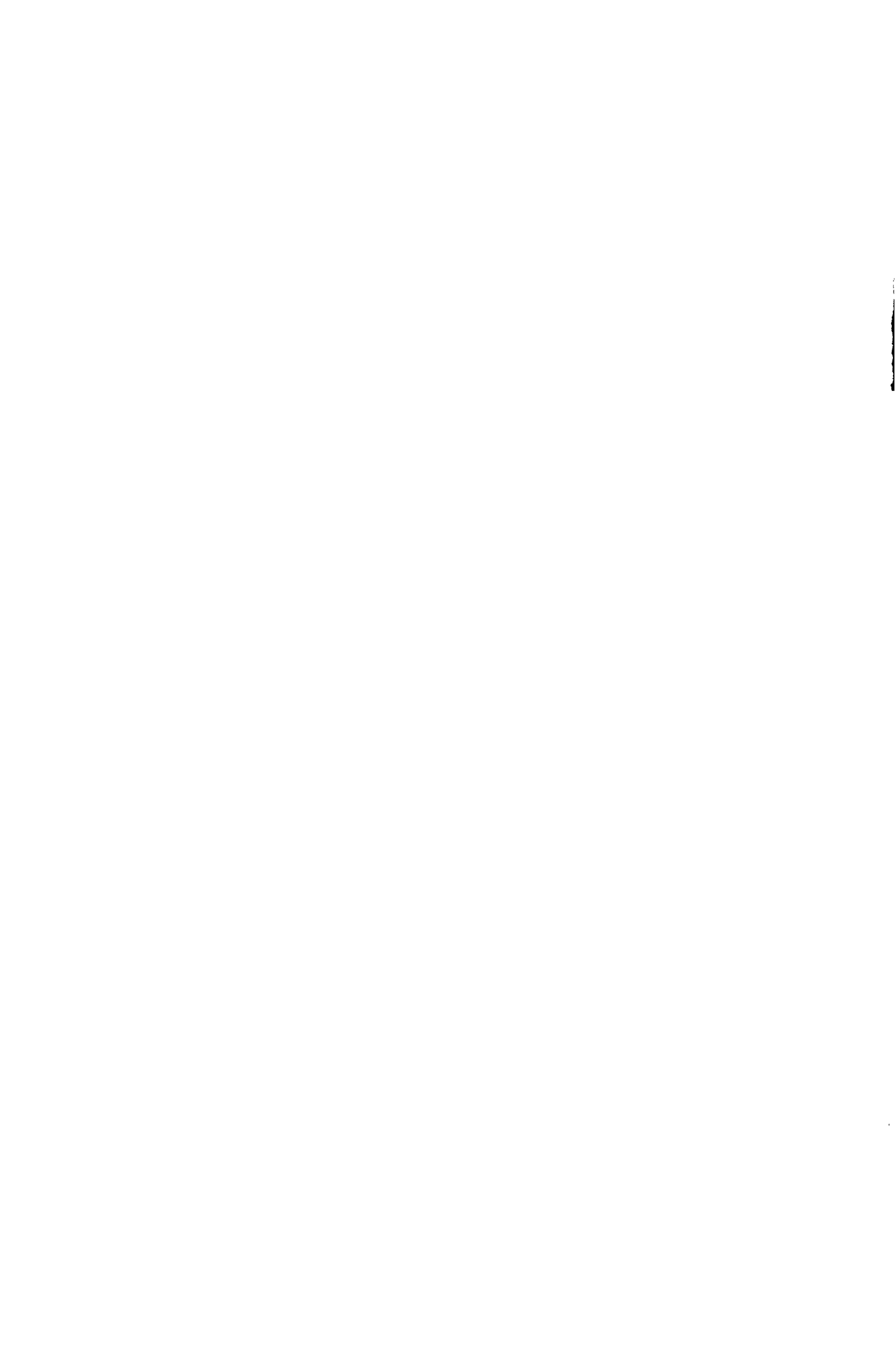
Answers to the questions of the EEC business survey carried out in Italy by ISCO-Mondo Economico.

GRAPH A : Answers to this question (put during the survey at the end of April 1962) were given for six branches of industry. The percentage for industry as a whole is indicated by the dotted vertical line.

GRAPHS B and C : The three colours (green, grey and violet) indicate the percentages of the three different answers in the total number of answers.

The black curves, the scale for which is between the graphs, indicate the figures obtained by adding the percentages together if the latter are weighted as follows :

- by 0.03 for the answers "too big";
- by 0.02 for the answers "adequate";
- by 0.01 for the answers "too small".



The rapid growth tempo of exports of consumer goods, notably of foodstuffs, continued in the first quarter, but the upward trend in sales of capital goods showed signs of flagging. The decline was largest in the growth rate for exports to the developing countries : for sales to other non-member and to member countries it was very slight. Exchange receipts from invisibles were also up, mainly as a result of heavy transfers from Italians employed abroad; in the first three months of 1962 they showed a 16 % improvement on the corresponding figure for 1961.

Fixed asset investment, particularly as regards equipment, continued in an upward direction. It is true that the year-to-year growth rate for the production of capital goods fell a little in the first two months of 1962, but this decline was solely due to a slight fall-off in demand from abroad. Imports of capital goods grew very vigorously. At the same time home sales of important equipment goods were growing faster.

Such information as is now available suggests that, apart from seasonal factors, *construction investment* grew once more. The number of units completed in January and February, both for business and for domestic purposes, did not however, reach the very high level of the same months of 1961. By contrast, the year-to-year growth rate of domestic sales of building materials, which presumably are synchronised with building activities, rose appreciably between the fourth quarter of 1961 and the first quarter of 1962 (from 11.5 % to 13.5 %). Public works must also have made considerable progress.

After slack conditions for about a year, there seems to have been a slight recovery in *stock building*.

Private consumption doubtless afforded a further and vigorous incentive to business activity. Given the substantial increase in employment and in income per employed worker, mass income must have increased considerably. In agriculture and industry, between December and March, agreed wages alone were raised by 4 %; if family allowances are included, corresponding incomes were no less than 17.8 % and 7.6 % respectively above the level of March 1961. In accordance with sliding-scale wage agreements cost-of-living allowances rose in February and more especially in May. Sales of the more costly consumer goods, particularly durables, continued to increase; in the first quarter the number of new motor cars registered and domestic sales of luxury goods in terms of value were 25 % up on the figures for the first three months of 1961. As far as can be judged at present, *agricultural work* in general proceeded normally. However, the harvests of various fruits and vegetables were affected by rather poor weather conditions, from which not even Italy escaped.

After the unusually rapid increase in the last quarter of 1961, the growth of *industrial production* in the succeeding three months was distinctly slower. However, the level reached a year earlier was exceeded by 11.9 %, compared with a year-to-year increase of 12.3 % for the fourth quarter of 1961. In the first quarter of 1962 the ISCO seasonally adjusted index rose by 1.3 %; in the previous quarter the growth had been

7.6 %. The greatest progress in production was made in synthetic fibres, transport equipment and petroleum products.

The *employment level* rose appreciably. According to the most recent ISTAT survey, the number of workers employed was 5 % higher in January and 2 % higher in April than in the same months of 1961; in July and November the corresponding increases had been 2.6 % and 4 %. The concurrent decline in unemployment was also particularly marked being over 15.5 % in the first quarter of 1962 as compared with the same period of 1961 (Italian Ministry of Labour figures). The shortage of manpower, particularly of skilled tradesmen, persisted, though it did not lead to any noteworthy strain on the labour market.

Imports of goods and services rose sharply. The ISCO indices show that the year-to-year increase of goods imported—in terms of volume—rose from 4.7 % to the last quarter of 1961 to 9.4 % for January and February 1962. Imports had been spurred on by the 10 % tariff cut and to a lesser extent by the complete liberalization of imports of industrial products in trade with member countries. In terms of value, the year-to-year growth rate rose from 9.8 % in the fourth quarter of 1961 to 10.7 % in the first quarter of 1962.

The lively growth of internal demand led, in particular, to an increase in imports of consumer durables and capital goods. It would seem that the increase in imports of raw materials, which was also vigorous, was connected with the recovery in stock-building. This has meant that purchases both from the Community countries and from the developing countries outside Europe made substantial progress. Unlike the 1961 figures, however, those for 1962 for imports from the United States only just reached the level of a year previously. Imports of services have also been increasing somewhat more rapidly, to judge by expenditure of foreign exchange under this heading which was 38 % higher in the first quarter than a year before : the growth rate in the fourth quarter of 1961 had been 23 %.

Although home production was elastic enough to meet the rising demand, and despite heavy increases in imports, the *rising price* trend, which had become steeper since the autumn of 1961, continued in the first months of 1962. Solely as a result of a substantial increase in the prices of consumer goods, mainly foodstuffs, wholesale prices rose by 1.4 % between December 1961 and March 1962; this brought them to 2.7 % above the September figure, around which they had been virtually stable for about 18 months. Because of this and because of large increases in the prices of certain services, prices to the consumer also rose sharply; the cost-of-living index in March showed a 4.9 % increase over the figure for March 1961. In Rome the increase was nearly 7 %.

Since the growth of exports was faster than that of imports, the deficit on *trade* for the first quarter was—at \$ 321 million—smaller than that for the first quarter of 1961 (\$ 336 million). The net surplus on services had continued to increase at the same time,

and the seasonal fall in official gold and foreign exchange reserves was rather less than a year before (\$ 140 as against \$ 144 million), although the balance of capital transactions, unlike for the first quarter of 1961, showed a deficit.

The balance of payments, however, deteriorated in comparison with the last quarter of 1961. This was not only due to the seasonal setback in the balance of current payments; it was also connected with certain capital outflows.

Despite this trend in the balance of payments and despite further government cash surpluses in the first four months of 1962, *bank liquidity*, so far from declining further, actually increased—apparently as a result of a fall in the total of notes and coin in circulation. Although credit was once again expanding at a lively pace, the ratio of the volume of credit to the volume of deposits, which had been increasing for 2 1/2 years, fell from 71.7 % in December 1961 to 71.4 % in March 1962. In addition, the cut in the minimum reserve ratio at the end of January tended to improve the banks, liquidity situation. Until April the net yield on government paper declined a little, whereas in 1961 it had been rising slightly for a fairly long period.

2. Outlook

Exports of goods and services will doubtless continue to grow. As regards goods, it is true that the most recent enquiries made by ISCO-Mondo Economico among managements (as part of the Community's monthly trend checks) tend to show that their books are not particularly well filled with orders from abroad. But the arguments put forward in the last quarterly survey that foreign demand will continue to grow fairly fast are still valid and are strengthened by the fact that in certain member countries the business recovery would seem to be more rapid than was to be expected at the time. Everything suggests that exports of services, particularly revenue from tourism, will once again surge upwards.

The outlook for *fixed asset investment* is perhaps even more favourable. According to the ISCO-Mondo Economico survey mentioned above, order books for the capital goods industry were at the end of April well filled with orders for the home market, and the outlook for the growth of production of capital goods in the coming months was indicated as being very good. Even on the purely hypothetical assumption that investment in the other sectors were to stagnate, the formation of fixed assets will increase in total value by at least 5.5 % if the investment programmes of government-controlled concerns are carried out. But to judge from plans for new housing and industrial and commercial building, investment in these fields will certainly continue to rise substantially. In this connection, official schemes for improving structures, which are to be put in hand in the second half of the year, will obviously be of special importance.

As had already been the case for the current financial year, a substantial increase in government expenditure on government employees has been provided for in the financial year beginning on 1 July. There may thus be a further rise of 10 % in public consumption.

The powerful expansion of *private consumption* will no doubt continue. It is true that an increase in taxation, bringing in about 50 000 million lire and affecting mainly industrial profits and yield on capital, has recently been introduced. However, the sums involved are not large and the nature of the incomes involved is such that these measures are unlikely to have any marked effect on consumption expenditure. The same applies to the 15 % tax at source on dividends provided for in a bill recently tabled in parliament. On the other hand, substantial increases in incomes, benefiting sections of the population in which the propensity to consume is strong, are to be expected, as a result of further movements of manpower from the land to other sectors, new collective bargaining agreements forthcoming stages in the new system of wage areas, more progress in introducing equal pay for women and, lastly, an increase in pensions.

In view of the progress made in the first quarter and the confident forecasts of managements as far as June/July, it is a reasonable assumption that *industrial production* will continue to expand. Even if production from now to the end of the year were to grow no faster than in the first three months, this would mean a growth rate of 10 % for the full year, as was forecast in the last quarterly survey. In these circumstances, *unemployment* should again decline appreciably.

The vigorous upsurge in demand, notable in home demand, will engender a further sharp increase in *imports*, particularly if the revival in stock-building should be maintained. Past events support the view that purchases abroad will again be boosted by the coming supplementary tariff cuts to be introduced on 1 July 1962 for trade between the member countries.

Neither business trends at the beginning of the year, which were a little slacker though still rising, nor the further general outlook warrant any change in the *forecasts* made in the last quarterly survey for the main headings of economic activity over the full year.

The *deficit on trade* is likely, if anything, to widen a little once more. The *balance of payments* should still show substantial surpluses, since net receipts from services will probably grow and the increase in the surplus on the balance of capital transactions will continue, though at a slower rate.

Government appropriations for the financial year 1962/63 will mean a larger *budget* deficit, rising from 380 to 400 000 million lire. The net balance of commitments carried over from previous years is also larger. In view of the many public schemes for structural improvement, which have now been ready for some time, the Governments cash situation might well show a deficit in the second half of 1962.

Trends in the balance of payments and in government finance should therefore tend to increase *liquidity*, particularly in the banking system, in coming months. However, since demand for credit will expand even faster as a result of the increasing difficulty industry has now had for some time in meeting capital requirements from its own resources, the monetary authorities will no doubt have to take care that investment is nevertheless not hampered by difficult credit conditions, particularly since other factors may in their turn lead to higher interest rates on the capital market.

The Government has felt concern at the distinct steepening in the upward price trend which has been observed for some time, and it is studying ways and means of bringing more goods on to the market at lower prices. For example, a measure enabling farmers to retail their produce direct is under consideration. For certain goods which have become much dearer—olive oil and oil-seeds, for example, — more liberal import arrangements are contemplated. Broadly speaking, Italy would seem to be another country which would stand to gain by giving greater encouragement to imports notably through anticipatory tariff cuts; not only price trends, but also the balance-of-payments situation, provide an incentive.

It is certain that a more liberal policy with respect to licences to set up supermarkets would help considerably to stabilize prices. Moreover, given the growing shortage of labour, it would perhaps be useful to ease official regulations on overtime so as to increase the elasticity of supply.

D. Netherlands

General economic activity continued to expand slightly in the early months of 1962.

The recovery in exports, of which the first signs appeared last autumn, seems to be more assured than it was. At the same time domestic demand remained brisk. Investment expenditure on equipment still contributed more to expansion than any other demand factor. When allowance is made for the influence exerted by the weather on building activity, the level of expenditure in the building sector remained very high. The growth of private consumption, on the other hand, seems to have been slower for a time, doubtless owing to postponements in the renewal and implementation of the collective wage agreements.

The trend in industrial production was again clearly upward, since most of the cuts in the working week have now been completed and investment will again be able to improve output per head. Imports were once more on a very large scale. The price level rose slightly during the early months of the year; from March onwards this upward trend sharpened as a result of certain increases in food prices caused by the bad weather.

A slight deficit was recorded on the balance of current transactions. However, when a repayment by the United Kingdom through the International Monetary Fund is taken into account, the overall balance of payments showed a small surplus.

The likelihood of a further expansion in overall demand is the main feature of the outlook for future development. The recovery in export may well continue. Investment will keep on rising. If growth in this sector should slacken during the year, this is bound to be offset by a vigorous expansion in private consumption, since substantial wage rises are to be expected shortly and a cut in income tax rates is planned to take place in July.

Industrial production may well show a further rise—especially as the numbers in employment are also likely to increase.

The outlook for consumer demand and protection costs is causing the authorities to curb activity in the investment sector—where certain factors such as reduced possibilities for self-financing are in any case acting as a brake on expansion—by restricting the growth of credit and recently by making it in addition more expensive. These measures are designed to weaken the forces causing domestic prices to go up. If long-term threats to economic expansion—and ultimately to competitiveness—are to be avoided, the policy pursued in connection with current economic developments will have to be very flexible, so that any boosting of productive investment which may prove necessary shall be given in good time.

1. Recent developments

The slight tendency towards a recovery in *foreign demand* (in terms of effective exports of goods and services), which began in September 1961, seems to be becoming more pronounced—despite setbacks—in the figures for the early months of 1962. This was due not only to the trend in orders received but even more to the fact that the industries concerned were in a better position to deliver—partly because of the somewhat more modest advance made by internal demand. While the value of goods exported in the fourth quarter of 1961 (according to foreign trade statistics) was less than in the corresponding period of 1960, in the first quarter of 1962 these exports were 0.5 % in value and 3 % by volume higher than in the corresponding period of 1961. For April-May the average rate of increase in terms of value was 6.5 %. If allowance is made for seasonal influences, exports of goods—in terms of national accounting—were up in the first quarter of 1962 by about 5.5 % in value and a good 3 % by volume on the last quarter of 1961.

Exports of crop products and machinery went up considerably. At the same time the tendency for sales of livestock products to fall became appreciably weaker. Exports of some other products, particularly metals and some textiles, continued however to reflect the weakness of demand which was already evident last year.

The recent increase in exports stemmed from an upturn in deliveries to other Community countries, particularly Western Germany and Italy. Exports to non-member countries, on the other hand, again tended to fall off, although the downward movement of sales to the United States now seems to have been halted.

Home demand continued to rise, even though its rate of growth was somewhat less than had been expected. Here investment demand was again the most dynamic factor. *Fixed investment by enterprises*, for instance, especially expenditure on equipment goods, again showed a definite increase. Up till now, therefore, the trend in investment does not seem to have been suffering seriously from the narrowing of profit margins that has been observed for some time past, especially since the labour shortage continued to act as a stimulus.

Demand in the *building sector* continued to be exceptionally heavy, but the figures for the first quarter were rather adversely affected by the bad weather. The measures taken to restrain unsubsidized housing and commercial and industrial building caused an appreciable drop in the number of permits issued but the number of permits already issued is still amply sufficient to ensure that building capacity is used to the full. The number of dwellings started, on the other hand, again rose steeply in March. *Public investment* tended to keep on rising and the fact that it was a little below the 1961 level in the first quarter was due entirely to the weather.

Investment in stocks may have again advanced somewhat faster in connection with the recovery of production.

The upturn demand in the *private consumption* sector gave every sign of continuing in January—a trend which was already apparent in the last months of 1961. After January consumer expenditure remained more or less at the level already reached without showing any noteworthy growth. This was due not so much to the bad weather conditions as to the delay in renewing the collective wage agreements caused by difficulties in applying the principles embodied in the policy on wages. Apart from some increases in the public sector there was little change in wage rates, in the early months of the year. For the first quarter as a whole private consumption showed a year-to-year growth rate of 4.5 % in value and 2 % by volume. *Public consumption* also expanded. The increase in the salaries of civil servants, in anticipation of which higher salaries have been paid from the beginning of the year, is now finally assured.

The effects of the vigorous investment activity noted in the last few years and of the adjustment to the shorter working week in industry are showing themselves in the greater elasticity of internal supply. Consequently *industrial production* (according to the seasonally adjusted index of the Central Statistical Office of the Netherlands) was in the first quarter of 1962 2.7 % up on the last quarter of 1961 and showed a year-to-year growth rate of 1.5 %. This confirms the trend towards renewed expansion which followed the fall in production which occurred in the period from the middle of 1961 to October. True, demand was still weak for the products of some industrial sectors—particularly crude steel and various textile goods. But the situation in most other industrial sectors is marked by the fact that production capacity is being used to the fullest extent that the manpower available will permit.

On the *labour market* the situation continued to be definitely strained. Despite the rather long hard winter, which led to a slowing down of building activity, seasonal unemployment was very limited. The average monthly unemployment figures were 20 % less in the first quarter than in the corresponding period of 1961.

The gap between the growth of demand and that of output again led to a rise in *imports*, although the increase was slower than in the corresponding period of 1961. Customs returns show that goods imported in the first quarter were 3.5 % in value and 5 % by volume above the figures for the corresponding period of the previous year. For April-May the average rate of increase in terms of value was 7.5 %. If the seasonal movement is discounted, imports of goods—in terms of national accounting—were up by about 7 % in both value and volume on the fourth quarter of 1961. Imports were largely of finished goods, especially investment goods.

The value of imports, unlike that of exports, rose not only in trade with member countries but also in trade with non-member countries—by 5 % for the former and 1.7 %

for the latter. Imports from the United States picked up again after a distinct drop in 1961 and were roughly 20 % higher in the first quarter of 1962 than in the first three months of 1961.

The cost-of-living index in the first quarter was 3 % higher than last year's figure for the same period. Two thirds of this rise can be ascribed to higher prices—owing to special factors—for potatoes and other vegetables. Had it not been possible to meet part of the excess demand from imports, the internal price level would undoubtedly have risen more steeply. When it is remembered that the price index of imports of consumer goods, which have been expanding vigorously, went up by almost 4 % despite revaluation, the Government's price policy appears on the whole to have been quite successful.

Since imports grew more than exports—both in relation to the corresponding period of 1961—the deficit on trade was also larger. According to customs returns it amounted in the first quarter of 1962 to nearly 1 000 million guilders, i.e. 150 million more than a year earlier. As in addition the net position on services was less favourable (mainly owing to the fact that incomes from investment abroad were temporarily depressed for purely fortuitous reasons). The *current account* (on a cash basis) closed with a slight deficit of 60 million guilders, as against a surplus of 350 million in the corresponding period of the previous year.

To this must be added net official exports of capital amounting to about 70 million guilders. When the repayments, totalling 130 million guilders, by the United Kingdom through the International Monetary Fund are taken into account, a slight surplus (about 30 million guilders) was recorded on the *overall balance of payments* for the first quarter. The *official gold and foreign exchange reserves* at the end of March exceeded those at the end of the year by about 44 million. The net foreign exchange position of the banks deteriorated somewhat. The rise in the official reserves continued in April, when they went up by 64 million guilders.

The slight deficit that developed on current account and the restrictive policy of the monetary authorities placed some strain on the *money and capital markets*. Not only did the State float a loan of 300 million in March to mop up liquidity, but the Central Bank too adopted various measures to tighten up its restrictive policy. The minimum reserve ratio, for instance, which had been 6 % since October, was raised to 8 % in January and was only temporarily brought down again to 6 % in March in connection with the floating of the loan. Similarly, when the banks exceeded the ceiling for the expansion of credit fixed under the agreement with the Central Bank—they were allowed to expand credit in the months of January to April by 0.5 % a month—they were forced to pay in special deposits as a disciplinary measure.

Money market rates were therefore substantially higher than in the fourth quarter of 1961 despite open market operations by the Central Bank which eased the market

situation. Finally, the Central Bank on 25 April raised the Bank rate as well (from 3.5 % to 4 %). Moreover, in line with their restrictive policy, the monetary authorities allowed foreign loans to be placed on the Dutch capital market; evidently in consideration of the way in which the balance of payments was developing, a limit of 150 million guilders up till September was placed on these loans.

2. Outlook

Economic expansion in the Netherlands may gather some momentum in the coming months.

Exports may well continue to expand. Business surveys suggest that orders from abroad for industrial goods, particularly consumer goods, have gone up in recent months. The increase in production should be sufficient to make the growth of exports possible even though the increase may be inhibited by the pull of internal demand. It may however become more difficult for certain products to maintain their competitive position on foreign markets. Moreover, it is not clear whether the growth of agricultural exports will continue to benefit from the factors which have been favouring it since last autumn.

Exports to other EEC countries are most likely to gather strength, especially after the tariff reductions to be made in the middle of the year. The tendency for the growth of exports to the Belgo-Luxembourg Economic Union to slacken does, however, provide a factor working in the opposite direction.

Effective expenditure on *fixed investment* will probably also continue to increase but it may well advance only slowly. The labour shortage and rising wage costs, it is true, will again put pressure on businessmen to increase the relative share of capital among the factors of production in their concerns in order to maintain their competitive position on foreign markets. In addition, the lowering of income tax could have certain effects on the investment of small enterprises. On the other hand, it is not impossible that as the year goes on the general propensity of firms to invest will be more severely curbed by the restrictive measures imposed in 1960 on rates of depreciation and the deductibility of investment from tax assessment, by the quantitative limitations placed on the expansion of bank credit since the middle of 1961 and by the recent increase in the cost of credit, especially since profit margins, and hence the possibilities of self-financing, have also diminished appreciably.

In the *building sector* demand may well continue to be very high for a long while, so that it looks as though extreme vigilance will still be called for in this sector.

The entry into force of new collective agreements and the retroactive payment of the agreed wage and salary increases may well lead to an appreciable rise in consumer incomes in the coming months and this trend has in fact emerged since May. It already looks as though it will be difficult to limit wage increases to an average of 6 % per wage-earner, as the authorities propose. By the middle of the year wage rates for women must be brought up to at least 85 % of equivalent rates for men. The expected rise in employment during the second half of the year, the higher transfers in the form of social security benefits and particularly the cut in wage tax and income tax from July may well contribute to a sharp rise in *private consumer expenditure*.

Thanks to the growth of the working population from the middle of the year on and as a result of the high investment in recent years *industrial output* is likely to be more elastic, especially since cuts in the working week are still to be expected in a few cases only. But even if there were no further expansion, higher growth rates would be attained for 1962 as a whole—if only because of the fall in output before the middle of last year—than for 1961.

Imports, especially of finished goods, should continue to increase under the stimulus of growing economic activity and particularly of rising consumer demand; but it remains to be seen whether they expand so much faster than exports that the net increase seriously affects the balance of trade.

In view of the excess demand still to be found in at least certain sectors, and the fact that costs, particularly labour costs per unit of output, may well rise further, it seems that it will be difficult in the coming months to maintain the relative *price stability* which was a feature of the first quarter. On the other hand further measures are being considered which should counter the trend towards rising prices. An example of these is the bill introduced in Parliament to reduce the scope of the luxury tax. The raising of controlled rents, which was originally fixed for 1 July, will in all probability be postponed for some months.

The high level of imports and the tightening up of the restrictive policy designed to curb investment demand, might help to ease the strain somewhat in the course of the year. It can already be expected that the tightness experienced on the *money and capital markets* will continue and that interest rates on the capital market will come further into line with those in the other Community countries.

The main problems facing the Dutch authorities in dealing with the growth of domestic demand are the choice of a balanced policy and, in particular, the search for ways in which they can curb the rise in costs. The difficulties that had been expected at the beginning of the year have, it is true, not yet emerged, but they are likely to become of some importance soon when wages rise on a greater scale. The Dutch authorities have, however, deliberately chosen a policy centred on an improved distribution of the fruits of

economic progress. They have preferred, even at a time when substantial wage increases are being granted, to reduce direct taxation—most of the reduction will go into an increase in the disposable incomes of households—and to increase social security benefits. True, the Netherlands are perhaps somewhat behind other Community countries in these fields. For the future, however, the instruments available to the authorities will have to be used very flexibly so that the economic situation can, if necessary, be influenced immediately. Stricter application of the basic principles of official budget policy can effectively help to overcome any difficulties that may emerge in the coming months.

E. B.L.E.U.

Belgium

During the first months of the year the expansion of economic activity in Belgium was very weak. It is true that there were still noteworthy year-to-year growth rates, but these were in part a result of the setback in January 1961. Apart from random and seasonal variations, economic activity has made no significant progress since the fourth quarter of 1961.

However, the general export trend was by no means unfavourable; if special factors are eliminated it showed an increase of about 6 % on the corresponding figure for the previous year, and the trend was slightly upward. By contrast, fixed capital asset formation tended to mark time at the high level reached at the end of 1961, although one element in this item—public investment—is booming. The same is true of private consumption; here, partly because of the bad weather, increases in incomes have not yet led to a corresponding growth in purchases.

For this reason, industrial production has also tended to stagnate at the level already reached. Imports developed rather hesitantly. Mainly because of the higher cost of some foods, the level of prices rose slightly.

The balance of current payments showed a surplus in the first quarter and there was a heavy surplus on the overall balance. Official gold and foreign exchange reserves remained virtually unchanged, but the bank's net foreign exchange holdings improved substantially.

The outlook till the end of the year suggests that the upward trend in economic activity will be resumed, but the pace is likely to be very modest. Exports should increase again, although perhaps somewhat more slowly. The chances that private consumption will grow would seem to be better for the second half of the year. Investment trends once again hold out little promise of an early resumption of expansion. Production, however, might well rise slightly.

Despite the slackening in the rate of growth, the current pattern of demand and the situation on the labour market do not at present make it seem advisable to follow a more expansive economic policy. By contrast, the structural measures already in hand should be intensified and speeded up in order to complete the improvements which alone in the long run can again make a higher rate of growth possible.

1. Recent developments

The expansion of overall demand seems to have continued in the first quarter, though at what was probably a very much slower pace. *Exports* in particular rose again. Customs returns show that exports of goods were about 18 % greater in value than a year earlier. It should however be remembered that the figures for the first quarter of last year were seriously affected by the strike in January. If the effects of this special factor are eliminated, the year-to-year rate of growth would have totalled about 6 % for the first quarter of 1962. In April the figure was about 5 %.

This improvement in exports is the more remarkable in view of the fact that sales of steel products have evidently been hardly any better than in the second half of 1961. This contrasted however with very satisfactory export trends in many other branches, particularly in mechanical engineering and in parts of the textile industry.

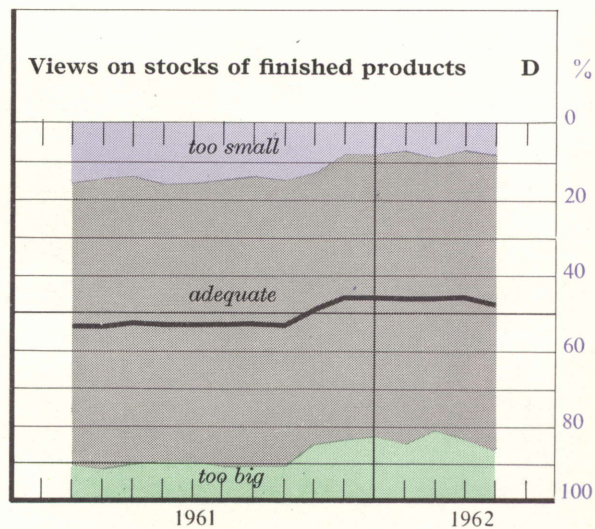
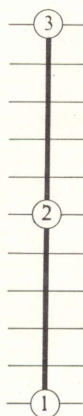
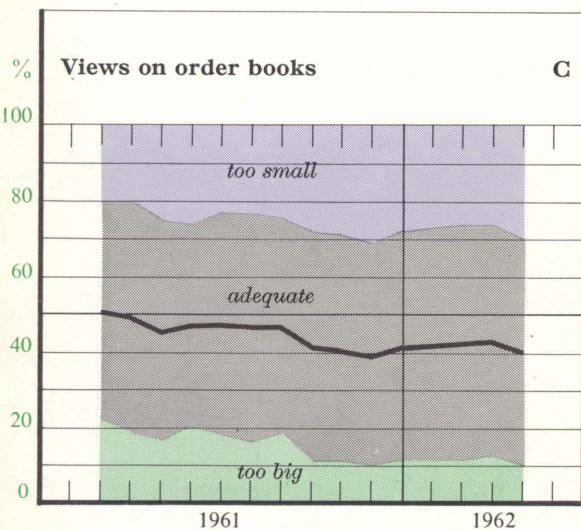
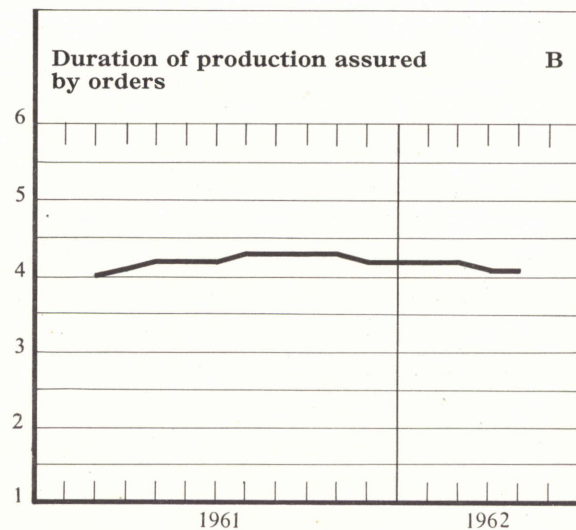
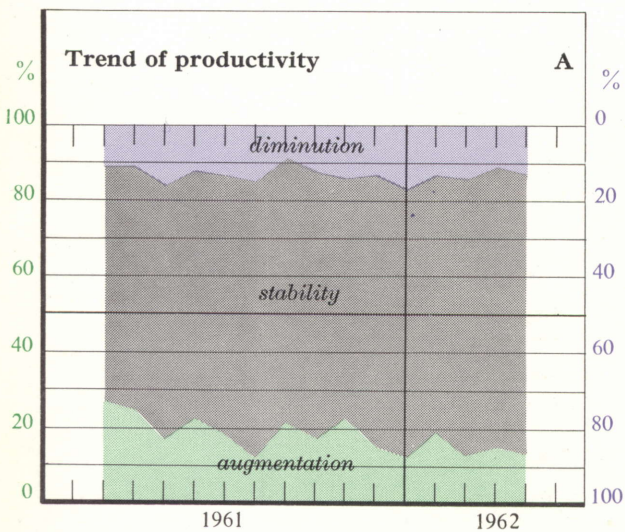
Apart from the special factors already mentioned, the breakdown of Belgian exports by country of destination shows that sales to Community countries grew more strongly—mainly because of a distinct recovery in imports by France and the Federal Republic of Germany—than did sales outside the Community. Moreover, improved export figures outside the Community are mainly accounted for by a rise in deliveries to the United States.

Outlay on *fixed investment* was still satisfactory; it made a decisive contribution to the maintenance of domestic demand, although the growth of fixed investment by enterprises began to flag visibly. None the less, it was still appreciably higher than it had been just a year previously, as is shown by various indicators, such as deliveries from the capital goods industries to domestic purchasers, imports of machinery and of appliances, the number of public, commercial and industrial buildings completed, and the answers given by managements to questions in business surveys. The figures for new housing, however, were in the early months of the year a little below those for the same period of 1961. This may be due in part to exceptionally unfavourable weather conditions, but is probably also not unconnected with other factors, notably a certain shortage of labour in this sector.

The overall expansion of fixed capital asset formation was greatly boosted by public investment, where the year-to-year increase for the first quarter of 1962 was 18 %. The greater part of this increase was invested in infrastructure, mostly in connection with transport.

Private expenditure on consumption does not seem to have made any very appreciable progress. The bad weather evidently led, it is true, to increased expenditure on heating, but it also inhibited the expansion of sales in certain lines, particularly spring clothing. At all events, the index of sales by the main departments stores in the period from February to April 1962 showed no improvement on the corresponding 1961 figure. The number of new motor vehicles registered was even substantially below the same figure for 1961.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Source : Business survey of the National Bank.

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

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

GRAPH B : The curve indicates the average of businessmen's answers, expressed in monthly production figures.

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

- by 0.03 for the answer "too big";
- by 0.02 for the answer "adequate";
- by 0.01 for the answers "too small".



These trends are all the more remarkable in view of the fact that disposable household incomes definitely increased : not only did employment continue to expand, although only very slightly, but there were a whole series of pay rises. Dividends distributed and withdrawals from profits by enterprises may have flagged a little as a result of a certain pressure on profit margins, caused particularly towards the end of the year by the weakness of export prices. Lastly, and this is perhaps also connected with the bad weather, the ratio of savings to disposable income also seems to have increased distinctly; in particular the amounts deposited with the relevant savings institutions rose considerably.

With the various elements in demand developing in this way *industrial production*, on a seasonally adjusted basis, remained stable at the level reached midway through 1961. True, the IRESP index showed a year-to-year growth of 9.8 % for the first quarter of 1962; this increase is, however, evidently a reflection of the heavy drop in output caused by the strikes in January 1961. For the months of February and March alone, the index showed a slight actual decline (of 0.5 %) over the same period for 1961, but the figures used are provisional and will probably have to be adjusted. Finally, the unusually bad weather hampered production in several sectors.

Whatever the causes, a tendency for output to ease has become clear in certain branches, particularly in many sectors of industry engaged in initial processing (various branches of metal working and of chemicals), as well as in several industries producing consumer goods (textiles, foodstuffs, furniture). With more pits being closed and labour in short supply, the output of coal has declined appreciably. In mechanical engineering on the other hand, the heavy demand for capital goods caused production to rise further.

The *labour market* in early 1962 was marked by a continuing shortage of workers with particular skills in various branches of industry and in building. The reabsorption of unemployed workers continued. At the end of April the number unemployed was 98 000 ⁽¹⁾ compared with 120 000 at the end of April 1961.

Imports, too, showed little further growth in the first quarter : their year-to-year growth rate in terms of value had been 8 % in the fourth quarter of 1961, but was down to 2.5 % in the first quarter of 1962. This trend reflects the decline in purchases of certain non-durable consumer goods (foodstuffs and textiles), of some durables (motor vehicles), as well as of some raw materials (minerals). On the other hand, imports of capital goods registered remarkable rates of growth; it was largely because of this factor that Belgium's imports from other Community countries were 5.7 % up on the figure for the first quarter of 1961, whereas imports from non-member countries fell 0.5 % short of the corresponding 1961 figures.

The *level of prices* inched up a little. Poor harvests and the long cold winter had the same effects in neighbouring countries, largely owing to the increased cost of certain

⁽¹⁾ Including 27 000 workers not fit for normal employment.

foods. In the first quarter the index of retail prices was about 1 % and in April and May about 2 % higher than in the corresponding periods of 1961.

The *trade balance* continued to develop favourably : in the first quarter of 1962 the deficit was only about Bfrs. 300 million whereas it had been Bfrs. 7 500 million in the same period of 1961 (when, however, it was affected by the strike). Net receipts from invisibles would also seem to have increased, so that there should have been a substantial surplus on current account. The Treasury continued its policy of reducing the floating foreign indebtedness, but heavy net official exports of capital did not prevent the overall balance of payments from showing a big surplus. At \$ 1 657 million the *gold and foreign exchange reserves* held by the Central Bank showed little change on the previous quarter, but by the end of May they fell back to \$ 1 632 million. On the other hand, the net foreign exchange holdings of the commercial banks improved appreciably during the same period.

Developments in the foreign exchange field helped to keep conditions on the *money and capital market* easy. Treasury operations would seem once more to have produced an increase of liquidity, despite the temporary mopping up of available funds which occurred when the Government floated a loan of Bfrs. 7 500 million in March. The Treasury's indebtedness to the Central Bank, which had been Bfrs. 5 600 million at the beginning of January, reached Bfrs. 8 500 million at the beginning of May. The overall increase in the public debt in the January to April period was Bfrs. 10 300 million, whereas in the corresponding period of the previous year it had been Bfrs. 14 100 million.

Private demand for short-term credit was very heavy from the beginning of the year onwards and the rates of interest charged on advances moved downward. In March Bank rate was once again cut—this time from 4.25 % to 4 %.

2. Outlook

Although it may be assumed that the slack conditions prevailing in the early months of 1962 will probably not continue, the outlook for the rest of the year does not, by and large, hold out any promise of particularly vigorous development.

In the months ahead *exports* of goods and services should again increase. The backlog of orders from abroad is heavy, particularly in the mechanical engineering industry. The outlook in the other Community countries also suggests that exports of goods will also continue to expand. Moreover, Belgian sales to these countries will also be stimulated by the cut in customs duties to be made in the middle of the year. The continued recovery in the United States makes it reasonable to reckon on increased Belgian exports to that country, too, provided better business conditions are not offset by the protectionist measures the American authorities have seen fit to impose on flat glass and carpets. In general it is being found that the stability of labour costs per unit of

output enjoyed by Belgian industry in recent years is still benefiting Belgian exports. However, the trend in this field seems to have been changing of late. Moreover, it might well be that the goods offered for export are not yet quite sufficiently adapted to the requirements of Belgium's potential export markets—as the unfavourable trend of sales to other non-member countries seems to suggest. The growth in exports of goods generally might for this reason slow down a little. At all events, the outlook at present does not warrant any revision of the forecasts made at the beginning of the year.

As far as *fixed investment* is concerned, there does not seem on the whole to be any good reason for expecting any further speed-up in expansion, despite the sustained growth of public investment; however the high level reached in the corresponding period of 1961 will certainly once more be exceeded.

The propensity of enterprises to invest seems, then, to be somewhat less than previously. It is true that the severity of international competition, the shortage of skilled manpower and more recently the resumption in the upward trend of wage costs should sustain or even strengthen the tendency of managements to spend money on rationalization. On the other hand, the outlook for expansion in the countries where Belgian exports have their principal markets does not seem as favourable as in recent years. The fall in export prices has reduced the scope for ploughing back profits in a number of major industrial sectors; moreover, the long-term capital markets are not yet flexible enough, and conditions on these markets not favourable enough, to allow of a corresponding increase in investment financed by borrowing. The trend in licenses granted for industrial and commercial buildings and in orders for machinery and appliances placed with the metalworking industry by domestic buyers indicates that managements are inclined to be cautious.

In the housing sector, too, a slowdown in growth rates is to be expected; the number of licences to build will in all probability rise more slowly than in 1961 mainly because of cuts in the appropriations for publicly assisted housing.

On the other hand, progress in general government investment is to be expected—mainly in connection with an expansion of public works programmes; in the first quarter, commitments for expenditure under this heading were more than 17 % up on the same period of 1961.

In addition, *private consumption* should make distinct progress as the year progresses. In the first place, there will be further and more general wage increases. Secondly, the rise in the retail price index in April and May set in motion the sliding wage scale, and the effect of this will very probably be that in important sectors of economic activity wages will rise 2.5 %. Moreover, wages and salaries in the public service will be raised in the middle of the year. Employment, too, may well expand again slightly. In addition, the improvement in old-age pensions and family allowances will help to step up the disposable income of households. Lastly it may be assumed that bad weather will

cease to be a factor acting as a brake on certain types of expenditure. The propensity to save, which tends to rise when substantial increases in pay are granted after a fairly long period of relative stability, is more likely to fall back a little.

Broadly speaking, then, demand may again increase a little and this should lead to a corresponding increase in *output*.

Although domestic supply is in general relatively elastic, further expansion in *imports*—albeit on a moderate scale—is to result from the hardening of overall demand. Firstly, the favourable outlook for the balance of payments, which is due in no small part to the continued investment of foreign capital in Belgium and, secondly, to the likelihood of a reduction in the budget deficit, make it very probable that liquidity on the money markets will once again be abundant.

Certain important financial requirements are therefore fulfilled and this means that the Government will in large measure be able to adapt its economic and growth policy to the situation created by the present outlook.

Again, the array of economic policy instruments available to the Belgian Government, which had already been improved by the reform of the money market has been further enlarged. An interministerial committee for the co-ordination of investment has been set up in order to establish a scale of priorities in connection with public investment. In addition, a “Société Nationale d’Investissement” has been established to encourage private investment and channel it to where it is most needed.

The importance of the action taken by these bodies is not limited to the maintenance of a satisfactory rate of long-term economic growth. In the present phase of business activity—characterized by a tendency for differences in levels of activity to widen and for the strain in various sectors to continue, the action of these bodies may also serve as a guarantee that specific measures will be taken where they are needed to offset or limit the tendency towards a decline which is becoming evident in various important branches of industry. The stricter criteria already being applied for the granting of investment aid under the 1959 law on economic expansion constitute in this respect a factor which is not without its importance.

It is obvious that it will be some time before these measures—which are aimed primarily at further adjustment of the economic structure but which by their impact improve the chances of more rapid long-term growth—can have their full effect. That is, why they should be put in hand as quickly as possible.

Grand Duchy of Luxembourg

The slowdown in economic activity recorded in the second half of 1961 showed a tendency to level out into stabler conditions as from beginning of 1962. The international steel situation, which still has a decisive influence on exports from Luxembourg and therefore on the country's economy as a whole, has become firmer, although there has not been marked recovery which would in turn have made a substantial improvement of prices possible. Domestic demand has continued to expand slowly. The fall in industrial production which had set in during autumn was halted in February.

The prospects for the expansion of overall demand in the coming months do not indicate that there will be any change in present trends. Public investment will probably again be the main driving force in what is, after all, a rather modest industrial expansion. It would accordingly seem very appropriate to go ahead with the efforts being made on the structural plane to make the country less dependent on developments in the world market for iron and steel products.

1. Recent developments

Whilst in the closing months of 1961 the position of the steel sector had weakened further, there were signs after the turn of the year that this trend was coming to a halt. From January to April *deliveries* of iron and steel products abroad settled down at a level only slightly below that of the corresponding period in the previous year; this was due largely to the slight revival of demand for sheet and plate in the other EEC countries.

In February and March orders received for iron and steel products exceeded deliveries for the first time since May 1961. As a result, the backlog of orders rose a little, though it was still considerably lower than a year earlier.

There has been a further rise in home demand because of the expansion of *gross fixed investments*, especially in the building sector. The considerable extension of investment from public funds has had a favourable influence on building and it also seems that investment by firms has increased, although somewhat less. In addition several new industrial establishments have been set up since budgetary measures were taken to encourage private investment.

Because of the slower growth rate of household incomes, as a result of lower dividends and smaller bonuses in the iron and steel industries, *private expenditure on consumption* has risen only slightly. A further increase in the number of persons employed in industry,

and the new wage-rates for workers in the building industry, are among the factors supporting income. Building wages were raised by 6 % on 1 March. The law of 20 April 1962 has introduced new conditions for employees in the private sector, including longer annual holidays.

According to the somewhat meagre data available so far, expenditure on private consumption seems still to be marked by the rapid rise in outlay on services; on the other hand, purchases of various consumer durables appear to have fallen off a little as compared with the figures for the first quarter of 1961.

Although *industrial production* has tended to level off since the turn of the year, the national index for the first quarter was, for the first time in three years, below the level of a year earlier. The difference amounted to 4.8 %, contrasting with the slight rise that had still been attained in the fourth quarter of 1961. Output in the iron and steel industry was down 6 %, and mining and chemicals also registered a drop. In several other branches of industry, however, progress continued and was coupled with a considerable rise in employment. In those sectors not connected with the production of iron and steel employment was about 8 % higher than in the first quarter of 1961, and this increase was made possible almost entirely by recruiting more foreign labour.

In the first quarter building activity was some 9 % higher than a year earlier. Despite the continuing shortage of labour and unfavourable weather conditions this growth rate was only slightly short of the 1961 average.

In contrast to what has happened in the other Member States, the index of *retail prices* in Luxembourg has remained practically unchanged since the beginning of the year; despite this, it was in May about 1 % higher than in May 1961 while this very modest change in the index is partly due to the fact that it is bound on a too narrow range of items, it is also to some extent the result of official price policy, which has prevented an increase in the price of various important items. In February, price increases for some textile products were again made subject to control.

2. Outlook

The outlook in the steel market for the coming months justifies the expectation that *Luxembourg exports* will maintain their present level—at least so far as volume is concerned. They may even increase slightly. On the other hand, demand for products outside the iron and steel industries will contribute relatively little to this development. By and large there appears to be little chance of export prices improving.

Investment in the iron and steel industries for purposes of rationalization and the extension of productive capacity will continue to bring about an increase in overall gross

fixed investment. Generally speaking, the outline law on economic expansion which was passed in May could well provide greater incentives for firms to invest. Public investment will rise further because considerably higher appropriations for this purpose are envisaged for 1962.

Higher incomes of private households, which result from the wage increases agreed in certain branches of industry and from the rise once again noted in the number of employed, will probably bring about a slight increase in *private consumption*. No increase of wage-rates which might lead to a more rapid growth of household expenditure, is to be expected before the end of the year in the two most important sectors, the iron and steel industry and the civil service.

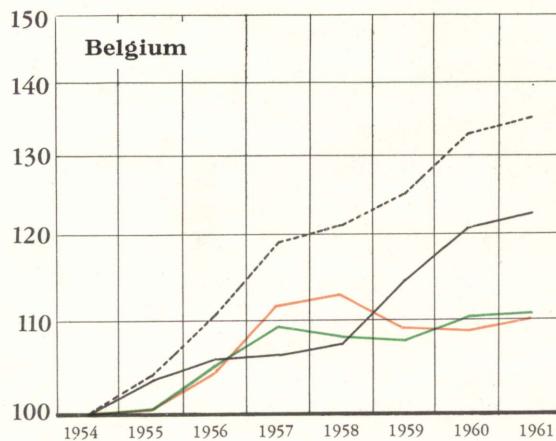
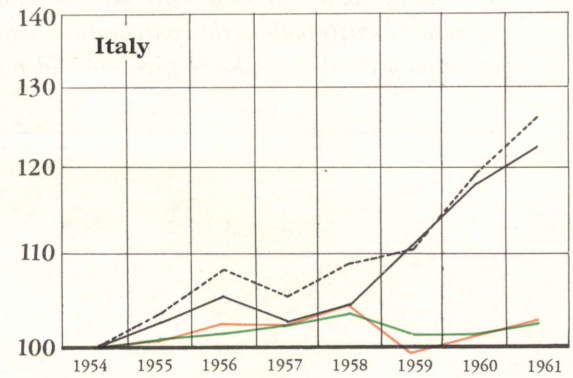
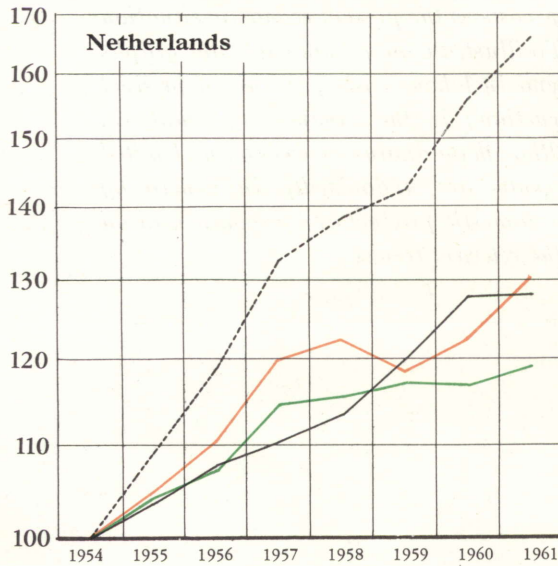
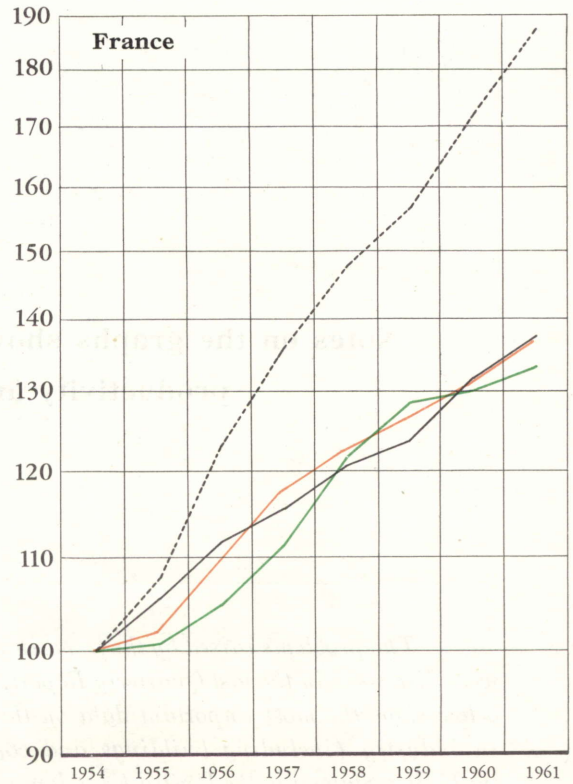
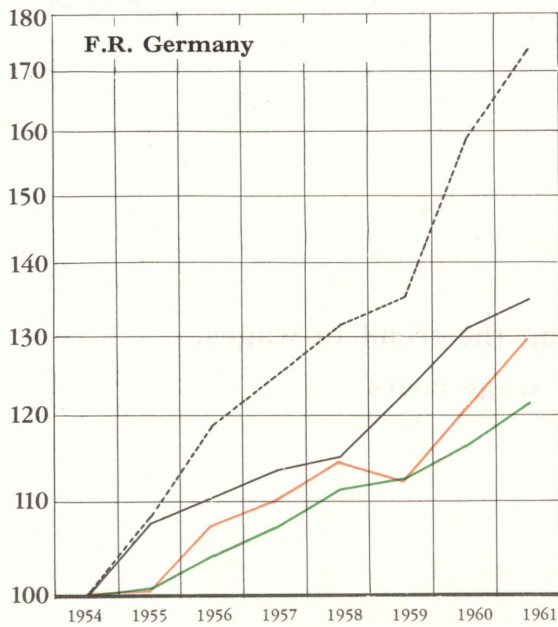
In the circumstances economic expansion in Luxembourg is likely to be very limited. All the more importance therefore attaches to the decisions recently taken on structural policy, and the relevant measures should be implemented as quickly and as resolutely as possible. All progress made in the coming months in putting the country's industrial structure on a broader basis will be of great value in underpinning the economic situation.

**Notes on the graphs showing the trend in wages,
productivity and wage costs**

The problems raised by the trend in wage costs in the present economic situation were discussed in the last Quarterly Report. To illustrate the points made, the graphs below show the most important data on the trend in labour costs per unit of product in industry (including buildings and construction) in the Community countries, the United States and the United Kingdom. Although the analysis covers only a limited section of total domestic product and the results are undoubtedly influenced by structural shifts both in the contribution to gross domestic product and in compensation of employees, the graphs do give some idea of the relevant trends.

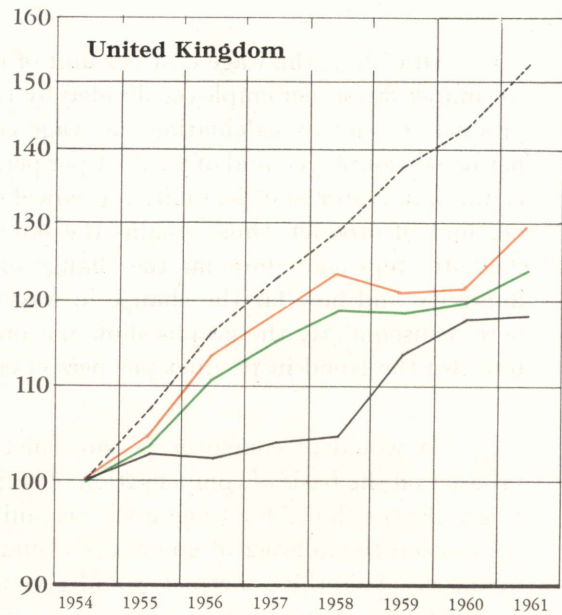
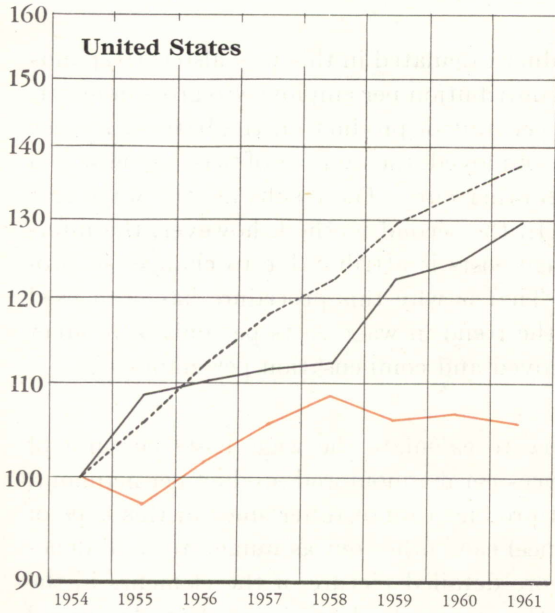
WAGES, PRODUCTIVITY AND WAGE COSTS IN INDUSTRY

1954 = 100



WAGES, PRODUCTIVITY AND WAGE COSTS IN INDUSTRY

1954 = 100



- *Total wages per head*
 - *Product per head*
 - *Wage costs per unit of product*
 - *Implicit price index*
- Semi-logarithmic scale*

In order to attain maximum comparability between countries, the figures used have been taken as far as possible from national accounts prepared on OECD definitions. To obtain the wage cost per unit of product, compensation of employees (value) is divided by the contribution to gross domestic product (volume). Compensation of employees covers not only wages and salaries (including overtime pay) but also bonuses, shares of profits, commission, holiday allowances, benefits in kind and employers' contributions for social insurance.

Of course, the wage cost per unit of product calculated in this way also corresponds to compensation per employee divided by the contribution per employee to gross domestic product; in fact by calculating the wage cost per unit of product on the basis of income per person employed and of product per person employed, the number of persons employed in the numerator and denominator cancel each other out. The result, i.e. the wage cost per unit of product, thus remains the same. In the second method, however, the intermediate steps show how far the change in wage costs is attributable to changes in productivity and how far the change in wages. That is why this procedure has been used here; consequently the graphs show not only the trend in wage costs per unit of product but also the trend in product per person employed and compensation per employee.

It would of course be possible in theory to calculate the wage costs per unit of product on the basis of compensation of employees per manhour and product per manhour. Logically the figure for wage costs per unit of product cannot differ since in this type of calculation the number of manhours would cancel each other out as numerator and denominator. This third method would give a more detailed picture of the elements in the trend and would make it possible, by using at the same time data obtained by the second method, to draw certain conclusions concerning the effect on wage costs produced by changes in the number of hours worked per head. In the present state of statistics on hours worked, sufficiently accurate figures concerning the total number of hours worked—particularly concerning the hours worked by salaried staff—are not available in all cases; even for the manufacturing industry alone, sufficiently comparable figures are not available.

Some of the figures for 1961 are provisional, and are drawn from national sources; others are estimates made by the staff of the Commission. In some cases it was not possible to derive the figures from the system of national accounts. In Western Germany and France, for instance, figures were not available for compensation of employees nor, for the USA, the contribution of industry to gross domestic product. In these cases it was necessary to assume the validity of other figures, based in part on calculations made by the Commission's staff.

In order to ensure maximum comparability between countries, the figures on employment have been taken from OECD statistics. They cover wage earners and salaried staff in industry and small undertakings.

Wage costs per unit of product in industry have been calculated and given in national currencies, since this trend is the most important for internal problems of price policy and economic policy. Finally, the graphs also show (except for the United States for which no figures are available) the implicit price deflator of the contribution of industry to gross domestic product, calculated on the basis of changes in value and in volume; this has been done to allow a comparison between the wage cost on the one hand and the prices of the product (contribution of industry to gross domestic product) on the other.

The trend in wage costs per unit of product has become one of the major problems of economic policy today. Indeed, the steeper rise in prices and the fall in profit margins are closely bound up with the trend in wage costs. This obviously provides a threat to balanced economic growth.

It must, however, be taken into account that there are also other factors, such as certain effects of the fiscal system and import costs, as well as price fixing arrangements adopted by firms which exert their own influence on the level of costs, prices and profit margins. The development of demand has, in certain member countries also exerted considerable influence on both prices and wage costs, at least for limited periods. It must be emphasized that the graphs do not explain the causes of the rise in prices, of the trend in wages and wage costs or of the reduction in profit margins, but only show how they are in fact developing.

The graphs show that in some member countries wage costs in industry have during the last few years been rising very steeply. While the increase in productivity slowed down appreciably after very rapid expansion in 1959 and part of 1960, wages rose in 1959, slowly at first but then with greater momentum. Except for France, where the currency was twice devalued in 1958, the "scissor" movement between trends in productivity and in wages meant that in 1959 wage costs per unit of product fell in all Community countries, in the USA and in England. In the next two years wage costs in industry went up steeply in Western Germany, the Netherlands and France, only slightly in Italy and the United Kingdom and remained more or less unchanged in Belgium and USA.

The wage cost curves shown in the graphs do not indicate how the competitiveness of each country is developing in relation to the others; conclusions as to relative competitive positions would have required separate investigations for all the various branches in which exports and/or imports are of importance. Moreover, the changes made in the rates of exchange in Western Germany, France and the Netherlands since 1954 would also have to be taken into account. Finally, conclusions on competitiveness cannot be drawn from the curves, since they cannot take the position in the base year itself into account. For example, the starting position in 1954 appears to have been marked by the fact that Western Germany had a considerable competitive advantage over the other industrial countries as regards the level of wages and prices, the pattern of production and productivity and established trade relations, so that till recently the rise in wage costs over the last few years could be looked upon as an alignment on the conditions prevailing in other important countries.