

EUROPEAN  
ECONOMIC  
COMMUNITY  
COMMISSION



DIRECTORATE-  
GENERAL  
FOR ECONOMIC  
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AFFAIRS

**THE ECONOMIC SITUATION  
IN THE COMMUNITY**

**2**

**JUNE**

**QUARTERLY SURVEY**

**1964**

Commission of the European Economic Community  
Directorate-General for Economic and Financial Affairs  
Directorate for National Economies and Economic Trends  
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**EUROPEAN ECONOMIC COMMUNITY**

**COMMISSION**

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**The Economic Situation in the Community**

**JUNE 1964**

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## I. THE OVERALL SITUATION

*In the first quarter of 1964, and most probably also in the following months, there was a further vigorous expansion in economic activity.*

*Largely owing to the marked expansionary trend in the world as a whole, the pressure of external demand was even stronger than before. The long-term rise in exports of goods to non-member countries became more rapid. In the first quarter the value of these exports exceeded the level for the corresponding period of last year — which was admittedly somewhat low as a result of special factors such as the severe cold spell in January and February 1963 — by no less than 15 %.*

*But internal demand within the Community also continued to grow briskly, partly owing to a faster increase in gross fixed asset formation. For one thing, the good weather gave a special stimulus to investment in building and construction. Furthermore, capital expenditure on equipment was generally influenced by the increased propensity to invest recently observable in several countries. This applies particularly to the Federal Republic of Germany, but also to the Netherlands and Belgium. Even in France it would appear that the previous weakness of the growth in private industrial investment may have come to an end. Only in Italy did investment remain slack.*

*The trend of private consumers' expenditure differed widely from country to country. With a somewhat quicker increase in the Federal Republic of Germany, a much higher level in the Netherlands, and a decline in the pace of expansion in Italy and France, there was hardly any slowing-down of the overall rate of growth.*

*The faster rise in industrial production which had already become perceptible in the fourth quarter of 1963 continued in the first quarter of 1964. According to the index of the Statistical Office of the European Communities, adjusted for seasonal and fortuitous variations, the increase on the previous quarter was 3 %, compared with one of 2.5 % from the third to the last quarter of 1963. The expansion in the Federal Republic of Germany, Luxembourg and the Netherlands was particularly brisk, while in Italy the growth in activity became very slight or ceased altogether.*

*The labour market remained strained throughout the Community, except in Italy, although seasonal unemployment and short time were very low, owing to the relatively mild weather.*

*The rise in Community imports was as fast as ever, partly because of greatly increased purchases of raw materials and semi-finished goods. Imports of goods from non-member countries were 16 % higher in terms of value than in the first quarter of 1963. As a result of the high exports, however, the tendency of the Community's balance of visible trade to run increasingly into deficit appears to have come more or less to a halt. Even so, on the basis of customs returns (cif-fob), there was a deficit for the first quarter of 1964 of about \$1 000 million — which is \$170 million larger than that for the corresponding period of last year. The overall current balance of payments also showed a deficit, albeit considerably smaller. On capital account there was a slight surplus. The gold and foreign exchange reserves of the monetary authorities of the member countries declined in the first four months of the year by about \$400 million, but it would appear that at the same time the commercial banks of the Community as a whole improved their net foreign exchange position.*

*Generally speaking, the upward pressures on prices continued unabated in the first four months of the year. True, the indices of consumer prices in all the member countries except the Netherlands rose less sharply than in the first four months of 1963. This was mainly due, however, to a — partly seasonal — decline or stabilization of food prices; there was only a slight slackening in the Community as a whole in the upward movement of prices for finished industrial products and services, and this was concentrated mainly in France and Italy.*

*The prospects for the coming months up to the end of 1964 point, for the Community as a whole, to a continuation of about the present rate of economic expansion.*

*The rise in exports to non-member countries is likely to quicken even a little more, largely owing to increased purchases by the developing countries. Internal demand should also increase appreciably, although at a somewhat slower pace. Demand for capital goods will rise faster in the Federal Republic of Germany and at a*

rapid pace in Belgium and the Netherlands, although a certain slackening in the Netherlands might occur towards the end of the year; in France investment demand might revive to some extent; only in Italy is it likely to remain at a really low level. Consumer expenditure, too, will rise further, a slackening in the basic rate of expansion being likely in France, Italy and perhaps also the Netherlands, while a certain quickening of the tempo is to be expected in the Federal Republic of Germany.

— Industrial production should continue to grow rapidly in all the member countries except Italy, although perhaps not quite so fast as in the first half of the year.

Despite an upturn in the imports of the Federal Republic of Germany, the expansion of imports from non-member countries might slow down somewhat during the rest of the year, while remaining quite substantial. The Community's balance of trade should not deteriorate any further.

Nevertheless, to judge by the trend up to the present and the outlook for the future, the Community's trade balance (cif-fob) for 1964 as a whole is likely to show a deficit between \$3 000 million and \$3 500 million. The Community's current payments will roughly balance out.

In other respects, too, there is little change in the outlook for 1964 as previously assessed and published in Quarterly Survey No. 1-1964. The growth in the real Community product is still estimated at 5 %, while the index of industrial production might go up by 7 %.

In contrast to the prospects for the Community's real economic growth, which, looked at alone, are very satisfactory, the forecasts of the economic trends up to the end of 1964 and — as far as is possible at this stage — on into 1965 point to a persistence of the Community's internal and external disequilibrium. Costs and prices are continuing to show an upward tendency; the changes in net balances which have occurred in intra-Community trade owing to the differing degrees of inflationary pressure in the various member countries remain symptomatic; and there is not likely to be any appreciable improvement in the Community's balance on goods and services with non-member countries.

It is true that, partly owing to the stabilization efforts undertaken by most member countries, there have been some signs of recovery of equilibrium. There has been an unmistakable slowing-down of the price rise in France and Italy, a distinct slackening of the growth in production and imports in Italy, and no further deterioration of Italy's balance of trade. In the Netherlands, however, the underlying inflationary pressure still appears to be strong, and in the Federal Republic of Germany

*there are indications of an incipient overheating of the economy, which is now also receiving an impetus from domestic demand. Furthermore, the tendencies towards improvement hitherto observable in France and Italy do not yet go far enough.*

*It is therefore necessary to continue the anti-inflation policy. To this end the Council of the Community on 14 April 1964 issued a concrete recommendation for "measures to be taken to restore the internal and external economic equilibrium of the Community". The economic policies of most of the member countries have in fact already turned along the lines indicated by this recommendation. It applies, however, not only to policies for 1964, but should also be borne in mind in taking all decisions affecting 1965. Strict observance not only of the letter of the Council's rules but also of their spirit and aims could make the prospects considerably more "balanced".*



## A. Recent developments

### 1. Demand

In the first quarter of 1964 and — as far as can be seen from the statistics available at this stage — also in the subsequent months, the economic situation in the Community was dominated by a further vigorous expansion of demand, including accelerated growth in external demand.

Exports of goods and services to non-member countries increased very substantially. According to the foreign trade statistics, the increase in the value of visible exports, adjusted for seasonal and fortuitous variations, from the fourth quarter in 1963 to the first quarter of 1964 amounted to 5 %, after a rise of less than 1 % from the third to the fourth quarter of 1963. In the first quarter increase in gross value over the level for the corresponding period of last year, which, owing to special influences (exceptional cold and strikes) had admittedly been relatively low, was no less than 15 %.

The main cause of the vigorous upward trend in the Community's exports was the growth in economic activity in most non-member industrial countries, which proved even more vigorous than had at first been predicted. Another contributory factor of increasing importance, to some extent connected with this, was the effect of the increased foreign exchange resources of the developing countries on their import policies.

The situation in the United States continued to be determined by underlying expansionary tendencies. Although the real gross national product in the first quarter, adjusted for seasonal variations, was only 0.7 % higher than in the fourth quarter (which was 1.3 % up on the preceding one), this would appear to have been only a temporary slackening. Stock-building in the first three months of the year was very low, as enterprises — contrary to their behaviour during the previous cyclical upswing — were obviously exercising restraint. Furthermore, investment in fixed assets tended to level off temporarily in expectation of the tax reduction introduced in March. The expansion in overall demand was thus largely based on the vigour of private consumption, particularly expenditure on durable consumer goods. In addition, however, there was an appreciable increase in public expenditure, and at the same time exports continued to show a distinct upward trend.

The Community's exports to the United States in the first quarter were 17 % above the level for the corresponding period of 1963 (which was admittedly relatively low owing to the aforementioned special factors).

The Community's deliveries to the EFTA countries in the first quarter of 1964 were also very considerably (14 %) up on the same 1963 figure). Exports to the United Kingdom, in particular, again increased sharply, with an annual rate of growth of 25 %

in the first quarter. The upswing in business activity which began in that country in the spring of 1963 continued during the recent period, with all the main components of demand still expanding vigorously. Industrial production, increased by 2 % from the fourth quarter of 1963 to the first quarter of 1964, and was up 10 % on the first quarter of last year. Although the economic expansion in the United Kingdom has not so far been accompanied by any serious strains, there has recently been a sharp rise in imports. The trade deficit in the first quarter of 1964 was more than twice as large as in the first quarter of 1963, despite a substantial rise in exports during the same period.

There was a marked increase in the Community's exports to the developing countries, the deliveries of the Federal Republic of Germany to these countries having, in particular, shown a pronounced rise in the first quarter. The expansion in the Community's total exports to the developing countries, compared with the corresponding period of the preceding year, was 13 %, deliveries to the associated overseas countries and territories having risen by 9 %.

*Community visible exports to non-member countries*

(% variation in value on preceding year)

Exports to	1963	1963				1964
		1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter
United States	+ 4.5	— 6	+ 8	+ 7.5	+ 7.5	+ 18
EFTA	+ 6	+ 1	+ 9	+ 4.5	+ 9	+ 14
including :						
United Kingdom	+ 8.5	+ 3	+ 9	+ 5	+ 18	+ 25
Developing countries	+ 2.5	— 6.5	+ 6	+ 6.5	+ 4.5	+ 12
including :						
Associated overseas countries and territories	+ 8	— 7.5	+ 20.5	+ 21.5	+ 3	+ 9
All non-member countries	+ 5	— 2.5	+ 7	+ 6.5	+ 7	+ 15

Unlike external demand, intra-Community demand did not expand any faster than before, but continued to grow steadily at a substantial rate. A slight slackening in the rise was observable in France and there was even a fairly marked loss of pace in Italy.

In the Federal Republic of Germany and in the Netherlands internal demand gathered momentum.

The growth in expenditure in the Community as a whole was very vigorous in the field of gross fixed asset formation. A leading part was played by investment in building and construction, where, in addition to a continuance of the high pressure of demand — still too high in most member countries — increased production possibilities, due to higher numbers of workers and very favourable weather for building, led to a sharp rise in activity and in actual outlays. This applied both to house-building and public construction activity in most member countries and also, especially in the Federal Republic of Germany and the Netherlands — but only slightly in France and not at all in Italy — to industrial building.

Investment in plant and equipment also showed a distinct upward trend in several member countries, especially the Federal Republic of Germany, where a full-scale investment boom might develop, and in the Netherlands. In Belgium, too, and to a lesser extent in France, further growth took place, while in Italy business investment as a whole was very slack.

The expansion of overall demand was again supported in the first quarter of 1964 by heavy investment in stocks, especially of raw materials and semi-finished goods.

There was a further very sharp rise in consumption expenditure. This was true firstly of public current expenditure, particularly as a result of large wage and salary increases in the Netherlands and Luxembourg, although there were also considerable and persistent upward economic pressures in other member countries. Secondly and especially, the expansion of private consumers' expenditure continued almost unabated. In Italy, where the year-to-year increases were particularly large, and to a certain extent also in France, the rate of growth appears to have slowed down. In the Netherlands, too, the pace of the increase in private consumers' expenditure, which had risen sharply in the previous quarter, showed some temporary slackening in the course of the first quarter of this year. In the Federal Republic of Germany, on the other hand, there were signs of a certain quickening of the rise in consumption, which had been very slight in 1963.

This movement of private consumer expenditure is a very true reflection of the changes in mass income, especially total wage and salary payments. With regard to the latter, there has up to the present been scarcely any slackening of the upward trend of wages in the Community as a whole. Here again, however, the overall movement is the product of differing trends in the various member countries. In Belgium there was a further rapid rise in wage rates, partly owing to the sliding wage scales, and also in actual earnings. In the Federal Republic of Germany there were clear indications of a further acceleration in the growth of actual earnings, despite the still relatively moderate develop-

ment of agreed wages. In the Netherlands there were very sharp rises in wages, particularly from 1 January and 1 April onwards. In France the rise continued, even rather more rapidly than in the fourth quarter of 1963. In Italy, on the other hand, while there was a faster increase in minimum scale earnings under agreements some of which had been concluded already in 1963 and also cost-of-living allowances (the latter owing to the effect of last autumn's particularly sharp price rise on the sliding wage scales), the increase in actual earnings slowed down somewhat.

There were certain changes in the structure of private consumers' expenditure, some of which, connected with the relatively mild weather in the early months of the year, were very short-lived: a relatively small rise in expenditure on heating and clothing, but a marked growth in outlay on furniture, household goods and textile furnishings, owing to the considerable increase in the number of new dwellings completed. Sales of passenger vehicles, which had previously slackened, also rose faster again in most member countries in the first quarter. In the Federal Republic of Germany and France, however, they did not regain the previous years' high rates of increase, whereas in Belgium and, still more in the Netherlands, there was a distinct acceleration, the number of new motor cars registered in the first quarter being 40 % higher in Belgium and no less than 70 % higher in the Netherlands than in the corresponding period of 1963. Only in Italy was there a distinct falling off.

## 2. Production

Supply from sources within the Community showed a further vigorous expansion, influenced not only by the force of demand but also by the weather conditions, which were much better than in the corresponding period of 1963.

The effect of the latter was reflected in agricultural production, which showed good results (especially in the case of vegetables and eggs) considering its seasonal limitations. Meat output appears to have been better in the case of pork than in the last quarter of 1963, while beef production was again insufficient to meet the demand.

Output in building and construction, too, remained very high, with a continued underlying upward trend, except in Italy, where, mainly owing to financing difficulties, the development of demand was quite weak. In the other member countries the year-to-year growth figures in building and construction in the first quarter were exceptionally high.

The basic upward movement of industrial production became more rapid. According to the index of the Statistical Office of the European Communities (adjusted for

seasonal and fortuitous variations, and excluding building and construction, foodstuffs, beverages and tobacco), production increased from the fourth quarter of 1963 to the first quarter of 1964 by no less than 3 %, after having gone up by 2.5 % from the third to the fourth quarter of 1963. In the first three months of 1964 the gross index was on the average 11 % higher than in the corresponding period of the previous year — although this was admittedly partly due to the relatively small rise in production during that period as a result of the special factors mentioned earlier.

It is worthy of note that the differences between one member country and another during most of last year are becoming more and more noticeable. In some countries where production was expanding at a relatively rapid pace last year — especially Italy, but also France — the rise in activity slowed down during the fourth quarter of 1963 or, as in Italy towards the end of the year and since then, came virtually to a standstill. In the Federal Republic of Germany, on the other hand, the upward price movement quickened perceptibly, and in Luxembourg the acceleration was even more marked. In the Netherlands production rose very steadily, but more slowly than in the same period of 1963.

The sharpest acceleration in the Community as a whole was in the basic materials industries, especially the iron and steel industry, the output of which in the first four months was 13 % above the corresponding 1963 level. This was attributable partly to the trends of stock formation in the Community and the rest of the world, and also to the long-term rise in demand from the processing industries, but also doubtless in part to seasonal shifts and fortuitous influences. The output of the capital goods industries in most member countries followed the trends, described above, of capital-goods and export demand, and turned sharply upwards in the Federal Republic of Germany. In the field of consumer goods production the expansion within the Community continued; in France, however, the growth slowed down and in Italy there was actually a certain decline in some branches of production, such as textiles.

The real contribution of services to the gross Community product — especially transport services, owing to the strong demand for basic materials — increased considerably more than usual for this time of the year.

The labour market situation in the Community was generally characterized by continued strains, although the good weather conditions meant relatively low levels of unemployment and little seasonal short time working, so that a large volume of labour (the number of employed wage- and salary-earners multiplied by the number of hours worked per head) was recorded. There was only a slow basic increase in the number of employed wage- and salary-earners, firstly owing to the relatively small growth in the working population and secondly owing to the almost complete exhaustion of the reserves of unemployed persons. Nevertheless, there was a further slight downward trend—symp-

tomatic of the strains—in the small unemployment figures in most member countries. Labour market strains became more acute, particularly in the Federal Republic of Germany, but also in the Netherlands (despite the hopes attached in various quarters to the large increases in wage rates), and in Belgium the labour market remained very tight. In Italy, on the other hand, there appears to have been an incipient easing of the bottlenecks created by labour shortage in a number of fields. In France there has so far been no marked change in the situation.

### 3. The balance of the markets

There was a further very sharp rise in the Community's imports, attributable not only to the brisk expansion in consumer, capital-equipment and export demand, with which internal supply was often unable to keep pace, but also to greatly increased demand for the purpose of adding to stocks of imported raw materials and semi-finished goods. Furthermore, the increased competitive power of goods from some non-Community countries may have helped to push up imports.

There was in any case a further upward trend in the Community's visible imports from non-member countries. Their value in the first quarter, according to the customs returns, was 16 % higher than in the first quarter of 1963, although it must be remembered that imports, too, were hampered during that period by the special factors which have already been mentioned a number of times.

In France and even more in Italy, partly as a result of the stabilization measures, the cyclical rise in imports from non-member countries slowed down. On the other hand, the Benelux countries' purchases from non-member countries increased. In the Federal Republic of Germany, too, commercial imports, adjusted for seasonal variations, rose faster than in the fourth quarter of 1963.

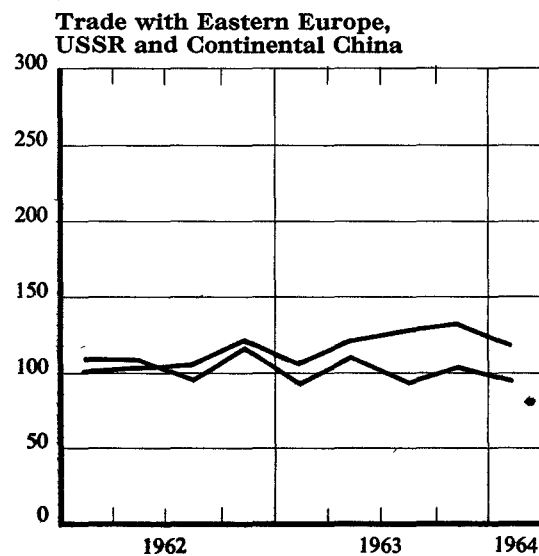
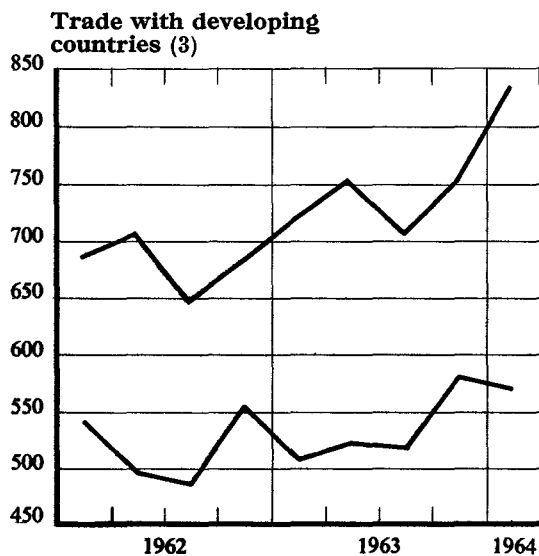
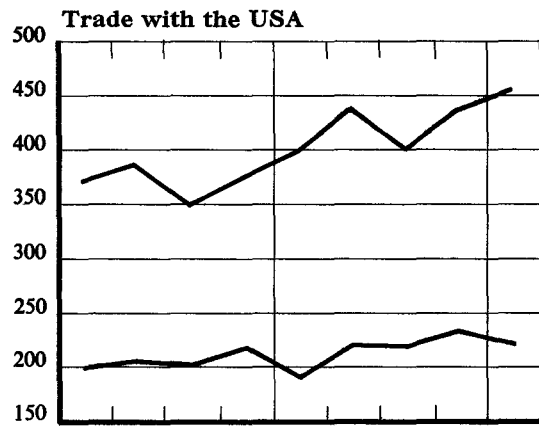
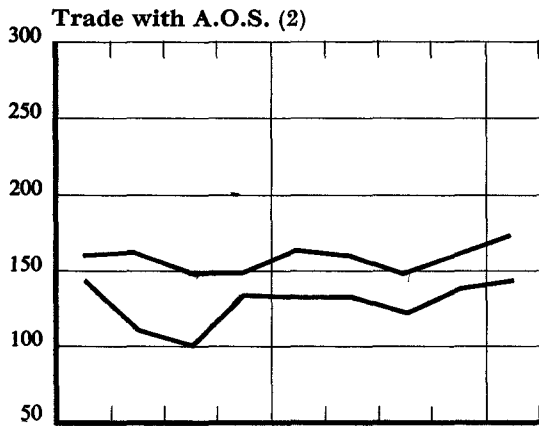
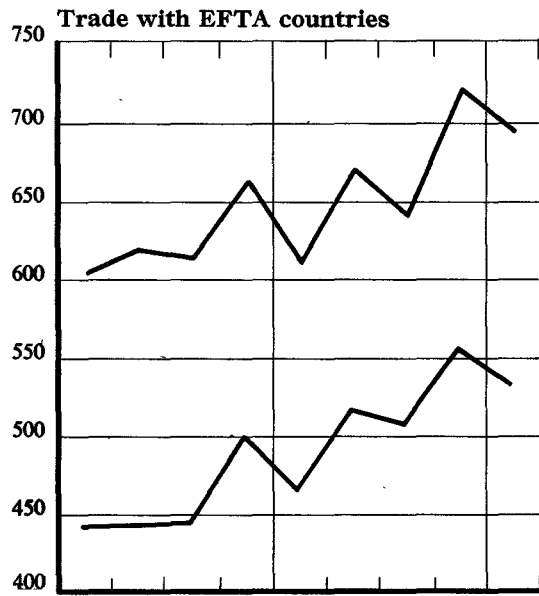
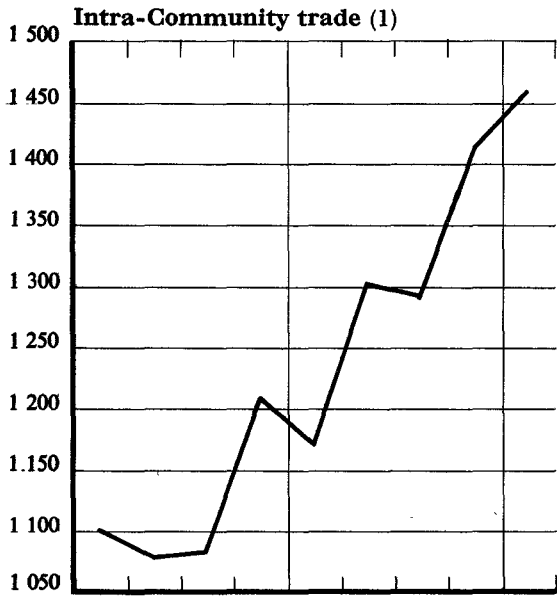
According to the incomplete figures available, there were no major changes from the fourth quarter of 1963 in the structure of imports according to categories of goods. The main feature was again the sharp increase in imports of finished goods. The rise in raw material imports which was observable in the second half of 1963 would also appear to have accelerated in the first quarter. In general, however, purchases of farm products fell off somewhat.

As to the geographical distribution of imports, the main feature was a distinct rise in purchases from the developing countries. There was also an appreciable growth in imports from the industrial countries, those from the United Kingdom, in particular, having risen faster again after the previous slackening.

# COMMUNITY TRADE

Monthly averages

In millions of dollars



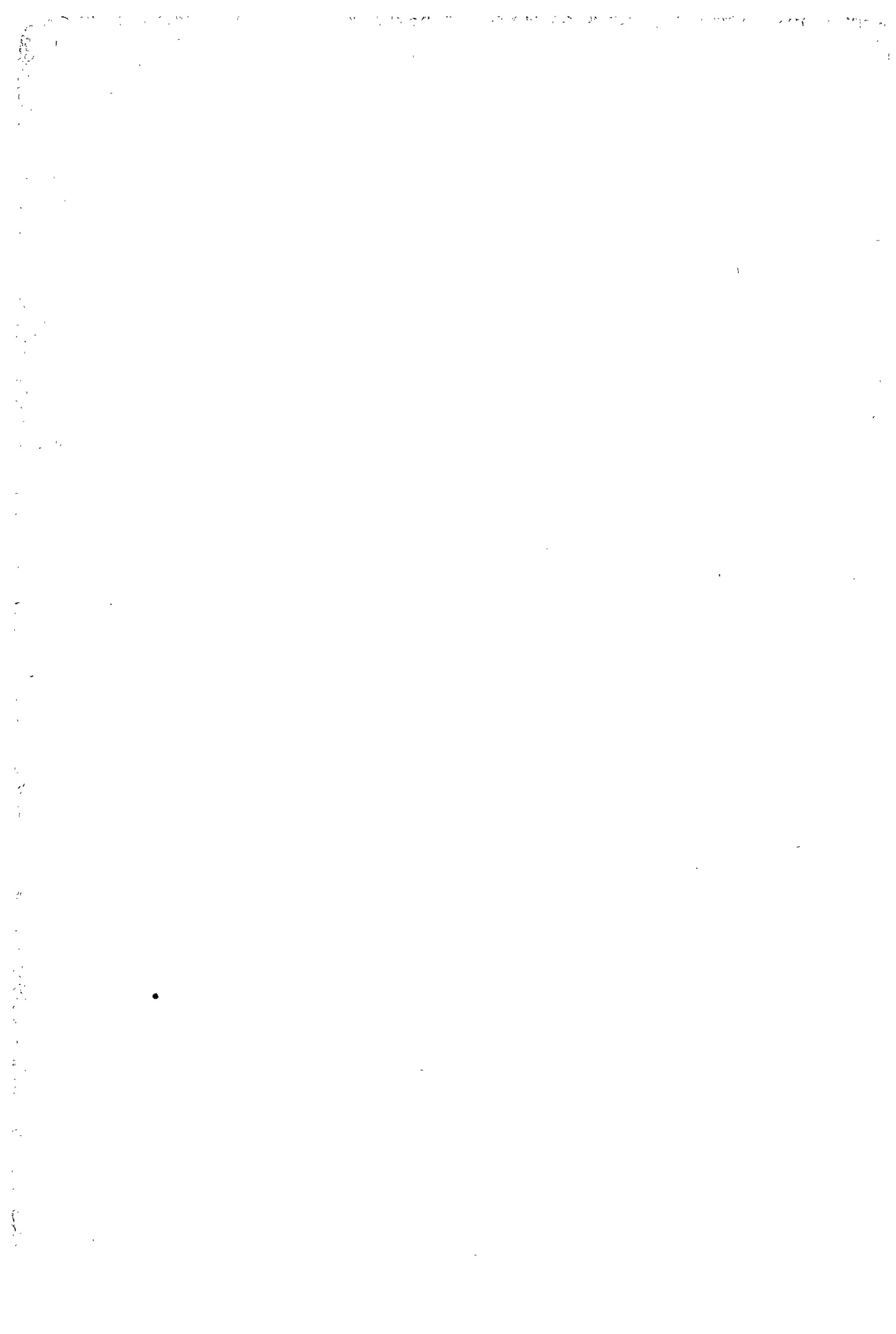
Exports

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.





*Community visible imports from non-member countries*

(% variation in value on preceding year)

Imports from	1963	1963				1964
		1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter
United States	+ 13	+ 9	+ 16	+ 14	+ 14	+ 14
EFTA	+ 12	+ 9	+ 16	+ 14	+ 11.5	+ 14
including :						
United Kingdom	+ 17	+ 15	+ 24	+ 21	+ 12	+ 14
Developing countries	+ 8	+ 9	+ 6.5	+ 8	+ 10	+ 16
including :						
Associated overseas countries and territories	+ 3	+ 3	0	0	+ 9	+ 6
All non-member countries	+ 10.5	+ 7.5	+ 11	+ 12.5	+ 11.5	+ 16

Visible trade between the member countries, measured by the customs returns (on the basis of imports) was 25 % higher in value than in the first quarter of 1963. Although this year-to-year growth is partly due to the effects of the very cold weather in the early months of last year on the level of trade at that time, it nevertheless reflects an even more vigorous expansive trend than was observable in the last three months of 1963. The purchases of France and Italy, in particular, showed a further substantial increase, although their basic upward movement slowed down somewhat in Italy in the first quarter. Similarly, the purchases of the Netherlands and, more still, those of Belgium, showed a high rate of growth in the first months of the year, connected with the vigorous expansion of domestic demand. On the other hand, Germany's imports from other member countries so far showed only a small rise—especially in the case of farm products, although the prices of these are certainly not higher than in the Federal Republic. There were really large increases in deliveries by France, and again in those by the Netherlands, while the expansion in Italy's exports to other member countries was somewhat slower. Demand from the member countries was, however, as previously, mainly directed towards the Federal Republic of Germany and the B.L.E.U.

The position in the first quarter as just described shows no very appreciable diminution of the disequilibria in trade between the member countries which have developed since the beginning of 1963. It can be said, however, that there has been no further aggravation of the internal imbalance in the Community. Indeed, signs of a slight improvement were observable during the last weeks.

The trade balances of the individual member countries with all the other members of the Community underwent no major changes in the first quarter. On the basis of the seasonally adjusted figures, the Federal Republic again had a very large surplus, almost as great as that for the previous quarter. The B.L.E.U., too, had a slight surplus, which has recently tended to increase somewhat. The continued substantial deficit of the Netherlands does not appear to have grown appreciably larger, while in Italy there has so far been no noteworthy improvement. There was some further deterioration in France's trade balance.

In the Community as a whole the underlying upward price trends continued without interruption. It is true that in France the increase was at the slower rate which had already become observable during the fourth quarter of 1963, and in Italy, too, the pace of the upward movements appears to have slackened. But in the Netherlands prices went up extremely sharply from the fourth quarter of 1963 to the first quarter of 1964, although the rising trend moderated somewhat during the latter period. In Belgium the tendencies towards higher prices continued at the accelerated rate which they had attained in the second half of 1963. In the Federal Republic of Germany there was already a certain further strengthening of the basic upward price movements.

This underlying price trend and the changes in it were either accentuated or concealed, in the individual member countries, by seasonal or abnormal variations. In Italy and France for example, the extent of the slowdown is not as great as it seems, since a decline in the prices of various foodstuffs retarded the rise in the index. In the Federal Republic, too, some food prices fell below their corresponding 1963 level.

In the Netherlands, on the other hand, the index certainly exaggerated the usual seasonal April rise in the prices of vegetables and potatoes, which caused a larger—doubtless temporary—jump in the index than was justified by the long-term trends.

Among the causes of the general upward trend of prices, the rise in production costs per unit of output continued to play a part. This factor has acquired increased importance in those member countries where, owing to the slackening of the growth in production (due to declining demand growth rates), the rise in productivity has become appreciably slower. Italy is a typical example of this. In the Netherlands, too, the price rises reflect a marked rise in wage costs, but in this case pressure is also being exerted

by monetary demand—a combination of a consumption boom and a capital investment boom. There is also one case—that of the Federal Republic—where the rise in costs per unit of output has, for the time being, stopped, owing to a considerably faster improvement in productivity coupled with a still moderate wage trend, but where excess demand is now beginning to force up the price level again.

In addition to being affected by cyclical, fortuitous and seasonal tendencies, price levels were also influenced during the period under review by external factors, namely by the repercussions of higher import prices for many raw materials and by government price measures. With regard to the last-mentioned factor, there are on the one hand the measures which exert a psychological moderating effect on prices, such as the direct controls over prices and trade margins in France, Belgium and the Netherlands, and on the other hand the increases in controlled prices and the rates of indirect taxes. The latter measures are usually adopted in order to exert an anti-inflationary influence on the trend of demand (the raising of the petrol tax in Italy and the Netherlands, the cigarette tax in the Netherlands, telephone charges in Italy and railway charges in Belgium, and the introduction in Italy of a special tax on the purchase of new cars). These measures in fact restrict overall real internal demand and at the same time help, directly or indirectly, to reduce the governments' budget deficits.

Altogether the consumer price indices for April 1964 exceeded their corresponding level for 1963 (December 1963 figures in brackets) by 4.6 % (6.9 %) in Italy, 4.7 % (6 %) in France <sup>(1)</sup>, 7.0 % (3.6 %) in the Netherlands, 3.3 % (4.2 %) in Belgium, 2.1 % (4.0 %) in the Grand Duchy of Luxembourg and 1.6 % (3.5 %) in the Federal Republic.

In assessing these rises, especially where they are smaller between December 1963 and April 1964, it should be borne in mind that prices increased very sharply in all member countries during the first quarter of 1963, chiefly owing to the effects of the exceptionally hard winter.

The previous very pronounced tendency of the Community's trade balance with non-member countries to deteriorate appears to have weakened distinctly, owing to the faster rise in exports in the first quarter of 1964. The trade figures, adjusted for seasonal and fortuitous variations, in fact show scarcely any increase in the adverse balance compared with the fourth quarter of 1963. Even so, the deficit (on the basis of customs returns) amounted to over \$1 000 million—\$170 million more than in the first quarter of 1963. There was probably also a distinct deficit in the Community's overall current

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<sup>(1)</sup> Old index (250 items).

balance of payments in the first quarter of 1964, while the capital balance doubtless still resulted in a surplus.

The gold and foreign exchange reserves of the monetary authorities of the member countries declined in the first four months by \$400 million. On the other hand, there was an improvement in the net foreign exchange position of the commercial banks.

The development of the balance of payments virtually ceased to have any expansive effect on internal liquidity in most member countries. In Italy, indeed, the heavy payments deficit was accompanied by a marked tightening. In the Federal Republic, however, the contrary was the case in the first quarter as a whole, bank liquidity, in particular, having been very substantially expanded as a result of the balance-of-payments position. The increase in bank liquidity took place in spite of the usual seasonal constricting influences emanating from the central public authorities. Demand for credit by business and industry remained moderate, being of course restrained by the sharp increase in the economy's liquidity resulting from the export surpluses. In France a certain amount of progress was made towards monetary stabilization in that the expansion of bank credit was kept within the prescribed limits until February, and the liquidity-creating effect of the public cash deficit was substantially reduced. In Italy both the balance-of-payments deficit and the high level of private households' cash holdings had a tightening effect on bank liquidity and the capital market. The expansion of commercial bank credit was less vigorous than before, despite a faster increase in the rate at which money was made available to the banks by the central bank. These funds were provided in such a way that, under the influence of the aforementioned restrictive factors, bank liquidity was on balance appreciably reduced. In the Netherlands, on the other hand, bank liquidity was clearly still very high; in the first quarter the commercial banks, under the pressure of the considerably greater demand for credit, largely attributable to the effects of the wage increases, again exceeded the agreed limit to credit-granting. In Belgium the quantitative expectations regarding limitation of credit expansion (from 24 % last year to about half that increase this year) were exceeded by an even greater margin by the way lending actually developed. A point worthy of note is that in this case capital market conditions have now improved, which has also benefited government borrowing.

The public authorities' cash transactions were characterized in nearly all the member countries in the early months of 1964 by a (partly seasonal) improvement in the timing of revenue receipts and expenditure. In France, for instance, the cash deficit was reduced in the first three months to half what it was in the corresponding period of 1963. In the Federal Republic further substantial amounts of funds were withdrawn from circulation—albeit only temporarily—by public loan issues and government payments to other countries. In Belgium tax revenues climbed appreciably; in the first four months the government was able not only to finance its excess expenditure by means of loans but also at the same time to consolidate a small part of the short-term public debt. In Italy, however, the government's indebtedness to the Central Bank, which had risen sharply up to the end of 1963, was only slightly reduced in the first quarter.

*Trend of supply and utilization of goods and services (1)*

	1962 (2)	1962 (3)	1963 (3) (4)	1964 (4) (5)
	At current prices (in \$ '000 million)	% variation by volume on preceding year		
Gross Community product	225.7	5.0	4	5
Private consumption	137.6	6.1	5.5	5
Public consumption	32.1	6.7	4.5	3.5
Gross fixed asset formation	51.6	6.3	4	5.0
Balance exports (6) minus imports (6) (in \$'000 m.)	+ 1.5	+ 1.2	+ 0.4	+ 0.65

(1) The aggregates for the Community (not including the Grand Duchy of Luxembourg) are computed on the basis of the official exchange rates.

(2) In 1962 prices; average 1962 exchange rates.

(3) In prices of the preceding year; exchange rates of the preceding year.

(4) Commission estimates; rounded figures.

(5) Commission forecasts.

(6) Goods, services and factor income.

## B. Outlook

For the coming months up to the end of 1964, the prospects for the Community as a whole are of vigorous economic expansion.

With regard to exports to non-member countries, the figures available point to a further pronounced rise in the second half of the year. The assumption that there will be a growth in external demand is based firstly on the very favourable economic conditions in the main industrial countries and secondly on the fact that demand from the developing countries, whose foreign exchange resources have recently grown still further, may be expected to increase.

In the United States the tax reduction recently decided upon undoubtedly represents a powerful stimulus to economic activity. It will increase available income in 1964 by about \$10 000 million, the effects being doubtless largely concentrated in the second half of the year. Moreover, the rise in wages might quicken during that period. In any case, some trend-setting wage negotiations will be taking place in some important sectors in the second half of the year. Investment in fixed assets will certainly make a larger contribution to economic expansion than in the first half of the year. According to the survey made by the Security Exchange Commission in February, industrial firms intend to increase their capital expenditure by 10 % in 1964. Indeed, the results of the MacGraw-Hill survey in April point to an even greater expansion. On the other hand, the expansionary effect of public expenditure is likely to weaken somewhat during the year. In short, the coming months can certainly be expected to witness a very substantial growth in demand in the United States, which will undoubtedly have its repercussions on imports.

In the United Kingdom, too, it is expected that the expansionary tendencies will clearly predominate. The increases in some indirect taxes introduced in the 1964-65 budget will probably have only a slight restraining effect on private consumers' expenditure especially as the rise in private household incomes is likely to quicken. Furthermore, the revival of capital investment activity which began in the second half of 1963 will continue, as is shown in particular by the distinct increase since the beginning of 1964 in the orders received by the engineering industry. Lastly, there will be a further marked rise in public expenditure in the coming months, mainly owing to increased capital outlay by local authorities.

There will thus be a further marked expansion in the Community's exports to the United States and the United Kingdom in the second half of the year; they will certainly continue to show a faster percentage rise than total deliveries to the other industrial countries, whose markets also offer very good prospects for the sale of the Community's products.

The economic expansion in most industrial countries will most likely continue to necessitate substantial purchases of raw materials, even if there is some slackening in the partly speculative stockbuilding tendencies, as is quite possible, at least in the Community. The purchasing power of the developing countries will therefore increase further, especially if raw material prices do not decline appreciably from the high level at which they still stood in the first half of 1964. Consequently there might be a further substantial increase during the rest of the year in demand for the Community's products from the developing countries.

With regard to the probable development of the individual components of internal demand, there should in the first place be very marked growth in gross fixed asset formation in the Community as a whole. True, investment in building and construction might increase rather more slowly owing to the restrictive measures adopted in some countries. Nevertheless, everything points to a more rapid increase in investment in plant and equipment. In the Federal Republic of Germany there have for some time been signs of a very marked growth in the volume of new domestic orders received by the capital goods industries. The position is similar in the Netherlands, where, however, the propensity to invest is expected to decline again somewhat in the last months of 1964 owing to the pressure of increased wage costs on profits. In Belgium business investment will continue to expand vigorously, and in Luxembourg it should also show a faster upward trend, at any rate in the steel industry. In France, according to the latest surveys carried out among business men, the decline in orders for capital goods from private firms would appear to have come to an end at the beginning of 1964, so that in the second half of the year firms are likely to be less hesitant than hitherto in embarking on capital expenditure. In Italy, on the other hand, conditions for capital expenditure will be adversely affected by a number of factors, particularly the slower growth in some components of demand, the narrowing of profit margins and the difficulty of raising the necessary funds.

In view of the brisk expansion in private consumers' expenditure in the Community as a whole, there is no reason to revise the forecasts made at the end of 1963, since the main changes of trend—a slight quickening of the pace of private consumption in the Federal Republic and a simultaneous slowing-down of the increase in France and Italy—should largely cancel each other out. This recent development can in any case be expected to continue in the coming months. The prospects for the autumn, however, are more doubtful, as it is not yet known whether there may not be a further round of excessive wage increases in the Netherlands and France; the same applies even to Italy unless internal demand has been sufficiently curbed by then. For the Federal Republic, too, it can be predicted with a fair degree of certainty that there will be very substantial wage increases in the autumn, chiefly owing to growing strains in the internal economy.

The coming months should see a further pronounced increase in supply from within the Community. This applies in the first place, assuming that normal weather conditions continue, to agricultural output, which, on this assumption, should be a good

deal better than in 1963. The vigorous upward trend of industrial production will probably continue, although there is hardly likely to be any overall acceleration, firstly because the growth in demand will have slowed down in Italy and France and perhaps also because in these countries—especially Italy—the reduced competitiveness might have a certain retarding effect and secondly because, particularly in the Federal Republic, physical bottlenecks, particularly labour shortages, are likely to make themselves increasingly felt, preventing the rise in production from keeping pace with the faster growth in demand.

The movement of price levels will reflect to an increasing extent the changes which have recently become apparent: a further weakening of the forces pushing up prices in France and Italy, without the price inflation being yet sufficiently arrested; very strong upward price trends in the Netherlands, although they will slow down somewhat during the year; a steady upward movement in Belgium-Luxembourg; and a gradually strengthening upward price trend in the Federal Republic.

The vigorous growth in imports will continue, but the rate of increase might be somewhat slower than hitherto: the expansion of imports into France is likely to slacken and might even cease altogether in the case of Italy. In general, raw material imports will probably rise slightly more slowly than before. In view of the estimated growth in exports it can be assumed that the Community's balance of trade will at least not deteriorate any further. Even so it can be expected to show, for the whole of 1964 as compared with 1963, a rather heavier deficit (at somewhere between \$3 000 million and \$3 500 million) and overall current payments may well therefore just balance out.

As to the estimated changes in the volume of the main components of overall demand and overall supply in the Community for the whole of 1964 as against 1963, there appears to be no need for any substantial adjustment of the figures published in the Quarterly Survey No. 1/1964. In particular, the Commission's staff still expect an increase in the real gross Community product of about 5%. The monthly average of the Community index of industrial production for 1964 may be expected to be 7% higher than in 1963.

The economic prospects for the coming months up to the end of 1964 do not yet point to a restoration of the internal and external equilibrium of the Community—that is, a cessation of the inflationary situation especially in France, the Netherlands and Italy, a better balance of the flows of trade between member countries and the restoration of an appropriate surplus in the Community's overall balance of current payments with non-member countries—even though the estimates take into account the stabilization efforts so far made in varying degrees in all the countries of the Community. This policy was in fact already largely in accordance with the requirements of the "Recommendation for measures to be taken to restore the internal and external economic equilibrium of the Community" which was made to the Member States on 14 April 1964 by the Council of the Community, at the suggestion of the Commission, under Article 103 of the EEC Treaty.



(The text of this recommendation, together with the Commission's accompanying explanatory report is reproduced in an Annex to this Quarterly Survey). Some new measures have also already been taken as a direct result of these recommendations. The country chapters of this Quarterly Survey contain comparisons of the economic policies of each of the member countries with the above-mentioned recommendations, but it should be pointed out that these comparisons are only very summary and provisional, as too short a period had elapsed before they were written; the member countries gave themselves two months to examine their economic policies, adopt or decide upon new measures and notify the Commission. The Commission, in turn, is then to report to the Council on the implementation of its recommendations. At the time of writing, the reports from the countries to the Commission had not yet been completed, and moreover a certain amount of time is needed for evaluating and assessing them.

The Commission is, however, naturally aware, owing to its regular contacts, of what is happening in the field of stabilization policy in the individual member countries: what concrete measures and decisions have been taken, what is still under consideration and what remains undecided or is giving rise to—primarily domestic—difficulties. The forecasts of economic developments up to the end of 1964 are therefore very realistic. They show that, largely under the influence of the stabilization policies, certain trends towards a restoration of equilibrium have in fact set in and become clearer than they were three months ago. This is reflected in the forecasts for internal demand, prices, production and imports, which for the most part indicate a certain slackening of the rise in the countries where inflationary pressure has so far been strongest, namely Italy and France. On the other hand, however, there are very clear signs of a quickening of the tempo of economic activity in the Federal Republic, now also partly due to internal influences—tendencies which, although they make for a better balance of the currents of trade within the Community, are far from desirable in other respects, since upward price trends in the Federal Republic create problems both from Germany's own point of view and from that of the Community, especially as they are certainly no help to stabilization in other member countries.

Those of the tendencies mentioned which can be regarded as desirable are, however, far from being sufficiently clear and strong to meet the needs of the situation. The stabilization policies must therefore be continued along the lines of the aforementioned recommendations, and some member countries would doubtless be well advised to adhere even more strictly to the rules laid down therein. This also applies to the Federal Republic, where, as stated, some of the incipient trends, involving a danger of "overheating" of the economy, must be regarded as harmful.

Nevertheless it would appear that the competent authorities in the member countries are endeavouring to comply with the main requirements of the recommendations, although perhaps not quite so fully in 1964 as they are likely to in 1965. For the EEC Council has recommended that the governments should frame their economic and financial policies for 1965—in so far as they have already been worked out and approved in 1964, which is the

case in most of the countries—on the same principles as are to be followed in 1964. While it is very difficult, both administratively and from the point of view of domestic policy, to make any major changes in economic targets for 1964, especially if they are really to take effect in 1964, it is at present relatively easy to adopt measures for the coming year which comply with the recommendations. For example, with regard to the reduction of the expansion in public expenditure previously planned for 1965, the Governments of the Federal Republic and France have already adopted decisions of principle which are largely in accordance with the recommendation.

The first conjectures regarding the possible course of economic affairs in 1965 suggest that there is every justification for planning, at least for a while, continued pursuit of anti-inflationary policies.

Some preliminary estimates for 1965 are already available. Firstly, within the Community, there are the "preliminary economic budgets" which are drawn up by the member countries and are to be compared before the summer recess in the Short-term Economic Policy Committee. These are initial, essentially "neutral" estimates, comparable between the member countries, of the main lines of economic development in the form of a few tables accompanied by passages of text stating the assumptions on which they are based. This procedure was introduced last year by the Short-term Economic Policy Committee at the suggestion of the Commission.

The purpose of this confrontation is to co-ordinate economic policy for 1965; its results can be—and certainly should be—taken into account, especially in preparing government budget proposals for 1965.

In addition, there are the preliminary forecasts produced by the staff of the Commission, which from a very early stage include the outlook for the coming year.

Lastly, mention should be made of the very welcome fact that preliminary forecasts are now also being prepared in the OECD, on essentially the same simple lines as the EEC's preliminary economic budgets. True, this is not done by the OECD member countries until the autumn, for the coming year, but the OECD Secretariat begins earlier, in April/May, to work out its own preliminary forecasts, which are discussed with the experts of the OECD member countries at a meeting, held in May, also attended by experts from the EEC Commission. This has the great advantage of giving an early and more reliable idea of the probable development of the world economic situation.

The results of all these investigations give much support to the assumption that world economic conditions will continue to be characterized in 1965, or at least in the first half of the year, by pronounced expansionary trends, although the pace of the expansion might be somewhat slower than in 1964. Most experts think it unlikely that next year will see any appreciable slackening of the rising trend of activity in the United States, especially as the effects of the tax reduction will continue into 1965, while at the

same time the expansion of demand will be supported by the stimuli to employment and consumption. The economic prospects for the United Kingdom also definitely point to further expansion; it is not inconceivable, however, that the internal strains in that country may become so acute as to produce stronger effects on the balance of payments and thus necessitate the pursuit of a policy designed to impose a sharper restraint on economic growth. Similar problems may also arise for some other industrial countries, but on the whole the expansion will again be considerable, at least on a year-to-year basis. Lastly, there would appear to be no reasons to suggest the likelihood of any appreciable slackening in the imports of the developing countries from the industrial countries in 1965.

In these circumstances, there might well be a further considerable growth in the Community's exports to non-member countries, although probably at a somewhat slower pace than in 1963. The rate of growth depends firstly on the extent to which advantage can be taken of these opportunities, in view of the recent relatively marked cost increases in some member countries (Italy, France, the Netherlands), and secondly on whether in the Federal Republic—which, on the other hand, appears to enjoy some cost advantages—exports are not at all hampered physically by reduced elasticity of supply.

With regard to internal demand within the Community, there can be little doubt that the expansion will continue. It will be particularly pronounced in the Federal Republic of Germany, where the investment boom might continue and also probably lead increasingly to a further growth in consumption. In most of the other member countries, on the other hand, the tendencies towards a slowing-down of the expansion in internal demand are likely to continue, at least in the early months of the year. Nevertheless, the underlying forces of expansion still appear to be very powerful, with the reciprocal action between the growth demand and the labour shortage both lending support to the growth in consumer incomes and stimulating capital investment. Indeed, there might even be a fairly distinct revival of capital investment by business in France.

In any case there still appears to be a danger that—compared with what is required for price stabilization and the restriction of external equilibrium—consumer expenditure, in particular, will remain too high and the increase in costs will be too marked in France, the Netherlands and Italy, although these forces making for disequilibrium should become less powerful. The position in the Federal Republic will probably be characterized by an increasing "overheating" of the economy. It cannot be expected that these dangers will be removed by internal supply—and in the Federal Republic imports are not likely to help either, particularly if and in so far as the extremely high degree of agricultural protection is maintained.

With regard to internal supply, it is at present thought—on the basis of the trends of demand described above and the effects of the competitive position and in view of the physical limits to growth—that an increase of 4.5 % in the real gross Community product from 1964 to 1965 is by no means beyond the bounds of possibility.

These prospects, assumptions and trends can be substantially influenced, and in many respects improved, by the economic policy pursued, individually and jointly, by the member countries. It is obvious that the forecasts which have just been briefly outlined clearly indicate that the recommendations of the Council of Ministers should also be implemented for 1965. If there were to be a complete reversal of the economic situation—and nothing is impossible in the field of economic affairs—there would be no difficulty at all in quickly adjusting the economic policy to the changed conditions. This would be all the easier in view of the fact that the stabilization policy consists essentially in a curbing—or postponement—of pressing demands, the satisfaction of which can if necessary quickly be accelerated again.

It is therefore strongly advisable for countries to continue in 1965 to observe the rules of economic policy laid down by the Council—that is, they should preferably adopt forthwith all the policy decisions necessary for their implementation and avoid taking any action which might run counter not only to the letter but also to the underlying economic aims of the Council's recommendations. The latter point applies, for example, to the policies pursued by the Federal Republic and the Netherlands with regard to taxation and transfer payments, and to Italy with regard to the growing tendency to restrict imports.

Despite their very uniform nature—or rather precisely because of it—the recommendations of the Council of Ministers are exactly appropriate to the differing situations and diverse stabilization requirements of the individual member countries. For compliance with these rules calls for the most arduous efforts on the part of the countries which are furthest from equilibrium, while the same rules can be relatively easily followed, in other words are much less drastic in their effects, in the cases where there is a better balance, since they are only designed to prevent the emergence of inflationary dangers. All in all, the recommendations by no means call for a deflationary policy, but only for a “disinflationary” policy.

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



## A. Federal Republic of Germany

*The speeding-up of the hitherto relatively moderate expansion in economic activity which was observable in the closing months of last year was perceptibly accentuated at the beginning of 1964 and during the spring months.*

*The main direct contribution again came from external demand, but the indirect effects of the pronounced export boom were also increasingly reflected in a distinctly greater readiness on the part of businessmen to undertake capital expenditure. Thus the continued marked expansion of investment in building and construction was again coupled with an appreciably faster rise in expenditure on equipment. The rate of growth of public consumption would appear to have remained unchanged. Although the overall upward movement of wage agreements was still fairly steady, private consumption expenditure rose somewhat more quickly than in the preceding quarters, owing to a rather faster increase in earnings.*

*The general quickening of the rise in overall demand led to a marked expansion in internal supply. The year-to-year rate of growth in industrial production rose—according to the Federal Statistical Office's index of output per working day—from 5.3 % in the last quarter of 1963 to 11.4 % in the first quarter, although it must be borne in mind in this connection that the level of production in the first quarter of 1963 was adversely affected by special influences. There was also, however, a pronounced increase in commercial imports. Prices continued to rise slightly.*

*The balance of current transactions with other countries showed a surplus of DM 2 110 million in the first quarter. The trade balance alone actually yielded a surplus of DM 2 380 million. The gold and foreign exchange reserves of the banking system (the Bundesbank and the commercial banks) increased by DM 2 230 million.*

*The upward trend of activity is likely to become more rapid during the remainder of this year and on into 1965, with the result that the tensions between demand and supply will become more acute.*

*There will be no slackening for the time being in the strong pressure of export demand; this is evident particularly from the continued large inflow of foreign orders and the further increase in orders on hand. The favourable state of the market and the resultant expectation of rising profits will also make businessmen even more ready to incur capital expenditure, so that there should in the immediate future be an appreciable further quickening in the rate of gross fixed asset formation. Public consumption will go on expanding rapidly, especially since, in addition to the general*

*rise in expenditure, there is also likely to be an increase this year in the salaries of public officials. Assuming an unchanged savings ratio, the upward trend of private consumer expenditure should become appreciably faster towards the beginning of the autumn and up to the end of the year, when the expiry of the collective agreements in important sectors of the economy will lead to further, probably quite considerable wage increases.*

*Although there is not likely to be any notable increase in the total of man-hours worked, industrial production will for a time continue to expand vigorously. As the physical reserves of production capacity become increasingly depleted, however, an appreciable reduction in the elasticity of internal supply may gradually set in, possibly during the second half of 1964 and in any case in 1965. Although this will push up imports faster, it seems unlikely, as things are at present, that the increase in imports will be large enough to prevent a further—although slower—growth in the surplus in respect of current transactions with other countries.*

*In these circumstances, the rise in prices—which will probably prove to have been more rapid in 1964 than was at first foreseeable—will tend to become even quicker in 1965, especially as the rise in costs per unit of output is likely to be greater in that year than in 1963 or 1964. It is obvious that these trends must be countered by an economic policy more specifically designed than hitherto to improve the relationship between overall demand in monetary terms and total real supply. The Federal Government has announced new measures to this end.*

## **1. Recent developments**

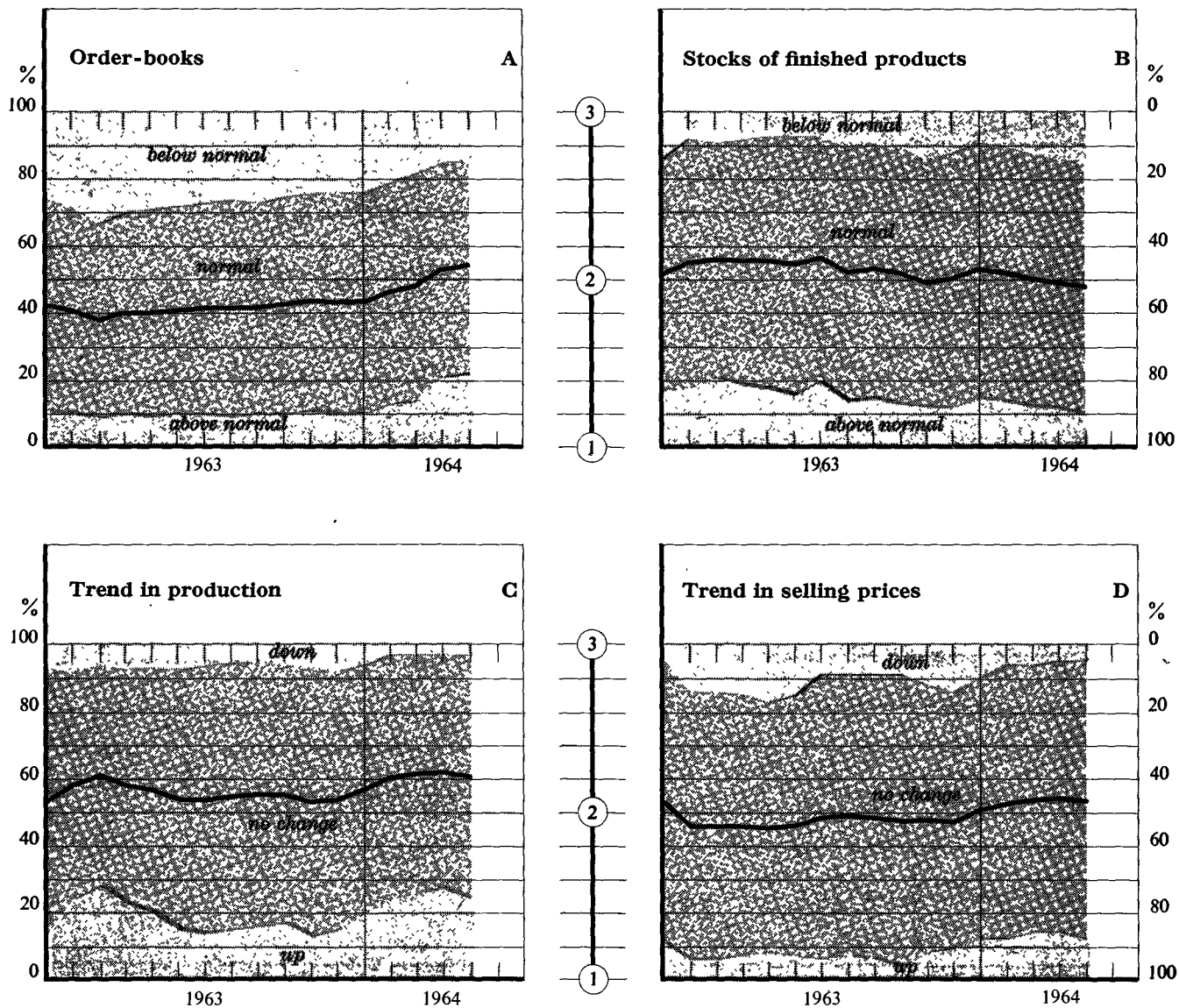
Exports of goods and services expanded faster in the early months of 1964. According to customs returns, visible exports in the first quarter were about 21 % up on the year in both value and volume, compared with corresponding rises of about 15 % and 16.5 %, respectively, in the fourth quarter of 1963. The increase in the year-to-year growth rates was indeed partly due to the fact that the level of exports in the first quarter of 1963 was depressed by special factors (the very hard winter and the dock strike in the United States); but even so these rates clearly reflect the marked upward trend of foreign orders since the middle of 1963. In April exports were 16.9 % higher than in April 1963.

Domestic demand, too, showed clearer signs of a faster rise in recent months. There was a brisker general increase in gross fixed asset formation. Expenditure on plant and equipment rose more quickly than last year, largely owing to the strong pressure from



Federal Republic of Germany

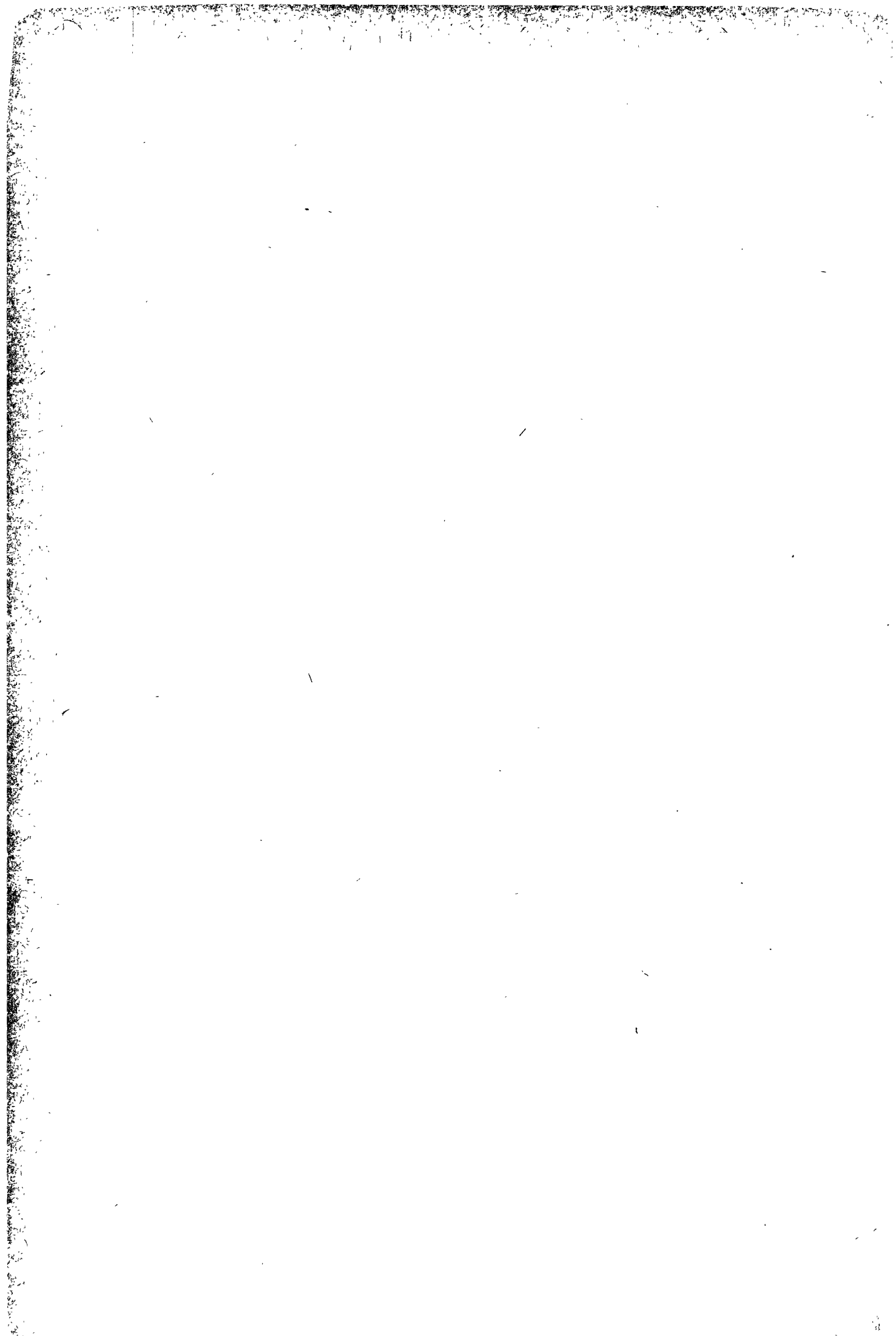
BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to questions of the EEC business survey, carried out in the German Federal Republic by the IFO-Institut.

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

- by 0.03 for the answer "above normal", or "up";
- by 0.02 for the answer "normal", or "no change";
- by 0.01 for the answer "below normal", or "down".



exports and the resultant marked improvement in conditions for capital investment. Investment in building and construction continued to show a vigorous expansive trend.

With regard to stockbuilding, the tendency to build up stocks of raw materials and semi-finished goods continued unabated. This is indicated by the further sharp increases in iron and steel production in recent months and also by the movement of raw material imports, both of which rose much faster during this period than did the output of the processing industries. This may no longer have been attributable solely to price speculation but was now also, and to a growing extent, due to expectations of further growth in production. Commercial stocks of finished goods probably also expanded again.

There was a further distinct rise in public consumption. In addition to the general growth in expenditure, there was also an increase of 2 % from 1 April in the remuneration of wage-earners and salaried employees in the public service. Most important, however, private consumers' expenditure has recently been rising faster than in the preceding quarters. Thus, retail turnover in the first quarter was up by 7.3 % in value and 6.0 % in volume compared with the corresponding period of last year (the rises in the fourth quarter of 1963 were 4.4 % and 1.8 % respectively).

These figures do not, however, reflect any marked quickening of the basic rate of expansion of private consumption. The year-to-year rate of growth for the first quarter in fact exaggerated real trends, since it was inflated through the loss of earnings early last year due to the severe cold on the one hand and by the fact that Easter fell early this year on the other; in April the rate fell back to 3.4 % (value) and 2.2 % (volume). Actually there has been little change from the previous tendency towards a slowing-down of the rise in agreed wages; in the first quarter the level of agreed wages in the economy as a whole was 4.4 % higher than in the corresponding quarter of 1963, after a year-to-year rise of 4.8 % in the fourth quarter of 1963. There has, however, been another rather sharper increase in earnings. Allowing for the growth in the number of persons in paid employment and the substantial rise in transfer incomes (notably the increase of 9.2 % in existing old-age pensions and of 8.2 % in new ones, and the rise in pensions to war victims), net mass income was probably about 11 % greater in the first quarter than in the corresponding period of 1963.

There was no easing of the strains in the labour market in the first quarter; on the contrary, there were once again signs of increased tension. In April the ratio between the number of vacancies and the number of unemployed was 4.2, against 3.9 in April 1963. At the end of April 1964, the number of unemployed was only 146 000, or 0.6 % of the potential labour force.

The growth in foreign demand, which has been accelerating for some time now, and the more recent stronger upsurge of domestic demand led, in the first place, to a substantial expansion of domestic supply. According to the Federal Statistical Office's

index of production per working day, industrial output in the first quarter was 11.4 % above its level in the corresponding period of last year (in the fourth quarter of 1963 it was up by 5.3 %). This rise doubtless reflected not only the effect on the year-to-year growth rates of the bad weather at the beginning of last year, but also a faster basic upward trend. This probably applies particularly to the capital goods sector. The fact that the year-to-year growth rate fell back to 4.3 % in April does not necessarily contradict this assessment, since this is a single-month comparison which may be distorted by statistical or other special factors.

Imports of goods and services rose faster than in the preceding quarter. According to the customs returns, visible imports in the first quarter were 8.4 % up on last year in value and 7.5 % by volume (against corresponding rises of 1.8 % and 3.0 % in the fourth quarter of 1963). It should, however, be borne in mind that the development of imports, too, was hampered in the early months of 1963 by the special factors already mentioned in connection with exports. Even so, a distinct acceleration of the upward trend is also observable in the case of imports, especially industrial imports of basic materials. The value of total imports in April was 11.4 % up on the year.

The general level of prices again showed a slight tendency to move upwards in the first quarter, especially if no account is taken of declines in prices for farm products which were either seasonal or represented a corrective adjustment in relation to the exceptionally high prices caused by the bad weather a year earlier. In the industrial sector, producers' prices in April were 1.2 % higher than in April 1963. This was probably attributable in part to the increase in the cost of raw material imports. In the building and construction sector, although there was temporarily a slight slackening of the price rise, the house-building price index in February was still 4.6 % up on the year. Consumer prices continued to move gently upwards, and in April were 1.6 % above their corresponding 1963 level.

The balance of goods and services account with foreign countries closed in the first quarter with a surplus of DM 2 110 million, against one of DM 2 790 million in the preceding quarter and one DM 750 million in the first quarter of 1963. The year-to-year rise is entirely due to the development of the balance of trade, the trade surplus, which at DM 2 380 million, was more than three times as great as in the corresponding period of 1963. It is worthy of note that the recent growth in the trade surplus is no longer primarily attributable to the development of trade with other Community countries, but is in all cases due to improvements in relation to all trade partners. On the other hand, there was a further deterioration in the balance of services. The deficit in respect of unrequited deliveries and remittances, at DM 815 million, was also rather larger than in the preceding quarter.

With regard to the balance on capital account (including errors and omissions but excluding changes in the foreign currency position of the commercial banks), there was a net capital inflow of DM 933 million in the first quarter, against a net outflow of about

DM 3 300 million in the fourth quarter of 1963 which had been mainly due to exceptionally large government payments to foreign countries. Altogether, therefore, the overall balance of payments showed a surplus of about DM 2 230 million. Almost the whole of this was reflected in an improvement in the net foreign currency position of the commercial banks, the official gold and foreign exchange reserves having increased during that period by only DM 8 million. In April, however, as a result of the measures taken by the Bundesbank and in particular of the announcement of the new capital yields tax on income from fixed-interest-bearing securities held by non-residents, there was a net capital outflow—a development which had already been foreshadowed in March.

Although the cash transactions of the public authorities—especially owing to seasonal influences and taking into account government payments abroad—had, if anything, a tightening effect on liquidity, bank liquidity tended to become more plentiful in the first quarter. In fact, the large balance-of-payments surpluses again added to bank liquidity during this period.

There was a further growth in bank credit to trade and industry. In the first quarter the rate of expansion fell off slightly, however, not only in the case of medium and long-term lending, but also in the case of short-term credit, this being probably due in part to the appreciable improvement—mainly owing to the large surpluses in respect of current foreign transactions—in the self-financing capacity of trade and industry. However, in the following months short-term credit to commerce and industry staged an unmistakable recovery. Credit-granting to public authorities, again increased substantially.

## 2. Outlook

The pace of the expansion in economic activity will undoubtedly quicken again during the rest of the year. One of the consequences of the lasting boom in foreign demand will be that domestic demand will increasingly become the main component of the overall growth in demand.

External demand should continue to make an important contribution to the business expansion. Firstly, the German economy's competitive position has been improved by the marked upward movement of prices and costs in leading importing countries. Secondly, owing to the present upsurge of world economic activity, demand for German products, especially capital goods, should increase. These prospects are clearly confirmed by the trend of foreign orders received by industry: in the first quarter, the volume of new orders from abroad was about 22 % up on the year and 9 % above the current rate of export sales (corresponding rises in the fourth quarter of 1963, 23.0 % and

7.3 %). The increase in orders on hand is also reflected in the results of the EEC Business Survey; whereas at the end of 1963 only 18 % of the heads of industrial enterprises questioned described their foreign order books as relatively large, by April the proportion giving this answer had risen to 27 % (end of March 1963: 8 %).

Gross fixed asset formation is likely to increase appreciably faster than hitherto, since there has recently been a further general improvement in capital-investment conditions in the economy, largely owing to the favourable state of the markets and the resultant improvement in the outlook for business profits. The rate of expenditure on capital equipment, in particular, should now become more rapid. This belief is strongly supported by the trend of new domestic orders received by the capital goods industries; in the engineering industries new domestic orders in the first quarter were more than 29 % above their level for the corresponding period of last year and, for the first time in quite a long period, above the current level of deliveries—actually by no less than 17 % (corresponding figures for the fourth quarter of 1963, 20 % and—6 %). It should be noted in this connection that, in addition to rationalization schemes, more plans are now being made again for the extension of plan. This is also reflected in the trend of industrial construction plans: the volume of orders for industrial and commercial building in the first quarter was almost 19 % up on the year (in the fourth quarter of 1963 it was still 2.0 % down).

Activity will also continue to be strongly stimulated by the expansion of expenditure on other kinds of building, especially public construction projects. This applies both to construction for transport purposes and to public building—sectors where there is not only already a large volume of outstanding orders, but where new orders will also continue to show an upward trend. The licences granted for the erection of public buildings in the first half of the year (measured by cubic feet enclosed) were 15.7 % up on the corresponding figure for the previous year (rise in the fourth quarter, 9.3 %). On the other hand, there was again only a very slight increase in the number of housing permits issued. In this sector, however, the backlog is still very large, and demand will continue to exceed the output possible with the available building capacity.

Public consumption is likely to continue to rise very rapidly. The increase will in fact become even faster, as there is going to be a substantial rise in public officials' salaries from 1 October of this year. In addition, the remuneration of wage-earners and salaried employees in the public service will also be raised again from 1 October.

The growth of private consumption, on the other hand, will generally continue at a fairly steady rate, at least for a while, as it is not likely to benefit from any major stimuli from incomes for the time being, and as the savings ratio is at any rate not likely to decrease.

The strain on the labour market is indeed likely to become greater owing to the quickening tempo of economic activity, and this can be expected to widen the divergence between actual earnings and agreed wages. Larger wage claims and rises leading to

substantial and widespread increases in earned incomes may, however, be delayed until towards the end of the year, when the collective agreements are due to be renewed in major economic sectors.

Agricultural production should advance slightly, given normal weather conditions. Industrial output will be able to maintain its present high rate of expansion only in so far as its elasticity has not already been reduced by the increasingly full employment of productive capacities and the growing labour shortage.

The rise in imports is likely to quicken somewhat, because the gap between overall demand and domestic supply will probably widen during the year, and because there might be a further rise in non-commercial imports (government purchases).

The price level will probably gradually begin to rise rather faster again, mainly because the discrepancies between demand and possible supply will become more marked in an increasing number of fields. This applies particularly to the building sector, where a further sharp acceleration of the price rise must be expected in the near future.

As the growth in imports of goods and services will still not be as great as the overall expansion in exports, there is likely to be a further increase in the surplus in respect of current transactions with foreign countries.

*Supply and utilization of goods and services*

	1962 <sup>(2)</sup>	1962 <sup>(2)</sup>	1963 <sup>(2)</sup>	1964 <sup>(3)</sup>
	At current prices (in DM '000 million)	% variation by volume on preceding year		
Gross national product	354.8	4.2	3.2	5.5
Imports <sup>(1)</sup>	65.3	11.4	8.3	6.5
Private consumption	203.8	5.8	2.7	3.5
Public consumption	52.9	11.9	6.3	5
Gross fixed asset formation	90.0	5.5	1.8	7.5
Exports <sup>(1)</sup>	68.9	4.2	9.8	10

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> *Wirtschaft und Statistik*, January 1964.

<sup>(3)</sup> Commission forecasts.

*Note* : The forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts from the member countries but are established and published on the Commission's sole responsibility.

These prospects mean that the forecasts of the real development of the main components of demand and supply for the whole for 1964 as compared with 1963 which were published in Quarterly Survey No. 1/1964 still largely hold good. There might be certain changes with regard to the development in monetary terms, in that the price rise might prove somewhat greater than was originally foreseeable.

In so far as anything can yet be said with any degree of certainty about the economic trend beyond the end of 1964, the prospects point to the possibility of a further aggravation of the existing strains. There will only be a slight slackening in the export expansion, especially as the growing backlog of orders is itself sufficient to ensure continuation of the expansion.

More or less the same is true of capital investment, in which there might be a virtual boom. Private consumers' expenditure, too, is likely to rise faster, as there will almost certainly be considerably larger wage increases than hitherto.

Domestic supply should go on expanding briskly in 1965, but the rate of growth will undoubtedly be affected more and more by the decrease in the physical elasticity of production. The Commission's staff, as a first very rough forecast, put the year-to-year increase in the real gross national product from 1964 to 1965 at about 5 %. Imports will rise further, and at a faster pace. Owing, however, to the differences between domestic and foreign prices, and also to certain time-lags which have been found to occur, the rise in imports will probably still be smaller than the rise in exports, even though the latter may be somewhat slower than before. The "external contribution", (i.e. the surplus in respect of current transactions in terms of the national accounts), is therefore likely, if anything, to increase still further. This being so, it is obvious that the upward price trends will at the same time be accentuated.

The present economic situation and the prospects for the future have caused the Federal Government and the Bundesbank in the first place to adopt measures designed to reduce the surpluses in respect of capital movements: firstly, with effect from 1 April the minimum reserve ratios for liabilities to non-residents, which up to then had been subject to the same reserve ratios as domestic liabilities (between 5 and 13 % depending on the banking centre and reserve category in question), were raised to the maximum legally permissible levels (between 10 and 30 %); and, secondly, it was at the same time decided to forbid the allowing of interest on non-residents' time deposits. The payment of interest on non-residents' sight deposits was discontinued some time ago. In addition, at the beginning of March the Bundesbank resumed the practice of giving an exchange guarantee for the commercial banks' deposits of funds in the United States (the "swap rate policy").

Furthermore, a bill approved by the Federal Cabinet, proposing the introduction of a capital yield tax of 25 % on future interest earnings on certain domestic fixed-interest-



bearing securities now held or henceforth acquired by non-residents, is also intended to curb the heavy capital inflow and stimulate the export of capital. This law, which is to come into force on 1 July, also provides for the removal of the securities tax (of 2.5 %) hitherto applied to security issues (except for German public loans) on the German capital markets.

These measures are undoubtedly in line with the recommendations issued by the Council of Ministers of the Community on 14 April 1964. But it is obvious—and the need for this is confirmed by the latest forecasts—that the competent authorities of the Federal Republic will have to adopt further measures, especially ones aimed at reducing the surplus in respect of current transactions with foreign countries.

On 14 May 1964 the Federal Government did in fact announce far-reaching reductions in customs duties. According to the revised version of 5 June, the remaining German intra-Community customs duties on industrial goods and a few agricultural products are to be lowered to half their present levels with effect from 1 July 1964. These reductions in intra-Community duties anticipate cuts which were in any case due to be made—in the absence of any further acceleration—in two equal stages (each of 10 % out of the current rate of 40 %) on 1 January 1965 and 1 January 1966 respectively. With regard to duties in relation to non-member countries, it is planned to reduce those on industrial goods for which the present rates of duty are higher than the Common External Tariff to the level of the External Tariff, again with effect from 1 July 1964. This in turn entails, for a few items, a corresponding additional lowering of the intra-Community rates of duty.

These measures, too, are undoubtedly in accordance with the Council's recommendations of 14 April 1964. The extent of their effects should not, however, be over-estimated; an immediate complete removal of the internal customs duties would probably have been more appropriate in view of the German surplus position. It is, however, not even certain yet that the Bundestag will approve the moderate proposals for tariff cuts. It should also be pointed out that one recommendation of the Council of Ministers was "to facilitate imports of agricultural products by all suitable measures". Although a really far-reaching effect could have been produced in this sector by reducing the degree of protection also in relation to non-member countries—which would immediately have helped to hold down the domestic price level—the authorities still appear to be very hesitant about taking steps in this direction. So far, only a few agricultural products, of little importance, are to be included in the operation to cut tariffs.

In so far as the German deficit position is due to the development of intra-Community transactions in the past two years—and this is largely the case—there are also other remedies. One is effective action in the other member countries to combat the inflationary trend which has created the strong demand for imports from the Federal

Republic—and it can be said that in this respect measures with every prospect of success have already been adopted and tendencies towards a better balance have become observable. Furthermore, the Federal Republic itself—justifiably in view of this policy in the other member countries—can in fact do much more to worsen the trend of its balance of current transactions with the “rest of the Community”. It would seem important to ensure, in so doing, that a still stronger influence is exerted not only from the import side—especially, now, in the case of agricultural imports—but also, in the opposite direction, on the export side: all measures, regulations and practices tending to promote exports should be discontinued or avoided.

The new surplus position should not deter the Federal Republic from doing everything possible to prevent its effects from being reinforced by a vigorous upsurge of internal demand, the main result of which would be to cause a further acceleration of the price rises—especially in those markets such as the building market, where imports can have little effect.

The Council’s recommendations emphasized the importance, as an instrument of economic policy, of taking a stricter line with regard to public expenditure. This should be heeded now, in 1964. Although the Federal Government and the Bundestag endeavoured, when approving the Federal budget for 1964, to limit the growth in expenditure to the percentage increase in the gross national product in monetary terms, it has not yet been found possible to prevent the total of the public cash outlays which affect the domestic economy from appreciably exceeding the recommended year-to-year increase of 5 %. Indeed, the deficits are still tending to rise. A sharper general curb on the rate of growth of public expenditure therefore remains desirable. A particularly appropriate step in this direction would be a more pronounced reduction in public outlays which directly or indirectly influence the building markets.

For 1965 the Federal Government has in fact decided to limit the expansion in Federal expenditures affecting internal demand to 5 %, in accordance with the Council’s recommendation. The Federal Länder have been called upon to keep their own public disbursements below the same growth ceiling. However, from 1 January 1965 a substantial income tax cut will become operative.

Lastly, it should be noted that in the present circumstances dangers are also likely to arise as a result of the probable development of capital expenditure by business enterprises. The rise in such expenditure should be restrained as much as possible, firstly by tax measures and secondly by credit policy. With regard to the latter, one possible line of action would perhaps be to fix suitably low ceilings to the expansion of bank credit, along the lines of the practice adopted in the Netherlands and France. This might also under certain conditions produce an effect on the balance of payments, in so far as the banks, which, as a result of the surpluses on current transactions, acquire a large amount

of liquidity which they cannot fully utilize within the country, make use of it for foreign lending. Should the efforts to moderate the expected upsurge of capital expenditure be unsuccessful, this would be likely to lead not only to a further wave of inflationary pressure in the domestic economy but also, in the longer run, to an increased lop-sidedness of the German industrial structure in the direction of exports, as it is mainly the export industries that are undertaking capital investment. This, however, would without doubt greatly increase the danger of a long-term structural disequilibrium of the balance of payments.

### 3. The economic situation in West Berlin

With a certain time-lag by comparison with developments in the territory of the Federal Republic, economic activity in West Berlin has also recently been expanding more rapidly.

In particular, foreign demand is now again giving a stronger stimulus to economic growth. In the first three months of 1964 the value of exports to foreign countries, which in the same quarter of 1963 was only slightly up on the year, was about 12 % higher than in the corresponding period of the previous year. Deliveries to the territory of the Federal Republic also increased substantially, their value in the first quarter having been 11 % greater than it was a year earlier (the corresponding rate of increase in the fourth quarter of 1963 was 3.6 %).

The expansion in gross fixed asset formation would appear to have appreciably quickened, chiefly owing to the vigorous rise in investment in building and construction. Private consumers' expenditure also showed a distinct increase. In the first three months the value of retail trade turnover was 8.7 % above the level for the corresponding period of 1963 (fourth quarter : + 5.4 %).

Despite continued strains in the labour market, the supply of labour showed considerable elasticity. The growth in industrial production in the first quarter in relation to the same quarter of the previous year amounted to nearly 6 %, after having been only just 2 % up on the year in the fourth quarter of 1963.

As deliveries to the territory of the Federal Republic increased much faster in the first quarter than purchases (+ 8.5 %), there was a distinct improvement in the balance of visible trade with the territory of the Federal Republic, which yielded a surplus of DM 25 million, compared with a deficit of DM 23 million in the first quarter of 1963 and one of DM 80 million in the fourth quarter of 1963.

Consumer prices have again risen slightly in recent months. In April the cost-of-living index was 2.4 % above its April 1963 level.

The outlook for the economy of West Berlin up to the end of the year is one of continued expansion. New industrial orders are showing a marked upward trend, having been 14.5 % up on the year in the first quarter. It is worthy of note in this connection that it is precisely in the capital goods industries that the inflow of new orders has recently shown a marked acceleration; in the first quarter it was about 10 % up on the year, and exceeded sales by 8 %. From the demand side, therefore, conditions are favourable for continued economic growth. In view of the fact that West Berlin's reserves of labour are now largely exhausted, the size of the increase in production will mainly depend on the extent to which the West Berlin economy is able to attract further workers from outside and to increase productivity by capital expenditure on rationalization.

## B. France

*The slight lull in the expansion of demand, which had already set in at the end of last year, continued during the first months of 1964.*

*External demand again increased substantially—and in fact at a somewhat higher rate—but the development of internal demand was clearly influenced, both directly and indirectly, by the stabilization programme which the Government introduced on 12 September 1963, and which has since then been progressively extended and tightened up. Although overall investment expenditure continued to develop at a fairly brisk pace, there was a tendency for private firms to hold back, and some programmes of public expenditure were temporarily suspended. The expansion of private consumers' expenditure was also somewhat less marked.*

*The slight easing in the expansion of demand has not yet had any very noticeable effect on the rate of actual economic growth. Supply continued to increase substantially. Between the first quarter of 1963 and the first quarter of 1964 industrial production—according to the seasonally adjusted INSEE index, rose by 1.6 %, and imports again increased.*

*It is difficult to gauge accurately from the trend of prices to what extent the strains in the demand|supply relationship have actually eased, since prices continue to be influenced by governmental controls. Nevertheless, the upward tendency of prices still seems to have been appreciable, although less powerful than in the autumn of 1963.*

*Thanks to the marked increase in exports, there was no further increase in the deficit on the trade balance in the first four months of the year, but the overall balance on current transactions with foreign countries seems likely to show a deficit. The surplus on the overall balance of payments was still small. Between the end of December 1963 and the end of April 1964, the official gold and foreign currency reserves increased by only \$76 million, compared with \$440 million in the corresponding period of last year.*

*In the coming months the expansion of demand is likely to continue at approximately the same rate. The strongest spur will probably be given by exports. At all events, foreign orders have shown a marked improvement recently, and the volume of outstanding foreign orders has increased. In view of current economic policy, it can scarcely be expected that this will lead to any appreciable reactivation of private investment in the near future, but expenditure by the public undertakings*

*and by the government on capital investment will certainly show a substantial increase. Demand will continue to rise strongly in the field of housing. Finally, private consumption, sustained by a continued though probably more moderate increase in incomes, will also continue to rise.*

*The probable development of overall demand should be sufficient to ensure continued effective economic growth. There is unlikely to be more than a slight decline in the expansion of imports, so that the balance of current transactions may well continue to show a deficit. Prices should be relatively steady, particularly in view of the continued decisive influence of government controls.*

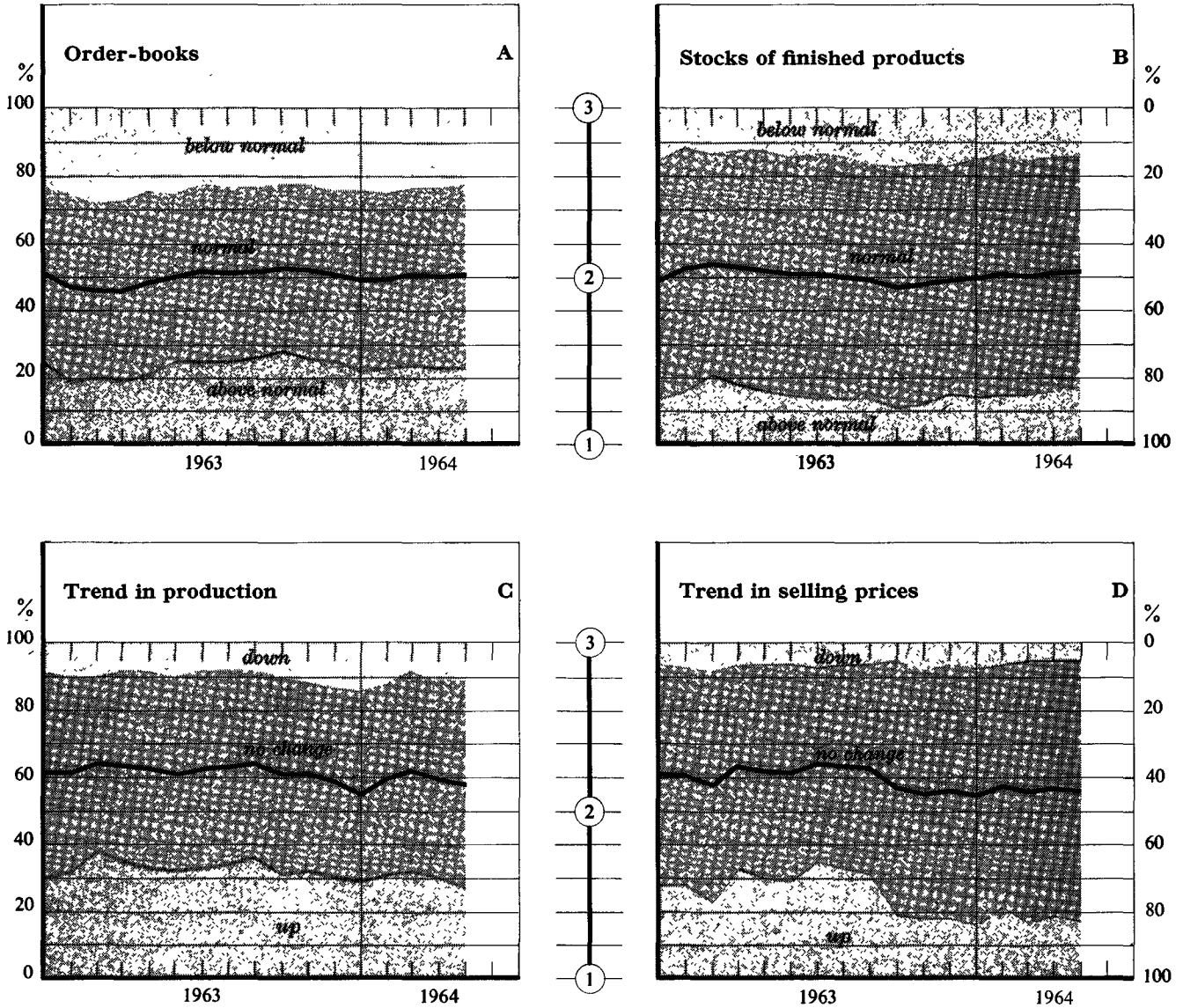
*Any attempt to forecast the further course of the economy for the end of 1964 and for the year 1965 is still hedged about by elements of some uncertainty, due mainly to the impossibility of forecasting the decisions of business managements in regard to investment, and to the attitude of the parties in the wage negotiations due to take place in the autumn. In some important sectors of demand, however, expansion seems almost certain to continue. On the other hand, the tendency towards a better equilibrium seems likely to persist, if the authorities pursue the existing policy of stabilization and intensify it at certain points, particularly in the field of budgetary policy.*

## **1. Recent developments**

Among the various elements making up total demand, external demand has shown the most marked increase during the last few months. The export of goods and services, which—apart from normal seasonal variations—had increased quite substantially in the fourth quarter of 1963, continued to rise at the beginning of 1964 and even rose at a slightly more rapid rate. The export of goods in the first quarter of 1964, according to the customs returns, was 19.4 % higher in value and about 14 % higher by volume than in the corresponding period of last year. Although this high rate of increase is partly a reflection of the handicaps imposed by the exceptional weather conditions in the first quarter of 1963, it still denotes a trend towards faster expansion, which continued in April.

On the other hand, the increase in internal demand in recent months has been somewhat less marked. The development of gross fixed asset formation has continued to be affected by a certain hesitation on the part of business managements, particularly in industry, which have taken a very cautious view of future sales possibilities and are

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

- by 0.03 for the answer "above normal", or "up";
- by 0.02 for the answer "normal", or "no change";
- by 0.01 for the answer "below normal", or "down".





faced with greater financing difficulties, as profit margins are under a certain degree of pressure owing to the continued, though less marked, rise in wages and the freezing of domestic prices. In addition, certain investment programmes planned by the public undertakings and by the Government were still frozen, and this may have checked not only the placing of new orders, but also the increase in actual expenditure in this sphere, although the latter was still very substantial. On the other hand, expenditure on housing probably increased at virtually the same rate, particularly as the clearance of the backlog of building orders from the previous year and the commencement of new projects were favoured by the exceptionally mild weather at the beginning of 1964.

Investments in stocks do not appear to have given rise to any particularly expansionary influences. For reasons of liquidity, trade and industry have undoubtedly been trying to restrict their stocks of raw materials. In addition, stocks of finished goods have been kept very low, although it is not unlikely that they may have risen again slightly in some sectors, particularly as sales have not always lived up to expectations, especially in regard to certain consumer goods.

There was a further heavy increase in public current expenditure on goods and services in the first months of the year—particularly in respect of salaries, as a result of commitments entered into previously—but the rise in private consumers' expenditure has slowed down a little since last autumn. In fact, between the fourth quarter of 1963 and the first quarter of 1964, the turnover of the Paris department stores fell rather more than is normal at this time of year. But other sections of retail trade achieved a more satisfactory turnover in the early months of the year. Moreover, it appears that a relatively larger share of expenditure went on travel and other services and the purchase of motor vehicles, probably because Easter fell early. There seems, however, to have been a slight overall increase in consumer savings.

The trend of personal incomes made little contribution to slowing down the expansion in private consumption. The slight slackening in the increase of income from salaries and wages, which had been observable in the fourth quarter of 1963, did not continue. In private trade and industry, hourly wages rose by a good 1.9 % in the first quarter of 1964, compared with only 1.5 % in the last three months of 1963; on 1 April the wage level was 8 % higher than at the corresponding time last year. Taking into account the higher rates of pay which took effect on 1 January and 1 April in public undertakings and the public service, together with the increase in certain social payments and the further rise in the volume of employment, it can be assumed that total incomes at the beginning of April 1964 had risen by at least 10 % by comparison with the previous year.

The slight easing of the expansion of demand has not yet had any very appreciable effect on the rate of growth of effective supply.

Thanks to mild weather, agricultural production reached a relatively high level for this time of year.

The upward movement of industrial production continued at a pace which, although quieter than that of the autumn of 1963, was quite as vigorous as that of the year 1962, for example. Between the fourth quarter of 1963 and the first quarter of 1964, the seasonally adjusted INSEE index rose by 1.6 %; the gross index exceeded the previous year's level by approximately 13.5 %, although the latter had, of course, been seriously affected by the hard winter and the strikes. In the individual branches of industry, the upward trends which had prevailed at the end of 1963 continued almost unchanged: in the basic industries, particularly iron and steel production, the improvement gathered further momentum. In the field of consumer goods, particularly motor vehicles, textiles and clothing, a slower trend began to emerge. In the investment goods industries there was further moderate growth, with some signs of slightly more lively activity. In the building industry, there was a further very substantial increase in production for the first quarter of 1964 owing to the considerable enlargement of capacity in the previous year and the exceptionally favourable weather conditions.

The increase in domestic production in the first quarter of 1964 was due partly to improvements in productivity but mainly to a further increase in employment. While there was practically no change in the number of hours worked, the number of persons in paid employment, which had already increased very substantially (by 0.8 %) in the last three months of 1963, rose again between 1 January and 1 April 1964. The total volume of employment <sup>(1)</sup> was about 2 % higher than a year ago. It was clearly easier to find suitable labour—due in no small measure to the further substantial flow of immigration. The number of vacancies declined slightly during the last few months, while the number of persons seeking employment increased very slightly. This may mark the beginning of a certain easing in the labour situation, although there is no question at present of any radical change.

Imports of goods and services again contributed substantially to the increase in overall supply. There was only a slight falling-off in the rapid rate of expansion. The flow of imports of consumer goods continued to be particularly strong, but there was also a surprisingly rapid increase in imports of investment goods in the last few months. Total imports of goods in the first quarter of 1964—according to the customs returns—were approximately 26 % higher by volume (26.7 % in value) than in the corresponding period of last year, which was, however, greatly affected by the unfavourable weather conditions. In April, too, the rate of increase was very high.

It is difficult to gauge accurately from the trend of prices to what extent the strains in the demand/supply relationship have actually eased in the last few months, since prices

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(1) Number of persons in paid employment multiplied by the average number of hours worked per employee.

continue to be influenced very largely by government controls. It is true that, as far as manufacturers' prices are concerned, there was a growing tendency to pass on increased raw material costs to the consumer—generally with official approval—which resulted in a perceptible rise in retail prices of textiles and clothing, for instance. The upward movement of prices was also very noticeable in regard to services which, apart from the rents of older properties, are only subject to price control in isolated cases. There has been some slackening in the rise of food prices recently, largely as a result of seasonal factors. The general level of consumer prices, measured by the revised INSEE index of 259 articles taken on a national basis, rose between December 1963 and March 1964 by approximately the same amount (less than in the previous months) as in the fourth quarter of 1963 (approximately 0.6 %). It was still 4 % above the level for the corresponding period of last year.

Since exports in the first four months of 1964 increased somewhat more rapidly than imports, (and the terms of trade were somewhat more favourable than before) there has been practically no further deterioration in the balance of trade. According to the customs returns, seasonally adjusted, the deficit calculated on an annual basis remained in the region of about \$1 200 million. It appears, however, that net earnings from service transactions are no longer sufficient to prevent the emergence of an unfavourable balance on current transactions. There was probably only a slight surplus on the overall balance of payments. At any rate, the official gold and foreign currency reserves increased by only \$76 million in the first four months of this year, after Italy had drawn approximately \$50 million in March from the French quota with the IMF; the corresponding figure at the same time last year was \$440 million. The net foreign exchange commitments of the commercial banks must have taken a considerable turn for the worse, particularly in April.

The substantial reduction in the net inflow of foreign currency put a perceptible check on the expansion of liquidity. In addition, the contribution of the government's cash transactions to liquidity, was noticeably less than hitherto. The deficit to be covered by the Treasury in the first quarter of 1964 was, in fact, only one third as large as the year before; this was due not so much to the less rapid increase in expenditure, which was still 10 % above that of the previous year, as to the rapid increase in revenue, which was partly of inflationary origin. The liquidity of the commercial banks was at times under considerable pressure, which led to increased recourse to the funds of the Central Bank, and, as it was accompanied by an upward movement in interest rates, to certain strains on the money market. It seems that the banks have recently been accepting an increased volume of foreign funds in order to meet the economy's continuing heavy demand for credit. In the first two months of the year bank credits to business were curtailed to a substantially greater extent than is normal at this time of year, taking into account the official limitation of credit expansion to 10 % for the period from the end of February 1963 to the end of February 1964, and in March they increased again very sharply. The total volume of outstanding short and middle-term bank credits at the end of March was some

14 % higher than a year before. The capital market continued to be very active. In addition to big issues by trade and industry, the market absorbed in the middle of March the second portion of the 4.25 %—4.75 % government loan 1963 amounting to 1 500 million francs.

## 2. Outlook

Over the coming months one may expect a continued expansion of demand and a further real growth at approximately the same rate as that which has prevailed since the autumn of 1963. Exports of goods and services will continue to provide a rather powerful stimulus to growth. The capacity of foreign markets to absorb imports has risen as a result of a general revival of economic activity or of an increase in the availability of foreign exchange, and at the same time French industry is showing greater interest in exports and is able to offer better delivery dates as a result of the falling off of excessive internal demand. Moreover, the competitiveness of French products, which had deteriorated to some extent in 1963, has recently improved, as a result of the slackening in the rise in domestic costs and prices, coupled with the persistent—and even increasing—inflationary tendencies in important foreign markets. At all events, the last few months have seen a striking improvement in the prospects of French exporters. The results of the EEC survey of business activity show that the inflow of foreign orders is regarded as being more satisfactory, particularly in the metal industries, vehicle manufacture and the chemical industry.

There are again prospects of moderate expansion in internal demand during the coming months. As far as investment expenditure (gross fixed asset formation) is concerned, it is unlikely that business managements will abandon their present attitude of caution in the very near future in view of the current economic policy, but at any rate there appears to be no likelihood of a falling-off in their investment-mindedness. Expenditure by the public undertakings and by the government on buildings and equipment will certainly show a further considerable increase, as laid down in the plans, but this will be kept more in line with available capacity than was the case last year. In the housing sector demand will continue to be high.

The upward trend in private consumers' expenditure will also continue as a result of the rise in personal incomes, which, although smaller than in the six summer months of 1963, is still likely to be quite appreciable. Nor can the possibility be ruled out that those households which possess relatively large cash reserves, will be ready to offset a lower rate of increase in their incomes to some extent by reducing the amount put aside in savings.

These probable trends in overall demand should be adequate to ensure a continued growth in industrial production. At any rate, managements take a thoroughly optimistic view: according to the EEC questionnaire on business activity sent out in April, their stocks of finished goods are in general exceptionally low, while new and existing orders are more satisfactory than at the end of 1963. This does not, of course, rule out variations in individual industries; in general, however, there is likely to be a relatively strong upward trend. The only limitations on increased production as a result of inadequate capacity are likely to occur in the building trade, although the other industries have been working nearer to capacity in recent months and shortages of equipment are once again forming a more noticeable bottleneck.

There should also be an increase in agricultural production. Provided that weather conditions are normal, results should be much better than last year, notably for crops.

Although the dominant trend in the coming months is likely to be one of better equilibrium between demand and domestic production, there will probably be only a slight slackening in the expansion of imports of goods. In addition, a small increase may be expected in net earnings from services, particularly from the tourist traffic.

Hence there will probably again be an unfavourable overall balance of current transactions, although there is no longer any fear of a substantial increase in the deficit, in view of the relatively more favourable prospects for visible exports.

The trend of prices, as reflected in the various indexes, should remain steady in the coming months. This still does not imply, however, that there will be a corresponding easing of the strains in the economy; it will still be due mainly to the continuation of direct government price controls. There are also seasonal factors which exert considerable temporary pressure on certain food prices. The basic tendency towards increased prices is likely to remain strong, however; at all events the expectations of trade and industry in regard to prices, which had become much more modest immediately after the introduction of the stabilization programme in the autumn of 1963, rose again substantially in March.

In view of this trend, which is very likely to prevail during the coming months, there is no reason to make any substantial alteration to the estimates given in the last Quarterly Survey (1/1964) for the whole year 1964 in regard to the volume of supply of goods and services and its utilization. The only upward revision which appears to be required is in connection with the estimated rate of growth of foreign trade, both imports and exports.

*Supply and utilization of goods and services*

	1962 <sup>(2)</sup>	1962 <sup>(2)</sup>	1963 <sup>(2)</sup>	1964 <sup>(3)</sup>
	At current prices (in FF '000 million)	% variation by volume on preceding year		
Gross national product	356.3	6.6	4.3	5.0
Imports <sup>(1)</sup>	48.6	9.2	12.0	11.5
Private consumption	230.1	7.0	6.3	5.0
Public current expenditure	47.9	4.3	2.0	2.0
Gross fixed asset formation	70.0	7.5	5.9	5.0
Exports <sup>(1)</sup>	51.1	2.5	7.4	9.5

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> Rapport sur les Comptes de la Nation de l'année 1963; SEEF., Paris.

<sup>(3)</sup> Commission estimates.

*Note* : The forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts from the member countries, but are established and published on the sole responsibility of the Commission.

There should be no substantial alteration to these figures for the whole year 1964, even if the expansion of the economy should slow down considerably towards the end of 1964 and during a large part of 1965. At any rate, the Commission considers that there is no real reason why this should occur, although, incidentally, it would be by no means undesirable in the interests of a rapid restoration of equilibrium, particularly in regard to the stabilization of costs and prices. At the present time, all forecasts concerning the likely trend of the economy towards the end of 1964 and during the year 1965 will be subject to some uncertainty, because it is particularly difficult to forecast the decisions which private managements will make in regard to investments. It is not impossible that the recent pressure on profit margins may lead them to continue their very cautious policy. On the other hand, taking the economy as a whole, there are a number of stimulating factors. In the first place, there is almost sure to be continued expansion in certain demand components. This is probably true in the case of foreign demand, at all events. Secondly, one may expect a further increase in expenditure by public undertakings and the government on buildings and equipment. In addition, the demand for house building is likely to increase still further. Hence, if allowance is made for the fact that private consumers' expenditure will still tend to increase, although doubtless at a

slower rate, (the extent of the increase will depend partly on the attitudes adopted by the two sides in the wage negotiations which are due to take place in the autumn of 1964) it would appear to be not unrealistic to expect a certain revival in private investment. Support for this point of view is found in the fact that the marked recovery which is at present taking place in certain important basic industries could well give rise to extensive new investment. Finally, the position of industry in regard to profits and liquidity—in absolute terms—is likely to show some improvement, in view of the slowing down of pay increases and the rise in output associated with substantial increases in productivity. The continuing strains in the labour market, though probably somewhat less severe, will again provide substantial inducements to modernization.

According to these working assumptions regarding investment—which, as we have said, are very uncertain, but are presumably admissible as a hypothesis—the slackening in the growth of private consumers' expenditure would prove to be less marked than it might otherwise be.

In these circumstances, there could be a very substantial increase in domestic demand. The Commission's current estimate—always assuming that agricultural production develops normally—is of a growth of approximately 4 %—4.5 % in gross national product in 1965 by comparison with 1964.

These forecasts point to a continuation of the tendency towards a better balanced economy, but the possibility cannot be ruled out that a slight upturn in investment, wages and consumption may, in fact, increase the imbalance once again.

In these circumstances, it is unquestionably right that the authorities responsible for guiding economic policy should continue the stabilization measures already in operation. The main measures are: a tightening up of budgetary policy by restricting increases in expenditure, reducing the adverse cash balance and making greater use of long-term loans; following a restrictive credit policy by limiting the expansion of credits, tightening up the conditions for hire purchase credit and raising the bank rate; making efforts to implement an incomes policy; stimulating competition and providing for an increase in the labour supply. All these measures are largely in line with the policy recommended by the Council of the EEC on 14 April 1964.

A new measure which has come into force since the unanimous adoption of these recommendations and the time of writing is an increase in some postal charges. This increase—yielding about 250 million francs in a full year—can be regarded, according to the text of the Council's recommendation, as an increase in taxation. Moreover, when the national product is increasing by 5 %, increased tax receipts solely due to the operation of progressive rates of tax can—disregarding the effects of inflation—be regarded as increases in taxation.

In accordance with the recommendations, France would in fact have to be able to point to an increase in tax receipts of this kind, since the increase in government expenditure in 1964, by comparison with 1963, is likely to exceed the recommended maximum of 5 % in the full year, despite the cuts which have already been made. Some further measures, on a limited scale, will probably be necessary in order to keep the budgetary position completely in line with the recommendations.

For 1965 a stricter control of the growth of government expenditure is planned by comparison with 1964. It is important that this growth should really be kept within the recommended maximum of 5 % and not based on the expected increase in the nominal national product, since this would involve continued dependence on inflationary tendencies.

In this connection it would seem desirable to mention that the 1965 budget should not provide for any tax concessions, particularly for the main bulk of incomes which are devoted primarily to consumption, even if there should be a prospect of increased tax receipts owing to the progressive effect of certain taxes reinforced by the effects of inflation. Reduction in tax rates may be necessary from time to time in connection with the general tax structure, but they should only be granted when they are possible, or even desirable, in the light of the general economic situation; in the case of France, this means only when over-employment has been eliminated and when wage costs per unit of production and the general level of prices have been completely stabilized. In the light of the latter objective, there could be no harm whatever in budgeting for surpluses over a limited period in the Treasury's cash transactions. In this connection, consideration might also be given to the possibility of issuing loans not only to finance expenditure, but also to mop up liquidity, particularly as a further reduction in the liquidity cushion would increase the effects of the measures already taken to control credits. It might perhaps also be desirable to consider whether the actual credit policy should not be remodelled on more restrictive lines in view of the need to achieve as rapidly as possible a restoration of internal and external equilibrium in accordance with the recommendation of the Council of Ministers issued on 14 April of this year.

On no account, however, should there be any departure from the present policy of restraint—e.g. to alleviate supposed cash difficulties affecting the banks and some individual firms. An easing of restrictions at the present time would be inappropriate in view of the present economic situation and the probable future course of development, and would also run counter to the recommendations of the Council of Ministers of the EEC issued on 14 April.

At the beginning of July the monetary authorities announced a reduction in the minimum reserve requirements of the banks (reduction of the "coefficient de trésorerie" from 36 % to 34 %) as a temporary measure, intended merely to facilitate monthly



settlements—always very difficult owing to seasonal conditions—and particularly to discourage recourse to foreign credits. None the less, this produces a very considerable increase in the banks' monetary reserves—and, because of the peculiarity of the French minimum reserve system, particularly for the granting of short term credits. By comparison with this, the fact that the penal rate of interest payable by the banks on exceeding the rediscount limit by a certain amount was raised from 6 % to 7.5 %, is only of minor importance.

Little restrictive effect can be expected from the further reduction—also announced at the beginning of June—of the limit up to which hire purchase firms may make advances, since the outstanding volume of hire purchase credits is in any case considerably below the permitted maximum and hence—from the overall point of view—a very substantial margin still remains for a further expansion of hire purchase credit.

## C. Italy

*In the first three or four months of the year overall demand continued to expand, but the pace seems to have slackened further.*

*Among the various components of demand, exports of goods and services again advanced quite briskly. On the other hand, gross fixed asset formation, after adjustment for seasonal and fortuitous variations, seems to have risen little if at all. Though the mild weather, which contrasted with last year's hard conditions, boosted activity, the building sector, like the capital goods industry, suffered appreciably from financing difficulties due in the main to dwindling profit margins, tightness on the capital market and a restrictive credit policy. Private consumers' expenditure will doubtless prove to have made an appreciable further advance, but here too the pace may again have been slower.*

*Farm output rose vigorously, and so too, for the first time in two years, did livestock production. On the other hand, industrial production would seem at most to have maintained its previous level; none the less the national index for the first quarter was 7.6 % up on the corresponding 1963 figure.*

*With demand expanding more slowly and domestic supply in a number of industries improving distinctly, the growth of imports lost momentum. Even so, the value of merchandise imports in the first quarter was still 22.5 % higher than a year earlier.*

*The favourable development of farm output, coupled perhaps with the incipient decline in the growth of private consumers' expenditure, tended to exert pressure on prices: wholesale food prices, which were still climbing sharply in the second half of 1963, actually fell slightly between December 1963 and April 1964, and the corresponding retail prices changed very little. On the other hand, the decidedly steep rise in the prices of other goods and of services continued almost unabated.*

*In April the year-to-year rises in the wholesale and retail price indexes were 3.9 % and 4.7 % (in December they had been 5.5 % and 6.9 %). The cost-of-living index was 5.6 % higher than in April 1963.*

*It would seem that the deterioration in the balance of current payments was below what is normal for the season, mainly because the increase in the deficit on trade was relatively modest; none the less the deficit on current account was once again very considerable; as however net exports of capital declined, the deficit on the*

overall balance of payments ceased to grow. Since moreover Italy drew on the International Monetary Fund in March to the full extent of its gold tranche, the drop of \$233 million of official gold and foreign currency reserves between the end of December 1963 and the end of March 1964 was, despite a further reduction of the short-term foreign indebtedness of the banks, substantially less than the overall payments deficit.

*The expansion of demand may well continue during the rest of 1964, though at a much slower pace. It will be appreciable in the case of exports and private consumers' expenditure, whereas gross fixed asset formation generally will again be decidedly weak. The increase in gross national product is likely to be 3.5 % for the full year. Although for the full year the relationship between the growth rates of exports and imports will be better than in 1963, a further slight increase in the deficit on trade can be expected. The deficit on the overall balance of payments is almost certain to be again quite heavy. The upward cost and price trends will continue, though at a slower rate.*

*So far the outlook beyond the end of this year holds out no promise of a sufficiently rapid return to equilibrium in 1965. The general trend is certainly in this direction, but there is no escaping the fact that more stabilization measures are necessary.*

## 1. Recent developments

Exports of goods and services as a whole again expanded quite substantially in the first quarter. The year-to-year growth rate for visible exports (in value, on the basis of customs returns) was no less than 12.1 %, compared with 8.5 % for the fourth quarter of 1963. It would hardly be safe, however, to deduce from the disparity between the two rates the trend was becoming steeper, since both figures would seem to have been affected by fortuitous factors.

With the exception of farm products and foodstuffs, virtually all sales abroad, and particularly sales of chemicals, probably showed an increase on the previous quarter. The expansion of sales to the rest of the Community and to other industrial countries was particularly rapid.

The trend in exports of services also seems to have improved in the first quarter.

The partial indicators now available suggest that the growth of home demand slowed down in the early months of 1964: gross fixed asset formation in the construction and equipment sectors appears once again to have been hesitant. In the first quarter completions in the residential sector (by number of rooms) were up more than 5 % and space enclosed in industrial and commercial buildings up more than 19 % on the same period in 1963, with corresponding figures of 4 % and - 12.1 % respectively for the final quarter of last year; but while building suffered from bad weather last year, this year it was boosted by good weather. The fact that since last summer the output of cement per working day, after adjustment for seasonal variations, has tended to flatten out, is probably a more reliable pointer to the situation in the building industry than the actual growth rates. Both the foreign trade returns for machinery, appliances and transport equipment and the corresponding production figures also betray the weak trend of investment in capital goods during the first quarter.

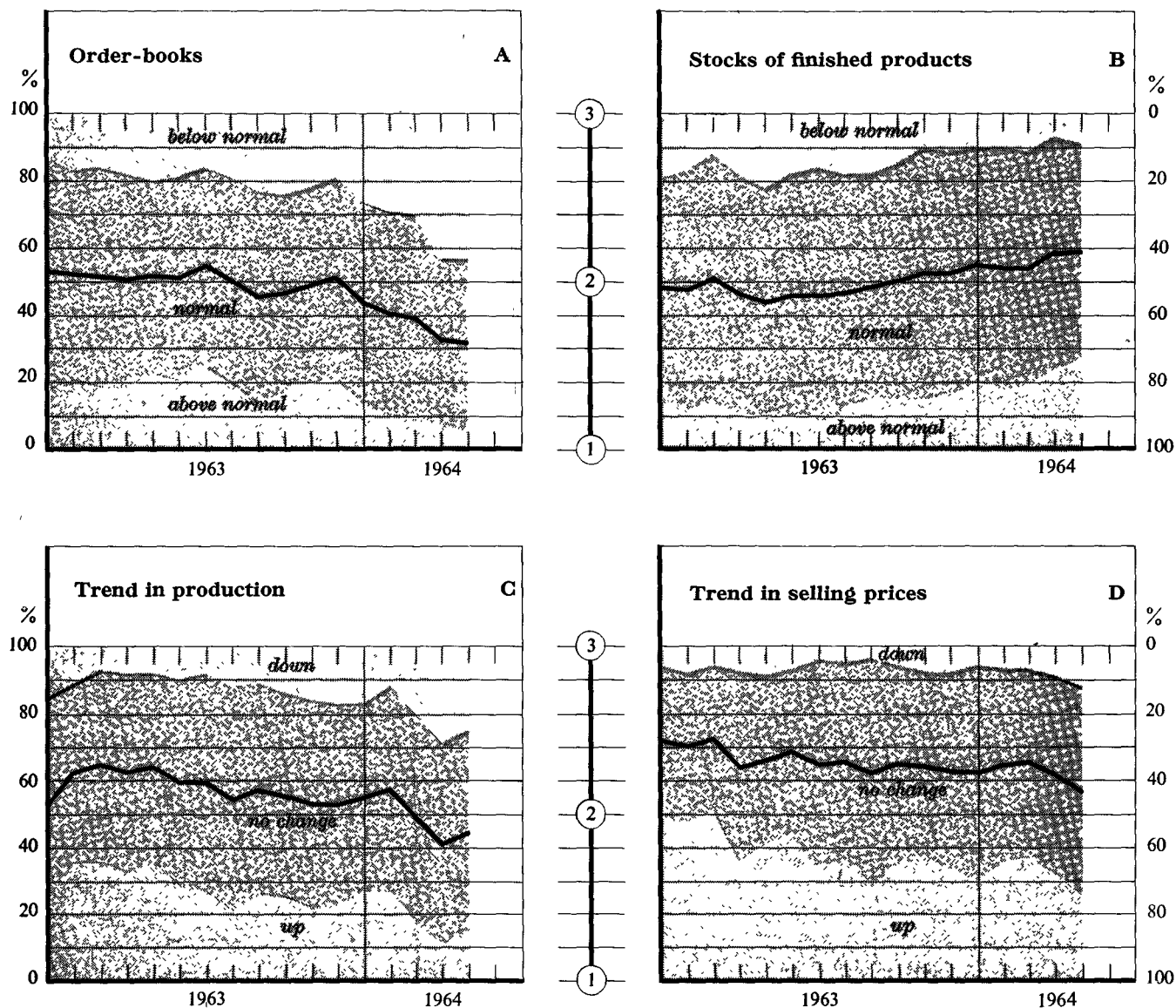
The expansion of private consumers' expenditure would seem to have slowed down. At any rate, production and particularly imports of consumer goods advanced less rapidly in the early months of 1964 than in the last months of 1963. None the less, mass incomes would seem once again to have swollen appreciably, because cost-of-living allowances have again been stepped up considerably under existing sliding scale wage agreements and by new collective agreements in certain industries, notably wholesale and retail trade and transport. The result was that in by far the greater part of the Italian economy (covering industry proper, agriculture, wholesale and retail trade, transport and government service), minimum negotiated wages and salaries, including family allowances, were in the first quarter a good 7.5 % up on the 1963 monthly average.

Strain on the labour market eased quite appreciably, mainly, it would seem, because of the slower growth of overall demand: the rise in unemployment figures normally recorded between October and January was, as the ISTAT sample surveys show, particularly sharp this winter. According to the same source, the number of women employed in industry fell, in January, to 75 % below the figure for January 1963, and the number of underemployed persons, men and women, was up 14 % on the corresponding 1963 figure. Between January and April employment does not seem to have built up as much as it usually does at this time of the year. Some industries, notably motor vehicles, have been working short time since March.

In contrast with the same period of last year, farm output this year benefited from the weather. It was not only crop products, especially fruit and vegetables, which improved, but livestock production, too, showed better results for the first time in two years.

Industrial production was 7.6 % up on the returns for the first quarter of 1963, compared with a year-to-year growth rate of 8.7 % in the previous quarter. But in relation to the figures for the end of 1963, the figures for the early months of 1964 will probably, after seasonal adjustments, show that production marked time or even suffered

## BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

- by 0.03 for the answer "above normal", or "up";
- by 0.02 for the answer "normal", or "no change";
- by 0.01 for the answer "below normal", or "down".



a slight setback. This applies particularly to chemicals, though capital and consumer goods also seem to have been rather listless.

Increased supply at home was again accompanied by an increase in imported goods and services. Customs returns show that the value of visible imports in the first quarter was 22.5 % higher than a year earlier (volume returns are not yet available), compared with 20 % for the preceding quarter. But if allowance is made for the impact of certain exceptional factors, the rate at which imports were expanding seems to have declined substantially. Preliminary information suggests that import trends in April and May were even decidedly weak.

With the exception of foodstuffs, textiles, capital goods and transport equipment, the year-to-year growth rates for imports of almost all categories of merchandise were in the first quarter of 1964 higher than in the last quarter of 1963. The growth rate for imports of farm products advanced with particular vigour, in line with the vigorous increase in deliveries from the developing countries.

The growth rate for imports of services seems to have eased.

The slackening in the upward trend of prices which had set in towards the end of last year persisted in the first four months of 1964. It would seem that this was mainly due to the weather, although a weakening in the expansion of private consumers' expenditure doubtless made its contribution. At all events wholesale food prices, which were still climbing steeply in the second half of 1963, eased nearly 1 % between December 1963 and April 1964. On the other hand, the rise in prices for manufactures continued virtually unabated, and totalled 1.5 % over the same period. The pattern of retail price movements was very similar: for foodstuffs, drink and tobacco, the April index was scarcely higher than in December 1963, while the price of other consumer goods, which had risen by 2.2 % from August to December 1963, rose a further 2.5 % between December and April.

All in all, wholesale prices were in April 3.9 % up and retail prices 4.7 % up on the figures of a year earlier. Last December the corresponding increases had been 5.5 % and 6.9 %.

The rise in the deficit on trade, which in the first quarter of 1964 stood at \$758 million compared with \$650 million in the final quarter of 1963, seems to have been at most slightly above the normal seasonal increase. Although, over the same period, net receipts from services declined in accordance with the seasonal trend, the deficit on the overall balance of payments in the first quarter was, thanks to a decline in the deficit on capital transactions, even a little lower (\$436 million) than in the preceding quarter (\$452 mil-

lion). The drop of \$233 million in official gold and foreign currency reserves proved, despite a further reduction in the short-term foreign indebtedness of the commercial banks, to be substantially less than the balance-of-payments deficit, since Italy drew on the International Monetary Fund in March to the full extent of its gold tranche.

These developments meant that in the first quarter of 1964, as at the end of 1963, the balance-of-payments position exerted considerable pressure on the liquidity of the banks. As the Treasury's cash operations, which in 1963 were still the key to the expansion of liquidity, now worked in the same direction as the payments deficit, there was, despite a decline in notes and coin in circulation outside the banking system and a further appreciable increase of rediscounting by the monetary authorities, a sharp reduction in bank liquidity both in absolute terms (more than Lit. 170 000 million down) and in its ratio to deposits; though the latter are still increasing only slowly, the ratio of liquidity to deposits fell from 5.7 % in March 1963 to 4.1 % in October 1963 and 3.7 % in March 1964. At the same time, the expansion of bank credit has continued to weaken: the

*Supply and utilization of goods and services*

	1962 <sup>(2)</sup>	1962 <sup>(2)</sup>	1963 <sup>(2)</sup>	1964 <sup>(3)</sup>
	At current prices (in Lit. '000 million)	% variation by volume on preceding year		
Gross national product	24 789	6.0	4.8	3.5
Imports <sup>(1)</sup>	4 365	15.4	20.7	7.0
Private consumption	15 006	6.7	9.2	6.0
Public current expenditure	3 645	4.5	5.2	4.0
Gross fixed asset formation	5 846	8.9	5.5	- 3.5
Exports <sup>(1)</sup>	4 357	11.8	6.4	8.5

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> Italian Central Institute of Statistics (ISTAT), Rome.

<sup>(3)</sup> Commission forecasts.

*Note* : The forecasts are approximations based on particular hypotheses, generally mentioned in Quarterly Surveys; they have been discussed with the experts from the member countries, but are established and published on the sole responsibility of the Commission.



year-to-year growth rate only just reached 18 % in February, after being 24.1 % in February in 1963 and 24.8 % last October.

The capital market was still sluggish. The net total of security issues evidently declined further in the first quarter. Interest rates again tended to climb sharply: the net rate on government securities rose from 5.6 % in December 1963 to 5.9 % in March. The securities market rallied for a time in the second half of April, evidently owing in part to certain movements of capital back to Italy.

## 2. Outlook

Even if the authorities pursue their current efforts to combat internal and external disequilibrium, overall demand in money terms is likely to expand further in the next few months, though far less rapidly than in 1963.

External demand will almost maintain its distinct upward trend: economic activity throughout the world can be expected to continue its brisk advance and the quantities of merchandise available for export should increase vigorously, not only in the agricultural sector, where production is expected to be higher than last year, but probably in other sectors as well, since in these the share of production available for export should increase as measures adopted by the Government to curtail the growth of internal demand leads to a greater export drive. In addition, it is likely that the tariff cuts to be introduced in mid-1964 by the Federal Republic—Italy's most important trading partner—will provide fresh opportunities for Italian exports (see Quarterly Survey No. 1/1964, Ch. II.A). Lastly, the following official measures, adopted or decided on at the end of April, should serve to sustain the expansion of exports: prompter and more generous turnover tax rebates on exports and an increase in the corresponding budget item; substantial lengthening of advance export credits; 50 % cut in export insurance premiums; reduction or abolition of stamp duties on bills concerned with exports; larger subsidies for the Foreign Trade Institute (ICE); increased tax reliefs for expenses in connection with exports; suspension of the levy on imports of cereals used in making flour products for export.

Internal demand in money terms is also likely to expand further, but in view of the persistent pressure on profit margins, the tightness of the capital market and the restrictive credit policy pursued by the monetary authorities there may be, if anything, some loss of momentum. The fact that in the first quarter the volume of building planned—both housing and industrial and commercial construction—was, after a long spell of increases, lower than in the same period of 1963, coupled with the fact that public works activity has virtually ceased to increase, points to a low level of investment in construction.

Lastly, investment in capital goods will expand only slightly; one factor supporting this view is the slack trend in domestic orders placed with the industries concerned.

Public current expenditure on goods and services is likely to show a further distinct increase. From 1 July onwards cost-of-living allowances are being raised in the public sector, a measure which will cost some Lit. 80 000 million for the full financial year 1964/65. For the same period, expenditure on salaries is being put at 12 % above the figure in the 1963/64 budget. None the less, it is probably safe to count on the growth rate being appreciably lower than in 1963.

Despite the increases in agreed wages already granted and those which must again be expected in major sectors of the economy (textiles, chemicals and public service), and despite possible improvements in pensions and family allowances, the expansion of private consumers' expenditure is likely to slacken further: industrial production (including construction) began to lose momentum some time ago and is likely to go on doing so, and the workers' take-home pay should therefore increase much less than last year. For the same reason the drift from the land into industry—i.e. to a better paid sector of the economy—may well come to an end. Lastly, it is fairly certain that the proposed control and tightening of consumer credit conditions will curb the growth of private consumers' expenditure.

The outlook for agricultural production is relatively favourable, whereas in industry and in the other sectors as a whole it is appreciably less expansive than last year because the growth of demand has slowed down. The backlog of orders in industry, at any rate, seems quite appreciably lighter.

In these circumstances imports are unlikely to gain more ground. Prices should rise more slowly in 1964 than last year, but the increase over 1963 is still bound to be substantial, if only because of the high level reached towards the end of 1963. Moreover, the outlook for the growth of wages and production points to a further appreciable rise in unit wage costs.

The seasonally adjusted trade figures—and even more the overall balance of current payments—should develop a great deal more favourably in the coming months. None the less, the comparison between 1963 and 1964 is almost certain to show a further growth of the deficit on trade; the current payments account as a whole may show a deficit of much the same size as in 1963.

The present outlook then, coupled with the official figures for 1963 now published by the Italian authorities, call for a downward revision of most of the forecasts published

in the last Quarterly Survey (1/1964) on the extent to which the volume of the main components of supply and demand for the full year 1964 will differ from the 1963 figures.

As to the further development of the Italian economy into 1965, it is at present clearly impossible to do more than estimate trends in the light of current economic policy and the economic situation in the world. It seems obvious, however, that economic policy needs still more substantial reinforcement if Italy is to avoid more serious balance-of-payments difficulties and even the considerable danger of a sharp recession resulting directly or indirectly from them.

At any rate, the outlook seems to point to continuing expansion of demand, though at an appreciably lower rate: exports will certainly climb further, especially as it becomes harder to dispose of merchandise at home. As for the components of internal demand, it can safely be assumed that public current expenditure will grow further, though not so fast as before. Nor will the expansion of private consumers' expenditure come to a halt, although the number of persons in employment might for a time cease to rise appreciably. Lastly, the downward trend in investment expenditure could well persist.

In these circumstances, the expansion of imports is likely to prove very weak and, as far as visible trade is concerned, appreciably less—on a percentage basis—than that of exports. Should this prove to be the case, it would be the first time for many years that the trade account for the full year closed with a smaller deficit. In these circumstances the increase in the real gross national product may be between 2.5 % and 3 %.

These trends are likely to be accompanied by some further increase in unit production costs and in prices.

Earlier Quarterly Surveys have already reported most of the stabilization measures adopted by the Italian authorities before the EEC Council's session of 13-14 April 1964, at which it adopted the Commission's recommendations on measures to restore the internal and external economic equilibrium of the Community <sup>(1)</sup>. The policy pursued so far can be summarized as follows :

The authorities have endeavoured to stem, by a variety of means, the unduly rapid expansion of internal demand in money terms, which was and still is at the root of current price and payments difficulties. From mid-1963 onwards a more restrictive credit policy was applied, and this has done much to check the expansion of industrial investment; on

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<sup>(1)</sup> See annex.

the other hand, the more stringent consumer credit arrangements proposed by the Government in February 1964 are not yet operative, and it would seem that they are likely to be less severe than originally intended. From the autumn of 1963 onwards a number of tax or budgetary measures were brought into force or decided on: these include use of certain increased tax revenues to cut the budget deficit; action to expand tax revenues, mainly by the prompter settlement of tax disputes and the introduction of new or the increase of existing taxes on certain non-essential goods; reduction of the rate of growth of government expenditure under the provisional budget for the period from 1 July to 31 December 1964; and limitation of the growth of the Treasury's cash deficit. In addition the Government has embarked on talks with both sides of industry on measures to promote price stability. A number of measures affecting competition, such as more generous granting of licences in the meat trade and permission for farmers to sell direct to consumers, and direct price intervention, particularly on sugar, drugs and rents, have also helped to hold down prices and costs. In addition, an effort has been made to speed up the growth of supply; this has been done through measures in the commercial field (introduced as far back as 1962), by others affecting the labour market (national service has been cut from 18 to 15 months) and by the grant of tax reliefs to stimulate investment. Lastly, the authorities are planning to inject new life into the securities market by reducing, by a measure not yet put into force, the tax on stock exchange transactions and, especially, by adjusting dividend taxation rules.

Most of these measures, which had been adopted or decided on before 14 April last, are broadly in line with the EEC Council's recommendations. Only in a few instances was this not the case: for example certain taxes, such as the higher tax on petrol and the new tax on private cars and motor-boats, have brought in more than was forecast in the budget, and the excess yield is to be used to finance investment, instead of all being devoted—as it should have been—to reducing the budget deficit.

Between 14 April 1964, when the Council adopted the recommendations referred to, and the time of writing, certain telephone charges have been increased in accordance with the recommendations. An increase in railway and post-office charges—services which have both been losing a lot of money—is apparently also under consideration.

The Council's recommendations state that additional receipts from these sources may be treated as if they represented increased tax revenue, which Italy must obviously be able to show if it is to fall in line with the recommendations. For despite all efforts made so far to curtail the growth of public current expenditure, it is likely that this item—in terms of value—will again exceed appreciably the 5 % ceiling recommended by the EEC Council, at least for the full year 1964 as compared with 1963. In any case, Italy will still have to stiffen its handling of the budget, not only from the angle of public current expenditure but even more from that of revenue, if equilibrium is to be restored with the necessary speed.

An incomes policy that could—as recommended by the Council—ensure better coordination between the expansion of income per head (in monetary terms) and the expansion of output per head could do much to allow other stabilization measures to be framed in a manner that would not unduly hamper economic activity. There can, however, be no question but that some temporary reduction in the tempo of expansion is inevitable if stabilization is to be achieved.

## D. The Netherlands

*The economy continued to expand during the first three months of 1964. The trend of exports picked up sharply and internal demand also expanded vigorously. Gross fixed asset formation continued to increase. There was again a marked expansion in private consumers' expenditure, mainly under the influence of the very substantial wage increases resulting from the agreements reached between management and labour last autumn, but the rapid rate of development achieved in the previous quarter was not fully repeated.*

*This increase in demand engendered a substantial increase in supply. Industrial production continued to rise and exceeded the—admittedly relatively low—level of the first quarter of 1963 by about 9.5 %. There was also a further substantial increase in imports. Conditions in the labour market continued to be very strained.*

*There has been a marked increase in the upward movement of prices since the beginning of the year, although food prices—apart from a sharp increase in April, due mainly to the statistical methods employed—remained stable. The deficit on the trade balance rose substantially. The overall balance of payments showed a deficit of approximately Fl. 500 million.*

*Over the rest of the year, the main trend of the economy will be in the direction of a further brisk expansion of overall demand, although the pace may slacken. This applies firstly to exports which, in view of the rapidly expanding world economy, are likely to make a better showing than had been anticipated, although they may be held back to some extent until the autumn owing to the increasing claims of domestic demand on the country's resources. Towards the end of the year there may be a slackening in the growth of fixed asset formation as a result of the effect of the economic policies introduced and of the considerable increase in production costs on the liquidity position of firms. Finally, the upward trend of private consumers' expenditure owing to the considerable rise in total salaries and wages during the first half year, will probably reach a climax in the summer and then slacken off.*

*Output will continue to rise briskly but its growth rate may also slacken somewhat in the course of the year. Nevertheless, it is estimated that the real gross national product for the year 1964 as a whole will increase by 5.5 % compared with 1963.*

*Imports will continue to expand rapidly, although the rate may slacken slightly. Prices will continue to show a strong upward tendency for the time being.*

*In the light of these forecasts, the internal and external equilibrium of the Netherlands economy will not be restored before the end of 1964, and probably only in the later part of 1965, always provided that there is a substantial slackening in the growth of internal demand. In fact, a falling off in productive investment—as a result of the contraction in profits and the decline in liquidity, which are likely to be substantial in 1964—could contribute to such a development both directly and indirectly, through a certain easing of the labour situation. But if the demand is to develop in accordance with the need to restore equilibrium, it is essential that no decisions should be taken in the autumn of 1964 which may lead to further wage increases in 1965 in excess of the increases in productivity. Moreover, the possibility of restoring the inner equilibrium will depend largely on the trend of prices in 1964. There is therefore a continuing need for an economic policy which will put an adequate curb on overall demand.*

## 1. Recent developments

There was a marked upward trend in exports of goods and services during the first quarter of 1964. According to the foreign trade returns, exports of goods and services were 17.7 % higher by value and 17 % higher by volume than at the same period last year; this compares with corresponding year-to-year figures of only 6 % and 3.5 % respectively in the fourth quarter of 1963. In making this comparison, however, it must be borne in mind that the export figures for the early months of 1963 had been relatively low, owing to special factors, of which the most important was the exceptionally hard winter. But the annual rates of increase do seem to reflect an effective increase in exports, and this hypothesis is supported by the figures after adjustment for seasonal and fortuitous variations. In fact, exports to non-member countries, in particular, seem to have risen considerably since November 1963; at the same time, the expansion of exports to member countries was maintained.

Internal demand continued to grow at the accelerated rate which has prevailed since the middle of 1963; the curbs which have been applied so far do not yet appear to have had any notable effect.

Gross fixed asset formation also increased considerably, both by value and by volume, and this applied not only to the building sector, which had been favoured by the relatively mild weather and the increased labour force, but also—to judge by the import and production figures—in the sphere of capital investment. It would seem that

managements were still quite ready to invest, owing to the healthy outlook for the world economy, the unexpectedly good trading results for 1963, the continuing labour shortage and the further steep rise in labour costs in 1964 which managements are attempting to offset as much as possible by rationalization.

Total gross fixed asset formation by enterprises, including house building, appears, on the basis of preliminary figures, to have been about 30 % higher in value (25 % by volume) in the first quarter of 1964 than it had been a year before; this compares with corresponding annual rates of increase of 20 % (and 15 %) in the fourth quarter of 1963. But building investment in this sphere was at least 60 % higher by volume in the first quarter of 1964 than in the first quarter of 1963. This obviously reflects the effect of the difference in weather conditions between the early months of 1963 and of 1964, but there can be no doubt that there was a very strong trend towards expansion. Growth was probably also very substantial in public investment expenditure.

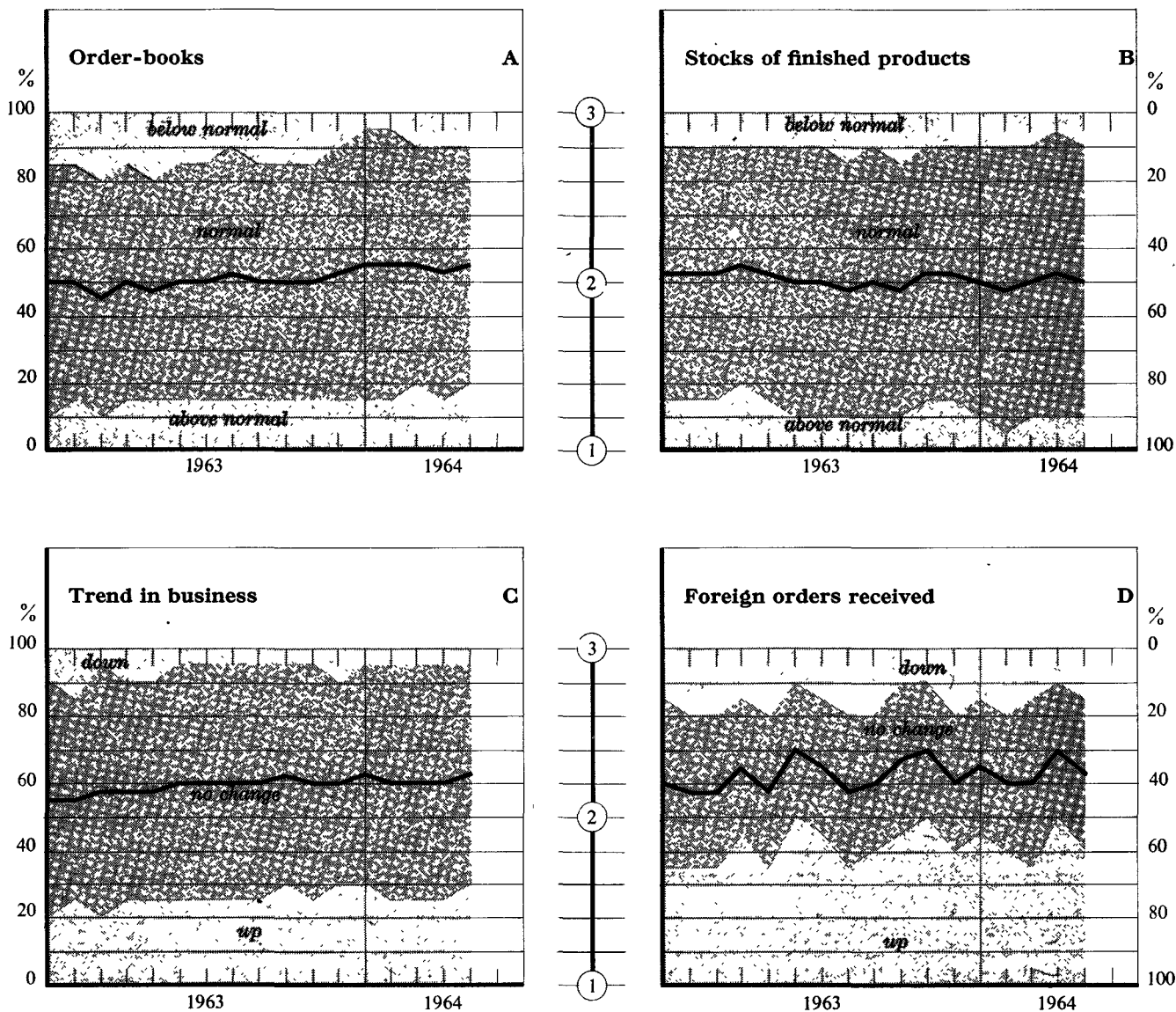
The expansion of private consumers' expenditure, which had gathered momentum from the middle of 1963 and particularly in the last months of that year, seems to have settled down again somewhat during the first quarter of 1964 from the point of view of the level which it had reached. Nevertheless, the expansion was very considerable, even if the rate of increase by comparison with the corresponding period of last year—13 % in value and 9 % by volume, compared with 11.5 % in value and 8 % by volume in the fourth quarter of 1963, was to some extent a reflection of special factors which affected the growth of consumption in the early months of 1963. It is noteworthy that 75 % more new vehicles were registered in the first quarter of 1964 than in the corresponding period of last year.

The most important stimulus to the expansion of private consumers' expenditure was still provided by the large increase in the income of employed persons. The wage agreement came into force, and the majority of the other agreements provided for increases and approved by the Government, started a general wave of upward "adjustment" on 1 January 1964. On that date the wage increases provided for in some of the collective agreement came into force, and the majority of the other agreements provided for increases by 1 April at the latest. In addition, the minimum weekly wage was raised to Fl. 100 in most sectors of the economy. By and large, average wage rates in the business sector must have risen by more than 7 % between December 1963 and January 1964. In the case of women's wages the upward movement at the beginning of the year was substantially higher—probably more than 11.5 %. As has already been mentioned, the upward movement continued in the following months. It was slower than at the beginning of the year, but on 1 March there was an effective wage increase of 16 % in the building industry.

Wages and salaries in the public service were also raised by approximately 16.5 %.



BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

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

- by 0.03 for the answer "above normal", or "up";
- by 0.02 for the answer "normal", or "no change";
- by 0.01 for the answer "below normal", or "down".



Under the impact of these wage movements, and as a result of a further increase in the volume of employment, the total wages and salaries bill in the first quarter of 1964 was probably at least 12 % higher than in the corresponding period of last year—which was, of course, a period of exceptional cold. In the fourth quarter of 1963 the annual rate of increase was 7.3 %. Allowance has been made here for the fact that the wage drift and the practice of paying “unofficial” wage rates probably decreased as a result of the substantial increases in official wages.

The easing of the labour situation, which had been expected in many quarters as a result of the exceptionally large wage increases, did not occur. The effect was rather the opposite. The mildness of the winter, by comparison with the previous year, coupled with the pressure of demand, produced average unemployment figures in the first quarter of 1964 substantially lower than those of the previous year and approximately 8 % below those for the first quarter of 1962. The seasonally adjusted unemployment figures at the end of April 1964 remained at the same low level. At the same time, the number of vacancies at the end of April was exceptionally high; at 125 000 it was more than five times the number of unemployed persons.

Under the pressure of overall demand, domestic supply continued to expand rapidly. This applied particularly to industrial production which, according to the gross index of the CBS was 9.5 % higher than in the first quarter of last year—a period which was, of course, affected by the special influences to which frequent reference has been made; the corresponding annual rate of increase in the previous quarter had been 7 %.

Imports of goods and services also continued to rise, although not so fast as in the period of marked import expansion which opened at the end of the summer of 1963. In the first quarter of 1964, imports of goods were 18.6 % higher by volume and 22.5 % higher in value than in the corresponding period of last year, which was conspicuous for its relatively low imports. The corresponding annual rates of increase in the fourth quarter had been 16.5 % and 20.5 %. Again, the greater part of the increase in imports was attributable to consumer goods, but imports of raw materials and semi-finished goods rose again as a result of the continuing trend towards building up of stocks.

Very strong forces tended to push prices upwards in recent months: in the first place, the large wage increases had an immediate effect on prices, both from the angle of costs and of demand. Secondly, import prices rose markedly—by 3.1 % between the fourth quarter of 1963 and the first quarter of 1964.

The strong upward movement of prices in trade and industry was checked to some extent by a firmer prices policy—i.e. by direct price controls on a number of goods and

services. In addition, there was a seasonal fall in the prices of some foodstuffs (principally potatoes and vegetables), which cancelled out the previous excessive rises. Hence the retail price index rose by 2.7 % between the middle of December 1963 and the middle of March 1964; in the middle of March the index was 3.7 % higher than it had been at the same time last year. The prices of services, too, must have risen more rapidly.

In April there was a rise in the price of cigarettes and petrol as a result of an increase in indirect taxation. This contributed to a 4.4 % rise in the retail price index between March and April. A more important cause of this rise, however, was an increase in the price index for potatoes and vegetables, due to variations in the base period adopted for statistical purposes (this factor accounted for 2.5 % of the rise in retail prices), coupled with some actual price increases.

The trade balance (as indicated by customs returns) showed a deficit of Fl. 1 340 million in the first three months of 1964, compared with deficits of Fl. 1 140 million in the last quarter and Fl. 940 million in the first quarter of 1963. There was also a marked deterioration in the overall current balance of payments (on a transaction basis), which showed a deficit of Fl. 550 million, whereas in the corresponding quarter of last year it had been in equilibrium. On the other hand, there was a small surplus on capital movement, so that the balance of payments as a whole showed a deficit of nearly Fl. 500 million. Between the end of December and the end of March, the official gold and foreign currency reserves (excluding transactions with the International Monetary Fund) fell by Fl. 290 million; the net foreign exchange position of the commercial banks deteriorated by approximately Fl. 260 million.

Thus the balance of payments had the effect of restricting internal liquidity. The same applies to government transactions. In this connection, it should be noted that in March two government loans totalling Fl. 550 million were issued and subscribed—not merely to finance the budgetary deficit, but also to mop up excess liquidity.

According to the agreement in force, bank credits in the first four months of 1964 were not to be increased by more than 5 % by comparison with the end of 1963 (calculated on the average of outstanding credits in the first six months of 1963); in fact, they increased somewhat more (by 1 % in March and by 2 % in April). Hence “penal deposits” of more than Fl. 109 million had to be held with the Central Bank at the end of April.

At the same time pressure on the capital market from private industry increased substantially; in the first quarter alone, new issues equalled the—admittedly very low—total for the whole year 1963. In addition, the demand for other medium and long term funds undoubtedly increased substantially.

*Supply and utilization of goods and services*

	1962 <sup>(2)</sup>	1962 <sup>(2)</sup>	1963 <sup>(3)</sup>	1964 <sup>(4)</sup>
	At current prices (in Fl.'000 million)	% variation by volume on preceding year		
Gross national product	47.55	2.7	4.5	5.5
Imports <sup>(1)</sup>	23.86	6.6	9.0	12.0
Private consumption	27.48	4.2	6.0	7.0
Public current expenditure	7.04	6.3	3.0	1.0
Gross fixed asset formation	11.60	4.2	6.0	11.5
Exports <sup>(1)</sup>	24.69	6.6	7.0	6.5

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> General Statistical Bulletin 1963, No. 12, Statistical Office of the European Communities.

<sup>(3)</sup> Commission estimates.

<sup>(4)</sup> Commission forecasts.

*Note:* The forecasts are approximations based on particular hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts from the member countries, but are established and published on the sole responsibility of the Commission.

## 2. Outlook

The expansion of total demand will probably continue in the coming months. Although there will be wider variations in the movements of the various demand components, there is little likelihood of any noteworthy reduction in the internal and external imbalance before the end of the year.

Exports of goods and services will probably continue to rise. The result of the latest questionnaire to managements on business prospects show a satisfactory trend in new orders from abroad. The substantial increase in wage costs per unit of production have had—and are still having—an adverse effect on the competitive power of the Dutch economy, but it would appear that this is offset to some extent by the strong stimulus exerted on the Dutch economy by the very buoyant trend in the world economic situation; this trend is particularly marked in non-member countries, in a number of which perceptible increases in costs and prices are taking place or are pending. Moreover, the possibility cannot be ruled out that the fairly strict price controls imposed by the government on home sales and the efforts of managements to offset narrowing profit margins by increased sales may provide greater incentives to export.

The rise in exports, however, is likely to be perceptibly slower than in previous months, at least until the autumn. In the first place, there will be increasing pressure on productive capacity as a result of high internal demand; secondly, the deterioration in the country's competitive position will have a restraining effect, even if only a limited one.

There will be a further considerable expansion of internal demand, but the rate of increase is likely to slacken somewhat during the course of the year.

Expenditure on gross fixed asset formation will increase substantially in the coming months, but towards the end of the year demand from this source is likely to fall off. This applies particularly to capital investment by business firms, with the exception of the steadily increasing investment in the exploitation of natural gas deposits. No doubt the appreciable expansion which lies ahead in the field of industrial building will give some stimulus to capital investment, but the narrowing of profit margins—partly in connection with the strict policy of price control—and the restrictions applied to credit, can be expected to produce a very marked reduction in business liquidity, which may begin to have an influence on effective investment expenditure in the autumn. In house building, demand will again exceed productive capacity, and further progress will depend mainly on the possibility of increasing the labour force and its productivity. Incidentally, in certain areas building permits are being issued with the deliberate aim of achieving a better utilization of available capacity. As a result of the curbs which have been applied, there should be no increase in the rate of growth of public investment expenditure, although this will still run above the level of the corresponding period last year.

There is unlikely to be any appreciable increase in public expenditure on goods and services, since salaries and wages in the public service were increased at the beginning of the year. Moreover, there is to be a cut in some items of military expenditure.

The outlook for private consumers' expenditure, at any rate, is extremely buoyant. There was a further appreciable rise in the total wage bill in April. Another point is that there is normally some delay before the full effect of wage increases is felt on consumers' expenditure. Moreover, the possibility cannot be ruled out that the continued labour shortage and the upward trend of wages in neighbouring countries may cause a resumption of the wage drift towards the end of the year. Finally, the very considerable progress achieved in housing will give a substantial fillip to demand, particularly for durable consumer goods.

Nevertheless, the rate of growth of private consumers' expenditure is likely to slacken somewhat at the end of the year, since practically no official wage increases are due in the second half of the year. Moreover, real expansion of demand will be held back by the increase in prices.

Under the pressure of overall demand, domestic supply will again show a marked increase, in spite of the bottlenecks in productive capacity and manpower which will

continue to be felt until the end of the year. At all events, industrial production should continue to expand briskly up to and including the third quarter of the year. Provided that weather conditions are normal, agricultural production will more than make good the slight setback experienced in 1963.

The labour situation is likely to remain strained, even though, as a result of new regulations for military service, 3 000 conscripts are being released ahead of time between May and July. A slackening in the growth of demand in some sectors, which may possibly be expected towards the end of the year, is unlikely to bring any radical improvement in the imbalance of the economy.

In view of the discrepancy between the increase in nominal overall demand and in domestic supply, imports will increase substantially—possibly more slowly than in the last few months, but certainly more rapidly than exports—and there will again be a perceptible increase in the level of prices, particularly as the substantial increases in costs are pushing prices upwards. Increases may also be expected in the charges made for certain services provided by the public utilities and transport undertakings, particularly the post office. In addition, controlled rents are to be increased on 1 July by from 10 % to 12.5 %, and this alone is likely to send up the cost of living index by more than 1.2 %.

Price increases will continue to be limited, however, by the government policy of direct price control, the scope of which has been increased. In addition, the ban on collective resale price maintenance, which came into force on 15 June, seems likely to intensify competition, particularly in the field of durables, and thus to have some restraining effect on prices.

Assuming that the restrictive monetary and credit policy is maintained, the relative contraction of liquidity (as compared with the increase in the national income) will become more marked during the second half of the year. This tightening of credit will probably become particularly noticeable from the autumn onwards, when tax payments fall due. Hence a further rise in interest rates on the money and capital markets is to be expected.

In regard to the public finances, the revised budget estimates for 1964 assume a much greater increase in revenue (approximately Fl. 1 000 million) than had been originally estimated; this will be achieved mainly as a result of the steeply progressive tax scale and by increases in certain indirect taxes. On the other hand, expenditure is likely to exceed the budget estimates by about Fl. 500 million. The net cash deficit will probably be only Fl. 400 million, instead of the Fl. 1 000 million in the original estimate, although this reduction is partly explained by a correction of the income and expenditure figures for the years 1962 and 1963.

The results of the first half year and the forecasts given here for the period up to the end of the year substantially confirm the estimates made at the end of 1963 for the trend of the main supply and demand components over the whole of 1964. Nevertheless, the growth rate of most of the demand components, and particularly of exports, may be somewhat higher. As, however, the growth of imports must be scaled up, the gross national product is unlikely to exceed the estimated rate of growth of 5.5 % by volume.

As regards developments beyond the end of 1964, the economy is likely to continue to grow, although at a substantially slower pace. If the government is able to prevent another sharp rise in wages, private consumption is likely to increase at a considerably slower rate. It must be added, however, that there is already a proposal before Parliament to raise old age pensions substantially on 1 January 1965, and this could increase consumer demand by a further 1 % or thereabouts.

A falling-off in industrial investment—mainly owing to a considerable slackening in the upward trend of profits in 1964—could produce a certain easing of the labour situation. In this case, the expansion of exports, for which the prospects are extremely favourable in view of world economic trends, might proceed at a faster pace and give rise to a recovery in external equilibrium during the latter part of 1965. On these assumptions—which are still doubtful in many respects—the real gross national product in 1965 might increase by about 3.5 % by comparison with 1964.

There is still a danger, however, that the after-effects of the inflationary tendencies may last for some time. In particular, the possibility cannot be ruled out that the autumn of 1964 will bring a new spate of wage increases for next year which would not only prevent a stabilization of prices, but would also set off a new price spiral, cause a further deterioration in the balance of payments and even give rise to a serious danger of recession.

It is therefore important that the authorities should maintain their policy of economic restraint, and that a total curb on the expansion of internal demand should be applied to produce, by the autumn if possible, a sufficient easing of the labour situation to enable wage increases to be kept under better control. In other words economic policy as a whole must create a climate in which a policy of moderating incomes becomes possible again and has a chance to succeed.

Energetic action in accordance with the recommendation of the EEC Council, issued on 14 April, should suffice to bring the Dutch economy into line with these requirements. In this connection it should be pointed out that the increase in Government expenditure in 1964 by comparison with 1963—mainly as a result of the substantial increase in salaries and wages—will be considerably in excess of the 5 % maximum recommended by the Council of Ministers, despite the curbs which have already been applied to investment expenditure; the increase is likely to be of the order of 10 %. However, as suggested in the recommendation, this can be offset by tax increases such as recent additions to the petrol and tobacco taxes, and by the higher tax revenue yielded from



graduated taxes on growing incomes, in so far as such is real and not inflationary. A rough and provisional calculation indicates that the amount by which expenditure exceeds the recommended rate of increase is only partially "covered" by tax increases as laid down in the recommendations. But the proposed increase in the charges of the public utilities and transport undertakings could bring the financial policy of the Netherlands, in its budgetary aspect, more into line with the recommendations; the extent to which this would occur would depend on the amount of the increases. The financing of the deficit, which will be carried out entirely by means of long-term loans, is in line with the recommendations.

In the sphere of local and quasi-public finance, the position is less clear. However, the obligation of the territorial authorities to finance their capital investment by means of long-term loans was extended in October 1963 by a regulation fixing a maximum limit for the issue of such loans.

In regard to liquidity and credit policy, it has already been pointed out that a very strict line has been followed, supplemented by budgetary policy. It is powerfully supported by the deterioration in the balance of payments. The agreement limiting the expansion of bank credits has been extended; it precludes any further increase in the volume of outstanding credits during the period May to August 1964. In addition, the discount rate was raised on 4 June from 4 % to 4.5 %.

These policies have been supplemented by measures to stimulate competition, which have already been mentioned (the banning of certain vertical price fixing arrangements), and which are fully in line with the recommendations of the Council.

Everything will depend on whether the policy can be maintained in its entirety. In particular, the stiff credit policy must be continued in the autumn of 1964 : whereas the stabilization of total outstanding bank credits from May to August largely followed the seasonal pattern, there will be heavy pressure for a substantial expansion in the following months; there must only be very limited concessions to these demands. In regard to public expenditure, the Government has already announced that it is anxious not to exceed the 5 % maximum in 1965 as recommended by the Council. This seems to be particularly necessary, because the increase in old age pensions by approximately 20 %, which should take effect on 1 January 1965, will tend to increase the growth in public expenditure, the Government's contribution to the increase in pensions being 1 % of the total budget for 1964.

It should be noted that the Government has also announced a reduction in income tax of the order of Fl. 1 000 million, to be introduced by early 1967 at the latest. The first reduction of some Fl. 500 million could take effect on 1 July 1965, provided that the increase in the volume of internal demand in 1965 (by comparison with 1964) is 2 % less than the increase in domestic production. There seems to be little hope that this condition will be fulfilled; in any case its fulfilment would give no guarantee of a restoration of

internal equilibrium, since it is expressed only in terms of volume. At all events, if the tax reductions affect the year 1965, increases in Government expenditure will have to be kept by a corresponding amount below 5 %, in order to comply with the recommendations of the Council.

Finally, if the country is to regain its internal and external equilibrium as rapidly as possible, it would seem to be essential for the policy of wage restraint to be revived in accordance with the recommendations of the Council.

## E. B.L.E.U.

### Belgium

*Economic expansion continued at the faster rate which had prevailed since the autumn of 1963.*

*The previous rather hesitant development of exports gave place to a more rapid increase in the first quarter. There was also a great upsurge in internal demand, particularly in regard to private consumers' expenditure, which had benefited from further substantial increases in personal incomes. Fixed investment also increased.*

*There was a considerable expansion in supply: according to the IRESP index, the annual rate of growth of industrial production in the first quarter was over 11%. Admittedly production trends had been adversely affected by special factors in the corresponding period of last year, but there can be no doubt as to the upward trend. The increase in production was achieved, in spite of some further slight increase in the strains on the labour market, by means of another increase in the volume of employment and, in particular, by a very considerable improvement in productivity. Imports, too, increased more rapidly. The upward trend of prices continued, but the steady rise in the price of industrial products and services was offset by reductions in the prices of a number of agricultural products.*

*There was again a large deficit on the trade balance in the first quarter, and a slight deficit on the balance of current payments. The overall balance of payments, however, showed a surplus, as a result of net gains in public capital transactions. The official gold and foreign currency reserves fell by \$7 million between December 1963 and March 1964, whereas the Banks were able to effect an even greater reduction in their short-term foreign indebtedness.*

*The prospects for an expansion of economic activity in the coming months are good. Exports will again contribute substantially to economic growth. There is unlikely to be any noticeable change in the readiness of managements to invest, but the expansion of building investment—particularly in the public sector—is likely to slacken perceptibly towards the end of the year as a result of the Government's restrictive policy. Finally, there will be a further expansion in private consumers' expenditure, although it may be somewhat less rapid than in the corresponding period of last year.*

*The labour situation is likely to remain strained. In spite of this, industrial production will probably show a further appreciable increase. In all probability, imports will continue to expand at a brisk rate. There are unlikely to be any substan-*

*tial changes in the general trend of prices, which will continue to rise. The outlook beyond the end of 1964—in the light of present assessments—is one of continued economic expansion, although the rate of expansion may be somewhat slower. But in 1965, as in the second half of 1964, it will only be possible to achieve a reasonable state of equilibrium, if the anti-inflationary policy is energetically pursued and even stepped up.*

## 1. Recent developments

The expansion of overall demand, which gained in momentum in the fourth quarter of 1963, continued at a rapid pace in the first quarter of 1964 and, according to the data available so far, in the spring as well.

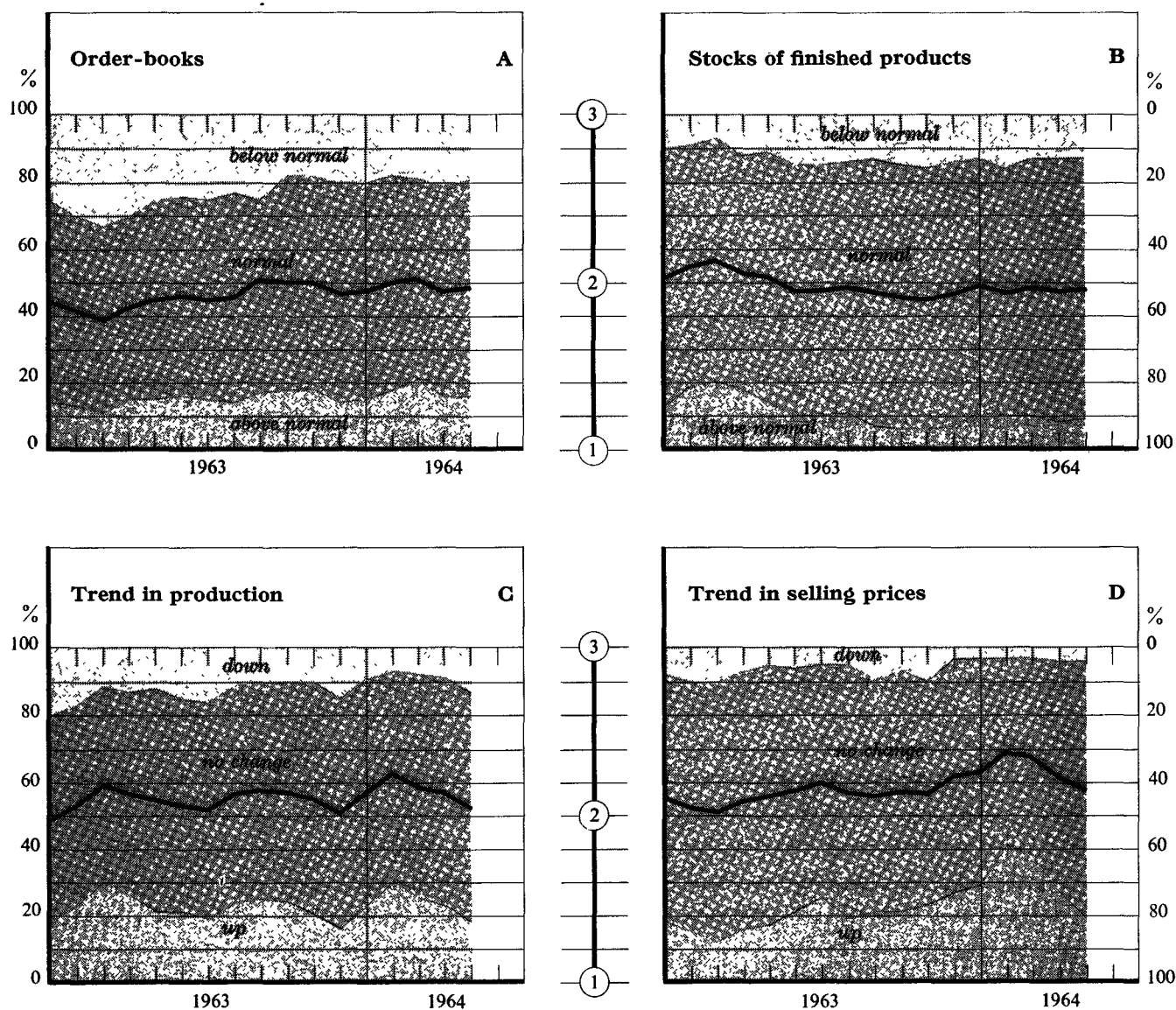
The upward trend in the export of goods and services, which had slackened slightly in the previous quarter, gained somewhat in strength again. The annual rate of increase in the export of goods (value), according to customs returns, was no less than 25.7 % in the first quarter of 1964, compared with 17.9 % in the last three months of 1963. In April, exports exceeded those of the corresponding period of last year by 15.4 %.

This development cannot be explained solely by special factors which held back exports in the early months of 1963; it clearly reflects the more rapid expansion in world demand and a consequent hardening of export prices, particularly for products of the iron and steel industry.

The rise in deliveries to non-member countries, which had been noticeable since the middle of 1963, continued, and resulted for the first quarter in a level of deliveries 19.6 % higher than that of the corresponding period of last year. Sales to non-member countries showed an annual rate of growth of 27.6 %.

There was also a marked upward trend in internal demand. Expenditure on gross fixed asset formation again increased perceptibly. This was probably due firstly to a further increase in capital equipment investment on the part of business undertakings, particularly as a result of intensified efforts to improve efficiency, and secondly to the further substantial increase in capital expenditure on building, thanks to favourable weather conditions in the first quarter. It therefore seems that the measures adopted since the end of 1963 to restrict investment expenditure have not yet had any noticeable influence on the trend of effective expenditure. This applies mainly to capital investment in the public sector, particularly that of the local authorities, which again rose perceptibly in the first quarter. However, a check has been placed on new appropriations for public works.

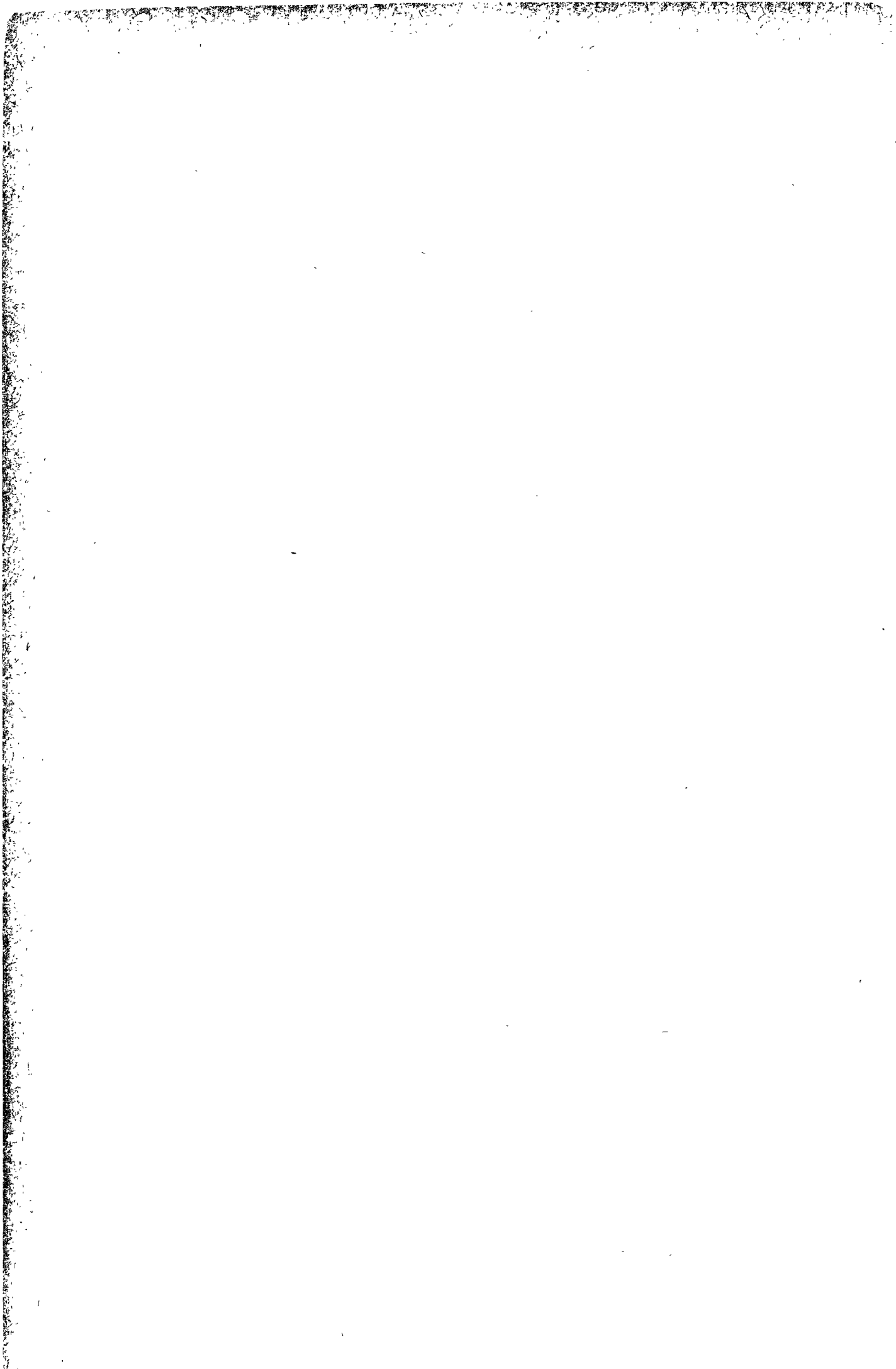
BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to the questions of the EEC business survey, carried out in Belgium by the National Bank.

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

- by 0.03 for the answer "above normal", or "up";
- by 0.02 for the answer "normal", or "no change";
- by 0.01 for the answer "below normal", or "down".



As regards investments in stocks, the vigorous build-up of stocks of raw materials and semi-finished goods appears to have persisted.

Consumption expenditure again expanded considerably, though certainly not at a faster rate, at least in the first quarter. The total of public current expenditure on goods and services continued to expand. But the most marked feature was the continuance of the very rapid rate of growth of private consumers' expenditure. There was a real increase in disposable incomes of private households during the period, due mainly to a further increase in the total wage and salary bill, resulting from steep wage rises and continued expansion in employment. Increases in wages and salaries were partly influenced by the fact that the rise in the general retail price index since the beginning of the year had resulted in additional increases in income owing to the operation of sliding wage scales in most sectors. Lastly, transfer income was up, largely owing to an increase in family allowances effective from the 1 April.

The measures taken with effect from 7 March 1964 to curb hire purchase credit did not have any obvious effects during the first quarter. At all events, more than 40 % more new private cars were sold than during the same period in the previous year, though the rate of increase was only 11 % in April.

The vigorous growth of demand evoked a strong increase in domestic production, which is all the more remarkable in that there is a definite shortage of labour in many sectors. Lastly, growth of industrial production, though somewhat slower than in the fourth quarter of 1963, was largely due to increased productivity. In the first quarter of 1964, the annual rate of growth was over 11 % (according to the IRESP Index which is not seasonally adjusted) over the corresponding period for the previous year, compared with a year-to-year growth rate of 8.3 % in the preceding quarter. The largest increase in output took place in the iron, steel and building materials industries.

The labour market continued to show many signs of strain. For instance, the number of fully unemployed persons fell to 26 300 in April compared with 33 500 for the same month in 1963. The ratio of unemployment (the relation between the total number of unemployed and the number of employees registered for unemployment insurance) reached 1.8 % in April compared with 2.3 % in the previous April.

Not only internal demand but also imports of goods and services showed a very definite tendency to expand during the first quarter of 1964. According to customs returns, imports of goods were valued at more than 25.4 % above the figure for the corresponding period of last year (foreign trade figures by volume are not yet available for the first quarter); this, however, to some extent reflects the very low level of the previous year. In the last three months of 1963 the annual rate of growth was 13.7 %.

Apart from reductions in the prices of some foodstuffs, due either to seasonal factors or to the fact that special circumstances had previously forced them up artificially,

the steady upward trend of prices continued. The retail price index, which hardly rose at all between December and March, rose by 0.5 % in April and by a further 0.3 % in May. This gave an average rate of increase of 3.4 % for the first five months in 1964 compared with the same period of last year. At the wholesale level the prices of finished goods, in contrast to those of other products, rose more sharply. Having risen by 1.2 % between September and December 1963, they rose by 2.5 % between December and March.

The trade balance again showed a considerable deficit in the first quarter : according to customs returns, this amounted to Bfrs. 3 800 million compared with 3 200 million in both the first and fourth quarters of 1963. Net receipts from services only partly made up for the deficit on visible trade. On the other hand, there was probably a surplus on capital account, since imports of foreign capital by the public sector (local authorities and semi-public institutions rather than central government) were exceeded by net exports of private capital. The overall balance of payments appears to have been slightly on the credit side; while official reserves of gold and foreign currency decreased by \$7 million during the period under review, the net foreign exchange position of the commercial banks showed a noticeable improvement.

*Supply and utilization of goods and services*

	1962 <sup>(2)</sup>	1962 <sup>(2)</sup>	1963 <sup>(3)</sup>	1964 <sup>(4)</sup>
	At current prices (in Bfrs. '000 million)	% variation by volume on preceding year		
Gross national product	637.2	3.8	4.0	4.5
Imports <sup>(1)</sup>	229.8	8.4	12.5	11.5
Private consumption	432.8	4.0	4.5	4.5
Public current expenditure	79.5	6.0	5.0	3.5
Gross fixed asset formation	121.7	1.6	3.5	5.5
Exports <sup>(1)</sup>	231.4	8.9	9.5	9.5

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> General Bulletin of Statistics 1963, No. 12, Statistical Office of the European Communities.

<sup>(3)</sup> Commission estimates.

<sup>(4)</sup> Commission forecasts.

*Note* : The forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts from the member countries, but are established and published on the sole responsibility of the Commission.



Notwithstanding the agreement reached between the National Bank and the Commercial Banks to limit the expansion of credit in 1964, a persistent and very rapid increase in short-term credits was apparent in the money and capital markets. The rise in interest rates appears to have practically ceased since February, at least until April, after reaching a level representing a substantial shift of the pre-deducted tax on securities introduced at the beginning of 1963, to borrowers. In consequence, public issues—a Government loan in February and a "Fonds des routes" in April—were markedly successful for the first time since the tax reform measures were passed. The money market, however, again showed signs of strain, which obliged the authorities to abolish the upper limit (which had been the same as Bank rate) on rates of interest for short-term Treasury Bonds from March onwards.

## 2. Outlook

Judging by present indications, the economy will continue to expand during the remainder of 1964.

Undoubtedly the most potent factor in stimulating economic growth will be external demand (meaning effective exports of goods and services). Answers to the last EEC questionnaire on business prospects indicate that the upward movement of orders from abroad is continuing. Even if Belgium's competitive position should worsen slightly owing to the upward trend of wage costs per unit of production observable over the last year, this is unlikely to affect the export figures within the period we are considering. Even though internal demand continues to expand rapidly, this is unlikely to have a perceptible braking effect on total exports owing to the very marked improvement in sales prospects for several important items exported from Belgium, including iron and steel, especially as the industries concerned still have considerable elasticity of supply. Moreover, the drive which has been under way for some time to expand sales in non-member countries as well is likely to help in keeping exports buoyant.

Gross fixed asset formation should also continue to stimulate expansion, though this is less true of investment in building, the growth of which is likely to be largely inhibited during the second half of the year, since the authorities are continuing their stabilization drive, especially in regard to public works and private housing construction. Therefore any advance in the total of fixed asset formation will be increasingly dependent on business investment, and the prospects for expansion appear extremely good in this sector, especially for capital equipment investment. New orders received by the Belgian industries concerned, and the results of the last inquiry on investment carried out by the National Bank, confirm the probability of such a trend, which would also be in line with

the continuing lively interest in investment for rationalization purposes. However, the restrictive credit policy and the increasingly sparing use made of the laws of 1959 for reviving economic activity will have some braking effect.

Publics current expenditure on goods and services will probably increase, though at an appreciably slower rate than in 1963. Private consumers' expenditure on the other hand, is likely to be an important factor in boosting total internal demand. The tendency for private incomes to increase appears to be as strong as ever. Not only will employment continue to rise, but actual hourly earnings will show an appreciable increase, due largely to the shortage of labour and competition among employers for labour. Furthermore, the probable trend of prices is bound to lead to renewed increases in wages and salaries based on sliding wage scales. Lastly, from October onwards, some family allowances will be raised.

The labour situation will remain tight, though any further accentuation of the imbalance is unlikely, since there may be some slackening in the building industry.

Agricultural production, which decreased slightly in 1963, will, in 1964, more than make good these output losses, given normal weather. Although labour shortages will again have some restrictive effect in certain branches of industry, total industrial production will show a further increase, largely due to a rise in productivity, though the rate of increase may be slower than in recent months.

It is likely that imports will also increase during the coming months at about the same rate as exports. One reason for this is that the elements of demand likely to be most affected by restrictive policies have only a very small effect on imports. Therefore, the trade balance may well show a heavier deficit than in 1963.

With regard to the probable trend of prices, it may be noted that, although the vigorous upswing at the production stage in industry observable towards the end of 1963 and at the beginning of 1964 appears to have slowed down somewhat, this change has not yet worked its way through to the retail trade, where further price rises are to be expected. Moreover production costs, which had temporarily levelled off somewhat owing to the large increase in production and productivity, will again move more strongly upwards, helped by the increasingly noticeable rises in prices of raw materials and semi-manufactures.

The latest trends in the economy and the prospects for the coming months necessitate some slight corrections to the forecasts of volume changes of the most important supply and demand items for the whole of 1964 which were made at the end of 1963 and in Quarterly

Survey 1/1964. External demand, in particular, has increased more than was expected. Gross national product should increase by rather more than 4.5 % instead of approximately 4 % as seemed likely hitherto.

In so far as it is possible to forecast with any degree of certainty the way in which the economy may develop after the end of 1964—i.e. in 1965—it appears likely that the expansionary tendencies will continue. This is confirmed by preliminary estimates concerning developments in important markets for Belgian products both inside the Community and, as far as they are known, outside it. Exports may indeed increase at a slower rate, partly because the limits of capacity will be reached in a number of sectors and internal demand will exert greater pressure, but also because it is questionable whether the exceptional market conditions for a number of important export products (steel, for instance) will improve still further. The prospects for investment are less certain, though it is entirely possible that the upswing in business investment will continue into 1965 long enough to have a decisive effect on the year's results. On the other hand, if present policies are continued, public investment is unlikely to expand—and this would have a very desirable compensating effect, particularly from the standpoint of Short-term economic policy. For there is no apparent reason to conclude that private consumers' expenditure will not continue to expand. Even if the expansion is somewhat slower than at present, the signs are that it will still be considerable.

If demand develops according to these indications, then—always assuming that weather conditions remain normal — an increase in the gross national product of the order of between 3.5 % and 4 % during 1965 over 1964 appears entirely possible.

But these developments will remain more or less in balance, only if the authorities responsible for economic policy in Belgium energetically pursue the anti-inflationary policy already introduced. This would also accord with the recommendations of the Council of the Community issued on 14 April.

There are some indications that public expenditure (or at least Government expenditure) for 1964 may only slightly exceed the growth rate of 5 % set by the Council of Ministers on 14 April: Government departments have exercised strong restraint in placing orders for public works since November 1963, the effect of which should be seen in expenditure from the middle of 1964 onwards. Even in the first quarter, the annual rate of growth of budgetary expenditure amounted to only 3.5 %, largely owing to a slower rise in extraordinary expenditure, while increased charges for certain public services have already been approved (e.g. the rise in railway fares from the 1 April) or put into effect (telephone charges). The increase in the charges for public services deserves mention here, because the growth of receipts it entails, together with, for example, increased receipts due to the progression in certain taxes, has to be brought into calculation of the effective rate of increase of public expenditure.

In view of this trend in budgetary receipts, it should not be too difficult to limit the planned increase of Government expenditure for 1965 to 5 %.

Information about the pattern of expenditure of the territorial authorities is not so reliable. Notwithstanding certain measures taken by the Government, particularly the limitation of investment by those organs of the administration, their total expenditure may possibly exceed the coefficient laid down by the Council of Ministers. There is therefore a need for increased efforts in this sphere.

Moreover, it appears generally speaking desirable to channel the policy of economy in the use of public funds more to transfer and consumption payments, instead of limiting it mainly to investment expenditure.

With regard to the financing of the budget deficit, information so far available indicates that the deficit for 1964 will be covered exclusively on the capital market. Nevertheless, it appears by no means certain that there will be no further recourse, even if only temporarily, to foreign credit. That should be avoided at all costs. In view of the predictable extension of private demand for long-term finance, it appears desirable and indeed essential to make further efforts to increase the efficiency of the capital market, especially by improving its structure in order to achieve a closer harmony between the supply of savings and the demand for funds.

In the sphere of credit policy, it was made known at the end of January that the expansion of bank credits in 1964 is to be limited to approximately 10 % to 12 % by comparison with the average for 1963, following an actual increase of 24 % in 1963 over 1962. But these efforts do not appear so far to have been fully successful. It may become necessary, as in other countries such as France and the Netherlands, to introduce stricter regulations, possibly in the form of an agreement between the Central Bank and the commercial banks, incorporating sanctions and hence guaranteeing strict compliance with the limits laid down.

In any event, credit policy will have to take a more definitely restrictive line before long, if effective counter-action is to be taken against the upward trend of prices and production costs. Such measures might well be selective, favouring credits for rationalization investment programmes at the expense of short-term trading capital.

As mentioned above, this restrictive credit policy has been supplemented by a tightening-up of the hire purchase regulations. It appears, however, that there are still some loopholes in these regulations, and it would therefore undoubtedly be expedient to pass the parliamentary bill dealing with new regulations for small credits to consumers as quickly as possible.

Furthermore, in the framework of an incomes policy the responsible authorities should pay increased attention to the need to keep the trend of incomes in line with the objectives of price policy. The speedy introduction of measures for improving the price mechanism by prohibiting restraint of competition would also constitute a useful step towards price stabilization.

## Grand Duchy of Luxembourg

*The improvement in world market conditions for iron and steel has made the Luxembourg economy distinctly more expansive since the end of 1963. Internal supplies of goods and services increased owing to the revival of exports and the accelerated growth of internal demand arising from a relatively rapid expansion of private consumption. Whereas in the last quarter of 1963 industrial production was up by only 1 % on the corresponding period in the preceding year, in the first quarter of 1964 it reached an annual growth rate of 9.6 %—partly, however, due to the effects of special factors in the previous year.*

*Demand will continue to increase in the second half of the year, when the indirect effects of the fresh rise in exports should be fully felt in the growth of internal demand. The gross national product should probably rise by about 4.5 % in volume during 1964 (compared with only 0.5 % in 1963) and there should be a noticeable improvement in the terms of trade. It is however likely that these developments will result in a continuation of the tight labour situation, possibly leading to a tendency for prices to rise. To combat this, the stabilization policy will have to be continued and intensified.*

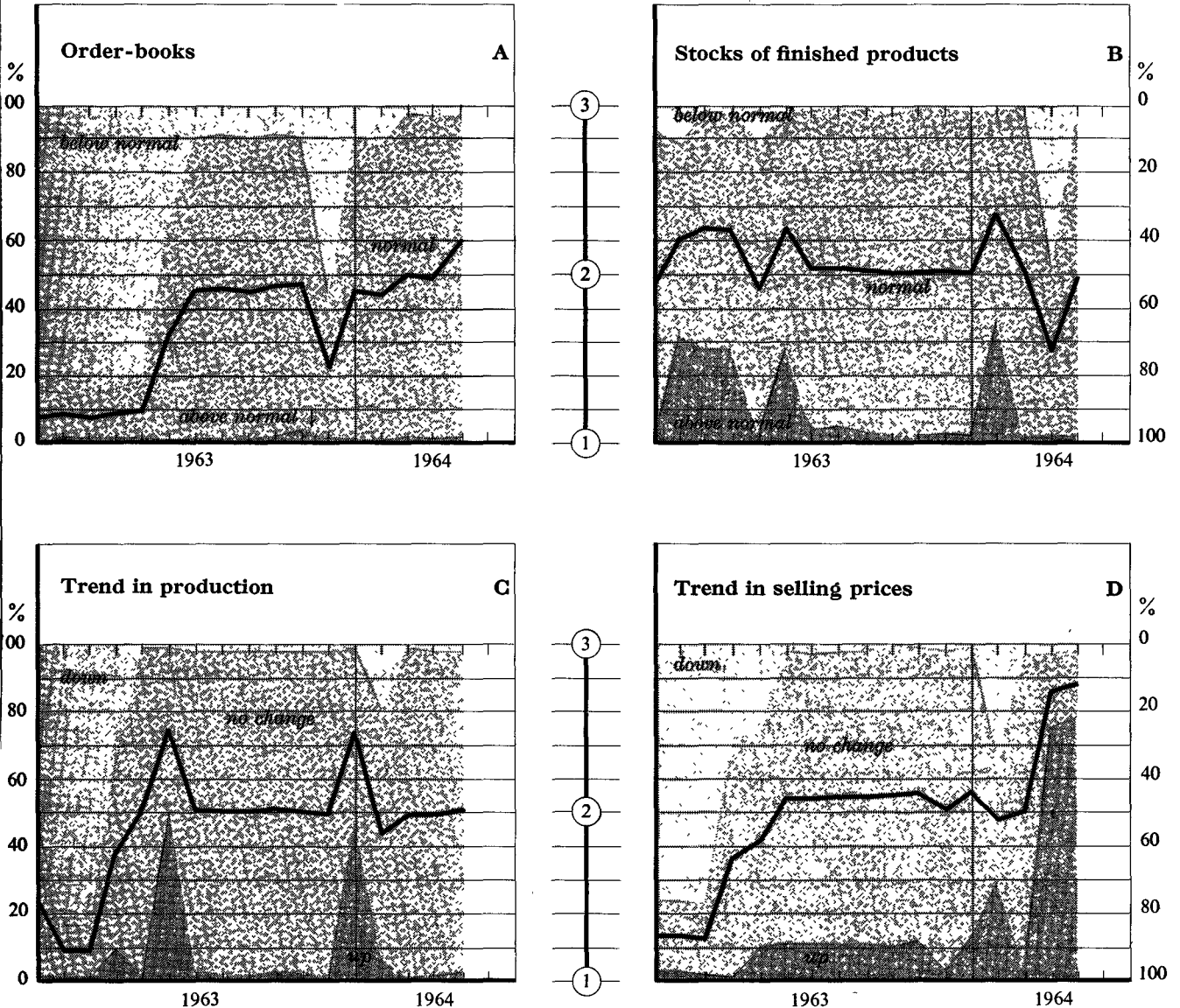
### 1. Recent developments

The improved world marketing situation for iron and steel had a decisive influence on the development of Luxembourg's economy in the first quarter of 1964.

External demand, which revived only slightly between the third and fourth quarters of 1963, has made an increasing contribution to economic growth since the beginning of the year. This is reflected in exports of iron and steel products alone, which greatly exceeded in volume those for the first quarter of 1963. The increasing firmness of volume sales of iron and steel products had its effect on prices; there was probably an appreciable increase in the export prices for iron and steel products over those for the previous year.

There was a definite expansion in gross fixed asset formation, largely due to increased investment in building. The index of hours worked in the building industry for the first quarter was more than 30 % higher than in the same period of last year, though that was partly due to the restraining effect of the unusually bad weather conditions then prevailing. Public investment, in particular, rose relatively steeply, owing to increased contributions from the Special Fund. Iron and steel enterprises also appear to have recovered their readiness to invest.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to the questions of the EEC business survey, carried out in Grand Duchy of Luxembourg by STATEC.

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

- by 0.03 for the answer "above normal", or "up";
- by 0.02 for the answer "normal", or "no change";
- by 0.01 for the answer "below normal", or "down".





The very rapid increase in consumption expenditure appears to have continued. As regards public current expenditure on goods and services, there was an appreciable rise in the salaries of public servants from the end of 1963 onwards, in addition to which the backdated salary increases from 1963 were paid to public servants in the first quarter of 1964. A rise in private incomes, the key to the growth of private consumers' expenditure, was also linked in the first quarter to an increase in employment and to higher production bonuses in industry.

Industrial production expanded at a faster rate, largely influenced by the revival in the export goods industries and the building industry. According to the national index, the annual rate of growth achieved in the first quarter was 9.6 % compared with 1 % growth for the previous quarter and for the whole of 1963. Production in the iron and steel industry alone exceeded the level for the corresponding period in the previous year by 10.8 %, after registering a slight decline in the fourth quarter of 1963. The production increases were largely due to higher productivity.

Whereas the number of workers employed in industry throughout 1963 was lower than for 1962, the situation has changed since the end of 1963. In the first quarter of 1964 there was an increase of 3.2 % over the same period for 1963, and the numbers employed were somewhat higher than for the corresponding quarter in 1962.

There was a considerable rise in imports, mainly due to the substantial increase in purchases of consumer goods and raw materials.

The favourable influence of weather conditions in the winter of 1963/64 on the level of agricultural prices resulted in the cost of living index rising only moderately in the first quarter, the annual rate of growth being 3.9 %, the same as in the last quarter of 1963. In April it advanced by as much as 4.1 % compared with 1963.

## 2. Outlook

It is likely that considerable expansion will take place over the coming months. Visible exports will again increase markedly under the influence of the improved world markets for iron and steel. New foreign orders have been increasing steadily and very considerably since the end of 1963. There may have been some slackening in restocking of iron and steel products by the processing industries, which had been one of the factors contributing to the revival of demand, but the general business situation in the investment goods and automobile industries in countries representing important markets for Luxembourg will no doubt result in a continued flow of orders.

The export of products other than iron and steel will also undoubtedly increase faster than last year.

Gross fixed asset formation may increase once more. True, the volume of government orders will not increase, and expansion in the building industry will be held in check by the continuing shortage of labour; but on the other hand there seems to be a renewed investment-mindedness in the iron and steel industry. Some producers even estimate that average investment for 1964 will be greater than that for 1963. Investment by the new undertakings will also give an impetus to expansion.

Private consumers' expenditure is also likely to increase. Incomes of private households will continue to grow from the middle of the year, because of increased employment, increases in hourly rates of pay and the operation of the sliding scale of wages. Moreover, a bill was passed in May providing for an increase in old age pensions, as a result of which these payments may total some 400 million francs more in 1964 than in 1963.

This prospective pattern of demand will undoubtedly lead to a renewed expansion of industrial production, even though the shortage of labour in certain branches of industry will continue as an inhibiting factor.

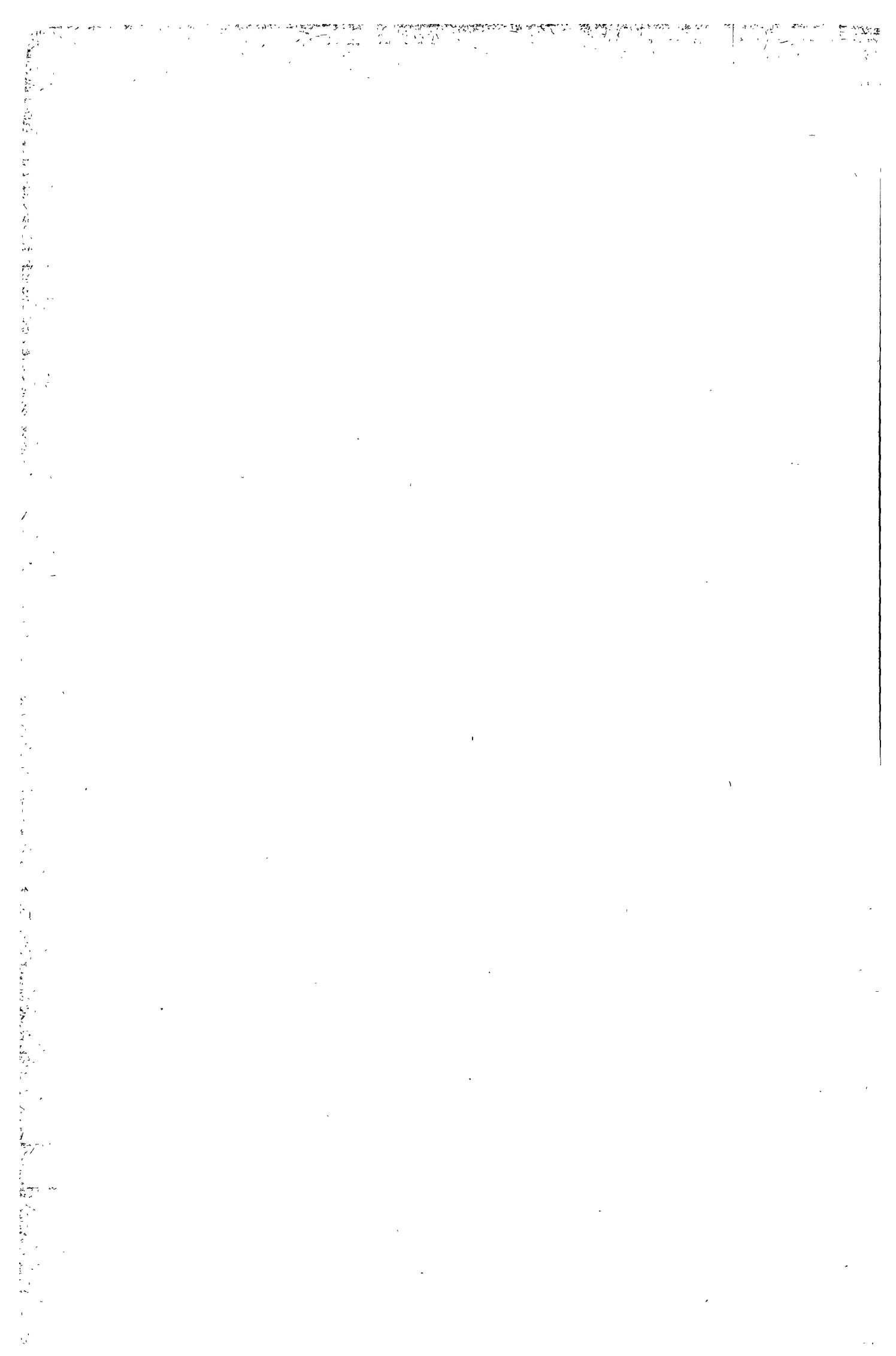
All in all, it can now be assumed that gross national product might increase by about 4.5 % in 1964 over 1963—after a growth rate of only 0.5 % from 1962 to 1963.

It is fairly certain that the fresh speeding up of the economy will tend to raise prices. Furthermore, the price level will probably be driven upwards by an increase in turnover tax and other indirect taxes; the object of these tax increases—some already in effect and others contemplated—is to finance the improvement in old age pension rates. Lastly, the tight labour situation makes it certain that wage costs will rise more quickly. In the climate of economic expansion it should not be too difficult to pass on the cost increases.

Since Luxembourg still largely depends upon a single industry, and on the world economic situation for the product of that industry, it is hardly possible to forecast the way in which the country's economy will develop in 1965. But there are certain to be some continuing strains, if only as a result of the upswing in exports during 1964.

This being so, it is important that the anti-inflationary policy begun by the Luxembourg government in 1963 should be pursued, and that effect should be given to the recommendations made by the Council of Ministers of the Community on 14 April 1964.

In this connection it may be pointed out that the government has already increased some taxes. Even if turnover tax were to be raised as planned, the amount by which public expenditure exceeds the maximum increase of 5 % over 1963 recommended by the Council of Ministers would be fully covered within the meaning of those recommendations. But the 5 % limit may be exceeded, owing to the increase of wages and salaries for public servants and nationalised concerns, together with the effect of the sliding wage scale from mid-year onwards and the increase in old age pensions mentioned above. It is strongly to be recommended that public expenditure should really be effectively curbed in 1965, and held within a 5 % increase.



## Trends of wages, productivity and labour costs in industry

As in previous years (Annexes to Quarterly Surveys 2/1962 and 1/1963) the trend of labour costs and production (understood as net production) per paid employee, labour costs per unit of product and prices in industry (including the building industry) in member countries and in some important non-member countries are shown in the following pages in chart form.

The Commission is continuing this series of charts, because it is convinced that they contain important statistical data, which it is essential to place in the hands both of political economists and the general public. The fact that, owing to the lack of the necessary statistics on cost structure and profits, it is not possible to provide similar charts and figures for other cost elements (indirect taxes, social insurance contributions, etc.) and on the gross and net earnings of industry, is no reason for withholding such information as is available or can be calculated regarding one element in costs—indeed, the largest one.

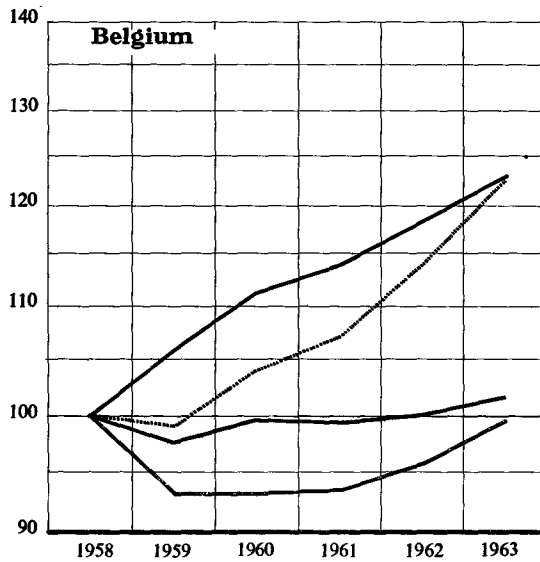
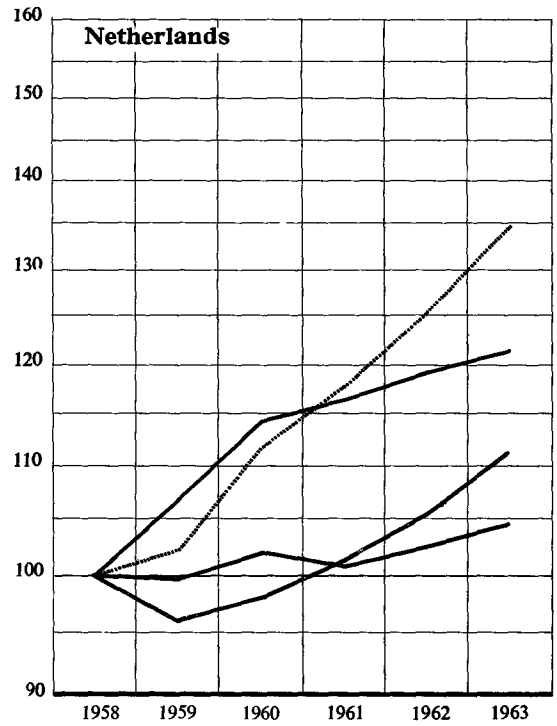
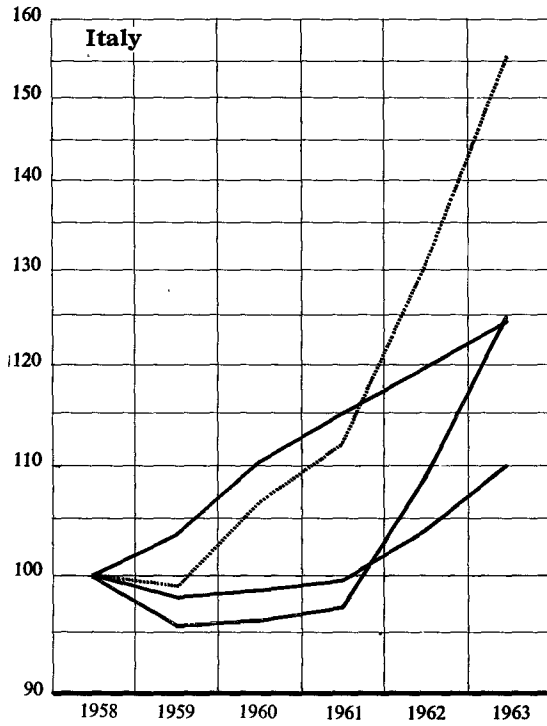
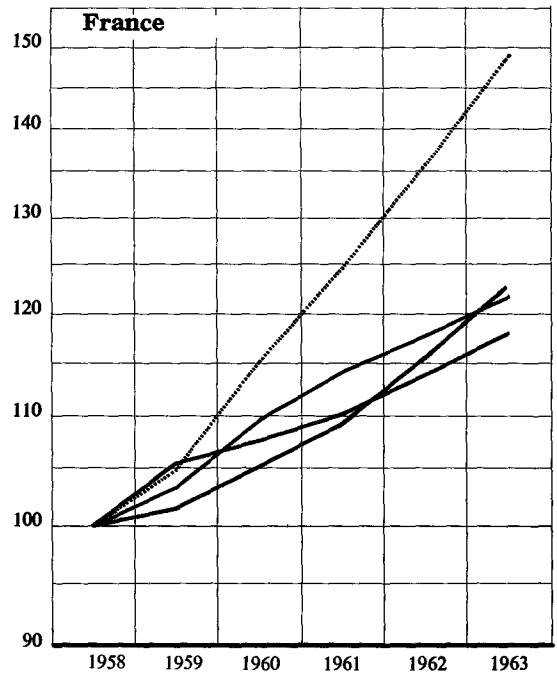
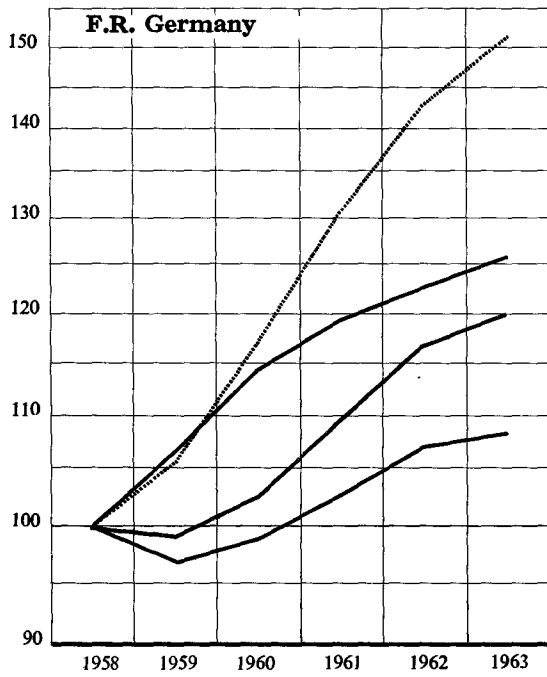
For the definitions and methods of calculation used, the reader is referred to the explanations in the annexes to Quarterly Surveys Nos. 1/1963 and 2/1962. Suffice it to recall here that statistical information has been taken as far as possible from overall national economic statistics. It must also be emphasised again, to avoid misunderstandings, that the charts only show the actual development of wages and salaries, "labour productivity", labour costs per unit of product, and prices, and do not enable conclusions to be drawn as to the reason for these movements. For example, the trend of labour costs per unit of product is purely an arithmetical calculation from the trend of labour costs on the one hand and of production per paid employee on the other.

The graphs are based on the latest available figures, some of which have been corrected; data for 1963 in particular is still only provisional, some of it even being estimates made by the Commission.

The curves are based on indices, and this time the base year is 1958. This was done partly to bring the figures into line with most of the other general indices published by the Statistical Office of the European Communities, and partly because of the special interest attaching to developments over the last few years. For developments during the period 1954-58, the reader is again referred to Quarterly Survey No. 1/1963.

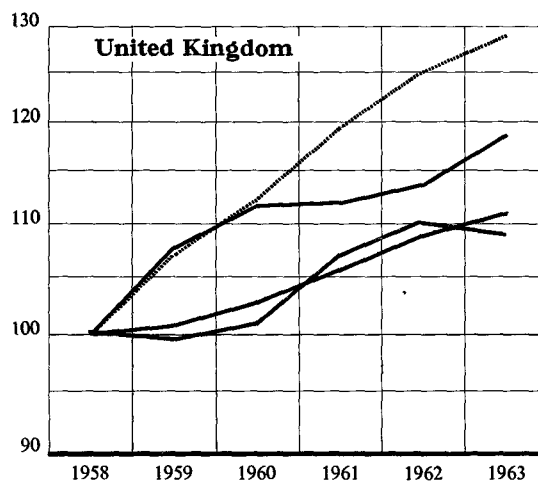
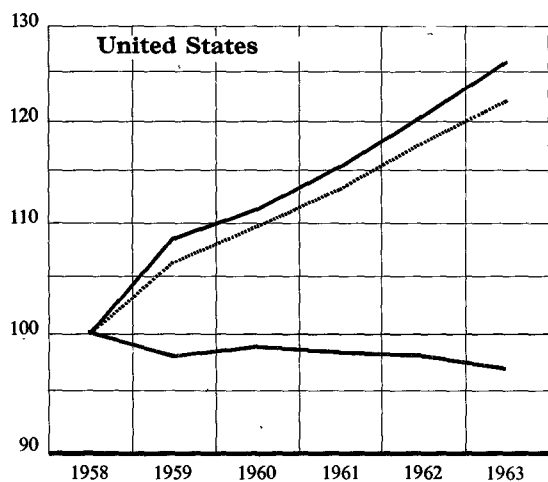
# WAGES, PRODUCTIVITY AND WAGE COSTS IN INDUSTRY

1958 = 100



# WAGES, PRODUCTIVITY AND WAGE COSTS IN INDUSTRY

1958 = 100



- *Product per head (by volume)*
- ..... *Total wages per head (in national currencies)*
- *Wage costs per unit of product (in national currencies)*
- *Implicit price index (in national currencies)*

*Semi-logarithmic scale*

In the nature of things, the curves show only the trend in each country during the period considered; they therefore give a comparison of the changes, but not an inter-country comparison of the respective levels. The curves are based on calculations in national currencies; and since there have been some alterations in exchange rates since 1958, this should be borne in mind when making certain comparisons.

The tendency for labour costs per unit of product to rise continued during 1963, again contrary to the trend in the United States and the United Kingdom, where the increment in labour costs did not outrun the increase in "labour productivity" (4.5 % in both cases). A slowing-down was noticeable in the Federal Republic; this slackening tendency was more evident in the second half-year than in the first, though the graphs do not bring this out. Being based on yearly averages, they show the trend from one year to another, but not the movement within a given year. The trend in Italy is particularly striking; there labour costs per paid employee and per unit of product have risen very steeply in the last two years.

Production per employee increased by about 3 % in the Community between 1962 and 1963, with very little variation between different countries. On the other hand, there were wide variations in wage and salary increases, which amounted to 6 %—7 % in the Federal Republic of Germany, the Netherlands and Belgium, 10 % in France and nearly 20 % in Italy.

It is expected that labour costs will rise more slowly in the Community during 1964, owing to a slowing-down in Italy and France, while production per employee may rise somewhat more quickly. This could lead to some slackening of the upward pressure on the level of labour costs per unit of product in the Community. But the slowing-down may not amount to much, in view of the fact that a rise of more than 15 % in the average level of wages has caused costs per unit of product to increase more rapidly in the Netherlands, and that costs are likely to rise in Belgium during 1964 at least as quickly as in 1963. Notwithstanding the expected cooling off in Italy, it is probable that costs will increase there at a higher rate than in any other member country, except perhaps the Netherlands.



EUROPEAN ECONOMIC  
COMMUNITY

—  
The Council

**Recommendation from the Council  
of the European Economic Community  
to Member States under Article 103 of the Treaty,  
for measures to be taken to restore the internal  
and external economic equilibrium of the Community**

Brussels, 14 April 1964

The Council, under Article 103 of the Treaty establishing the European Economic Community, having regard to the resolution of the Assembly dated 23 March 1964, on the proposal of the Commission, recommends Member States to take the following measures to restore internal and external economic equilibrium of the Community.

1. Member States are recommended to follow the economic and financial policy necessary to ensure that, not later than the end of 1964, the stability of price levels and unit production costs is restored or consolidated. Measures of economic and financial policy planned or taken in 1964 but which do not become effective until 1965 should be governed by these same aims.
2. To this end the Governments of Member States should, during the coming months, give the aims set out in paragraph 1 priority over all other aims of economic policy or policy in other spheres.
3. Member States should regard the maintenance of a liberal import policy, both within the Community and in relation to non-member countries, as an essential factor in their policy of stabilizing price levels or maintaining their stability.
4. Speedy action to stabilize costs and prices should be primarily based on a more stringent policy towards public expenditure. Member States are recommended to limit the expansion of Treasury disbursements of all kinds which take effect within the country

so that the gross expansion from one year to another does not, so far as possible, exceed a rate of 5 %, regardless of any changes which may rise from methods of financing the public debt. So far as their Constitution permits, Member States should ensure that, on the whole, regional and local authorities and State or semi-State undertakings follow the same course. Where this is not possible, the Governments of Member States are recommended to make every possible effort to ensure by negotiation that such local authorities and undertakings adopt a similar attitude.

Member States are further recommended to take appropriate action to spread public expenditure, so as to avoid excessive concentration of spending in any given period of the year or in any specific area.

5. Where the Governments of Member States are unable, for legal or administrative reasons, to limit the growth of Treasury disbursements to 5 % per annum, or where they are unable to obtain the necessary decisions from their Parliaments early enough, or where the Governments themselves regard a larger increase in expenditure as absolutely essential, they are recommended to supplement their budgetary action by immediate fiscal action designed temporarily to increase existing taxation or to create new taxes, so as to influence the expansion of internal demand in monetary terms as though the rule in paragraph 4 were strictly applied.

Any increased revenue yielded because certain taxes are graduated could be regarded as increased taxation within the meaning of this paragraph. The yield of increased or new taxes should be calculated on the basis of stable prices and of an increase in internal production not exceeding 5 %. The above recommendation is no bar to certain adjustments to existing tax systems, provided that the overall effect is not changed.

The Governments of Member States are recommended, so far as possible, to reduce the deficit of public undertakings by raising the relevant rates, subject to special measures for the benefit of the less-favoured classes of the community. The proceeds of such increase may be regarded as increased taxation within the meaning of the present paragraph.

The creation or increase of taxes and the increase of public utility rates should be selected in the light of sliding scale clauses and indexing clauses in force in each member country so as not to accentuate the upward movement of money incomes. It would be desirable in France and Italy to deploy any increase in taxation in such a way that it mainly tends to slow down the expansion in private consumption and affects industrial investment as little as possible.

6. If, in spite of the application of the provisions referred to in paragraphs 4 and 5, there is still a deficit between Treasury income and expenditure, the Governments of Member States are recommended to finance this deficit solely by the issue of long-term

loans and to refrain from recourse to bank credits, including credits from the Central Bank, or to the issue of short-term Treasury bonds or direct or indirect credits in foreign currency. If the Treasury cannot obtain the necessary capital on the domestic capital market, Governments should immediately take all necessary action to improve the operation of that market. They should, further, administer their public debt in such a way as to ensure greater consolidation.

7. The measures taken by the competent authorities of Member States to implement a restrictive credit policy should be maintained and, where necessary, strengthened. This applies equally to measures designed to limit consumer credit.

8. Governments of Member States are recommended to explain to the representatives of the main economic and social groups, and especially to management and labour, the imperative requirements and essential principles of their stabilization policy. They should endeavour, in negotiations with these groups, to ensure the implementation for the rest of 1964 and the whole of 1965, of an incomes policy which, so far as possible, ensures that the increase in money income per member of the working population keeps in step with the increase in the percentage of real national product per member of the working population.

At the same time closer supervision is needed of markets on which competition is not perfect and the campaign against such restrictions on competition as inflate prices should be stepped up. If action in the sphere of incomes and competition fails to achieve the desired results, measures designed to check the overall expansion of internal demand should be strengthened.

9. In all Member States where the increase in the demand for building exceeds capacity (and in this connection an increase in building prices substantially exceeding the increase in the general price level of other goods and services should be regarded as a warning not to be ignored) and where building capacity cannot be increased fast enough, Governments should resort to special measures of restriction including, inter alia, a reduction in the direct demand for building by the public authorities, a reduction in the tax advantages, subsidies and bounties granted, limitation on mortgage credit and a temporary ban on luxury building. In countries where there is a shortage of school premises, hospitals or housing for the poor, building in these categories should, however, not be restricted or made more difficult.

10. Member States with a balance-of-payments deficit are recommended, so far as they do not finance it from their own gold and foreign exchange reserves, to reach agreement with other Member States within the Community's Monetary Committee on ways and

means of financing this deficit. In view of the close solidarity between Member States within the Community, it is desirable that reliance should primarily be placed for this purpose on Community solutions and in particular on the mutual aid which Member States can render each other in conditions to be determined by common agreement. The Commission will, should the need arise, recommend the introduction of mutual aid.

11. The Government of the Italian Republic is recommended to amplify the overall programme of anti-inflationary measures already adopted, so as to stabilize internal prices and costs without delay and to strengthen Italy's power to compete and its balance of payments. It is particularly desirable that the financial objective should be attained not later than the second half of 1964.

In general it is recommended that tax weapons be used to moderate the expansion of internal demand, that the policy of restricting the expansion of credit should be continued and that a balanced incomes policy should be introduced.

12. In the case of the French Republic, the Kingdom of the Netherlands, the Kingdom of Belgium and the Grand Duchy of Luxembourg, the pursuit of the policy recommended in general to all Member States and already embarked upon should be enough to ensure the return to stability.

13. In the case of the Federal Republic of Germany, where relative stability of prices and production costs was established in 1963, and in order to ensure that it is not jeopardized, it is recommended that the policy already initiated along the lines of the recommendations laid down in paragraphs 1 to 9 should be continued.

There is manifestly no need to tighten up credit policy under present circumstances, but it is nevertheless desirable to avoid any marked speeding up in the expansion of bank credits.

It is recommended that the policy already adopted should be continued, aimed at neutralizing the inflow of liquidities resulting from the balance-of-payments surplus and that efforts should be made to re-export these liquidities. Fiscal or other obstacles to the export of capital, and especially those which result from restrictions on the investments of institutions which provide capital, should be rapidly eliminated.

In addition, measures should be taken to slow down the increase in the surplus on the balance of current transactions. All suitable action should be taken to encourage imports and to avoid anything which might stimulate the expansion of exports. Full advantage should be taken of the opportunities for cutting customs duties ahead of schedule afforded by Article 15(2) of the Treaty; similarly, where German duties exceed

the common customs duties, the difference should be reduced or eliminated. It is further recommended that imports of agricultural products should be encouraged by all appropriate means. Finally, action should be taken to make exports of German capital less dependent upon deliveries of goods and services by the Federal Republic of Germany and to place more Government orders abroad.

14. Member States shall inform the Commission within two months of the action taken to implement this recommendation. The Commission, after consulting, so far as possible, the Economic Policy Committee and the Monetary Committee, will report to the Council and will keep it regularly informed of the situation and of developments. If necessary, it will submit further proposals.



EUROPEAN ECONOMIC  
COMMUNITY**Report on the problems arising for the Community  
because of internal and external disequilibrium**

(revised version)

Brussels, 25 March 1964

**I. Introduction**

The generalized inflationary strains which, having developed mainly in 1963 in certain member countries—first in Italy and France and, subsequently, in the Netherlands, are now spreading to the other member countries, call for prompt and energetic counter-measures co-ordinated at Community level. It is true that the Governments of those Member States suffering from inflationary pressures already put in hand stabilization policies some time ago, but stronger measures and more complete synchronization of views and means of implementing such policies—notably on the point that stabilization must be achieved quickly—are vitally necessary.

This is so not only because of the economic and social damage that the inflationary process inevitably causes, but also because the persistence of trends of this kind in a few member countries might well undermine the coherence of the Community and jeopardize the attainment of its objectives. Although any reversion to protective measures at national level or to measures to isolate domestic markets (to which a balance-of-payments crisis in one or other Member State could probably lead in the end) would be far from a reasonable solution in economic or even in political terms; the danger cannot be ruled out that the present situation may provoke steps which would practically wipe out the considerable progress the Community has made in recent years. The fight against inflation is therefore not only in the interests of the Member States affected, but also, and above all, in the interests of the Community's unity. In addition, the consequence of failure to take energetic action now might be extensive structural deterioration of the Community's competitive position vis-à-vis non-member countries, which would greatly increase the danger of recessions against which the ordinary instruments of short-term economic policy would be powerless.

## II. The contamination process

The annexed tables, which show what proportion of its total exports and imports each Member State buys from or sells to the rest of the Community (Table 1) and trade trends between 1962 and 1963 (Table 2), give an idea of how deep the interpenetration of the Member States' economies has gone. But they also show how much greater is the risk, for this very reason, of an undesirable trend that has developed in one or more Member States contaminating the others.

To take a case in point in EEC internal trade the Federal Republic of Germany's surplus of \$517 million in 1962 rose to \$1 112 million in 1963; over the same period, France's surplus of \$188 million became a \$35 million deficit, a deterioration of \$223 million. Italy's deficit rose by \$416 million to \$683 million. Although on a year-to-year basis the Netherlands' deficit was to all intents and purposes stable, the last quarter of 1963 showed considerable deterioration, and all the signs are that this trend is continuing unabated. The surplus in the Belgo-Luxembourg Economic Union—until the end of the summer of 1963 a region of the Community like the Federal Republic enjoying relative stability—rose by \$126 million from 1962 to 1963 to reach a total of \$260 million.

These shifts in the trade balance pattern suffice in themselves as a gauge of the extent to which the Member States in which demand first began to exert inflationary pull—Italy and France—have exported net demand to the other member countries and brought pressure to bear on their supply resources. It is certain that services figures would tell the same story. In view of the fact that even in the member countries still enjoying relative stability the production factors, particularly labour, are virtually fully extended, these shifts are bound to lead to inflationary strain in the very near future.

## III. The Community's ability to compete

Energetic measures to eliminate surplus demand and to re-establish or maintain the stability of the cost and price level in the Community are needed not only to smooth out the disparities in economic development within the Community and to forestall their consequences, but also to protect the Community's competitive capacity vis-à-vis non-member countries. The Community's trade balance with non-member countries (on the basis of customs returns), which was still in relative equilibrium in 1961, showed a deficit of some \$3 000 million in 1963. Its overall balance of current payments deteriorated practically to the same extent: where there had been a surplus of about \$3 000 million



in 1961, current payments just balanced out in 1963. These figures reflect not only differences of degree in the pressure of demand—the emergence of increasingly acute inflationary strain within the Community contrasting with relative stability in the economies of certain of the Community's main competitors—but without doubt also, and already to an appreciable extent, a deterioration of the Community's competitive position due mainly to inflationary thrust of costs and prices.

For prices and costs have developed quite unfavourably in the Community and, of course, particularly in the member countries where inflationary pressure is strongest: in Italy, according to the consumer price index <sup>(1)</sup>, prices already went up by 4.6 % from 1961 to 1962, and then by 7.4 % from 1962 to 1963. For the same years, wage costs per unit of output in Italian industry advanced in two successive bounds of 11 % and 12 % <sup>(2)</sup>. In France the corresponding price increase was 4.7 % from 1961 to 1962 and 5.9 % from 1962 to 1963, and that in wage costs per unit of output was 6 % in each of these two years. In the Netherlands the increases were 2.9 % and 4.6 % for prices, and 4 % and 5 % for wage costs per unit of output. In Belgium and in Luxembourg, trends were appreciably more stable; none the less prices were nearly 3 % higher in Luxembourg and nearly 2 % higher in Belgium in 1963 than in 1962, and in Belgium the wage-cost trend accelerated from a 3 % increase for 1962 to 4 % for 1963. In general, the rising price trend speeded up clearly in France and in Italy until the end of the summer and in the autumn of 1963, in Belgium from the end of the summer of 1963 onwards, and in the Netherlands from the fourth quarter of 1963 onwards. For example, in Belgium an increase of more than 4 % in the general consumer price index was recorded towards the end of 1963. In Germany, trends between 1961 and 1963 were the opposite of those recorded in the other countries: the upward price curve tended to level out (from 3.5 % to 3.1 %), and wage costs per unit of output followed up a leap of 6 % in 1962 with a more modest advance of only 3 % in 1963.

These wage-cost data do not mean that wage costs and the attitudes of men and management as reflected in collective agreements should be singled out as the main reason—or still less the only reason—for higher prices and the decline in the Community's ability to compete. In fact, the real culprits are the trend of overall demand in monetary terms, and, as a pre-condition and concomitant circumstance, the growth of the volume of money. The resultant over-rapid expansion of the economy and of the demand for labour, which itself was thwarted by the sheer lack of manpower—or of manpower with the right skills or sufficiently mobile—necessarily caused wages to run considerably ahead of productivity gains. Efforts to put in hand a moderating incomes policy, which could have curbed this process, have generally not been crowned with success. In the Nether-

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- (1) Consumer price, retail price, or cost of living indexes, as published by the Statistical Office of the European Communities (base year 1958 = 100).  
(2) The rate of 12 % was a tentative estimate; according to official Italian statistics established since, it should be increased to 16 %.

lands, where such a policy has been followed for many years, experience has shown that its value is limited when acute strain besets the labour market.

If, then, the development of wage costs has been mainly a consequence and a concomitant of the inflationary process, rather than its cause, it is still a factor which, because wages are the most important element in costs, can make all the difference in efforts to retain old markets abroad or win new ones. It should be noted in this context that in some of the non-member countries which are the Community's main trading partners and its main competitors wage costs per unit of output have increased much less in recent years (the United Kingdom) or have even declined slightly (the United States).

#### IV. The causes

There can be no doubt whatever that the too rapid expansion of demand in monetary terms is at the root of the inflationary disequilibria which have developed. Historically, the initial onset came mainly from demand in non-member countries, which, again, under the influence of heavy American balance-of-payments deficits over several years, had made quite lively progress. Since costs and prices had not then risen as much in the Community (save in France, which devalued the franc in consequence), as in the main non-member countries and since, generally speaking, there was no surplus of demand in the Community, the latter's imports lagged behind its exports. Moreover, considerable net capital inflows began to accumulate in the Community. This led to the formation of large surpluses on the balance of payments, which imparted a strong stimulus to the expansion of internal liquidity and business activity. The countries in which costs and prices were lowest—Germany and the Netherland—were the first to be affected by this "imported inflation" followed by Italy and France. In France the situation was influenced by the war in Algeria, which led, in 1961, in 1962 and, to some extent, in 1963 still, to an influx of capital, the repatriation of French families from Algeria, the conversion of large quantities of savings into cash and exceptional government expenditure.

In Germany, in particular, prices and costs climbed quite considerably during 1960 and 1961, especially if account is taken, in country-to-country comparisons, of the fact that the Federal Republic revalued its currency in 1961, with the Netherlands immediately following suit. Partly for these reasons Germany's balance of current payments deteriorated considerably and by 1962 was showing a deficit; this naturally contributed, through the workings of intra-Community trade, to an appreciable increase in demand in the other member countries. Trends then reversed themselves when the economy began to be overheated in these countries, particularly France and Italy, with rising internal

liquidity fed by payments surpluses. Meanwhile, in the Federal Republic the situation had already begun to settle down, largely as a reaction to previous investment boom, and because the overall payments account even showed deficits. At the present time, inflationary pressure from the other member countries again threatens to spread, especially to the Federal Republic.

The fact that economic development has been out of phase in the six countries has clearly made co-ordination within the Community very difficult, but it is no less obvious that the upward spiral must be stopped. This is the right time to do it, since inflationary stimuli from outside have lost some of their edge mainly because of the relatively rapid price and cost increases in the Community in recent years and the resultant deterioration of its current payments situation. This applies especially to Italy, where the overall balance of payments now shows a heavy deficit, but there is also this outside pressure on France and the Netherlands, where overall payments appear likely to run up small deficits. Alone among the Six, Germany has for some time been subject, once again, to external expansionary stimuli, from beyond as well as from within the Community. However, the surpluses which have reappeared on the Federal Republic's current payments balance are largely attributable to the development of trade with the other Community countries.

The struggle against inflation in the Community has now become an internal problem. In most member countries, internal demand of the Community is practically the only reason for price and cost increases.

The first demand-generating impulse came from outside the Community but it was long since supplemented—on a large scale—by internal developments: there was firstly an investment boom, matched very soon by a sharp increase in expenditure on private consumption, mainly based on large wage and salary increases. These are processes which would scarcely have been imaginable had a quite vigorous expansion of credit not been tolerated: great increases in the volume of bank credit, with year-to-year growth rates of from 15 % to 25 %, were recorded in 1961 and 1962, particularly in Italy, but also in France, and in 1963, in Italy and in Belgium. Moreover, government expenditure, the expansion of which had at first been slower in varying degrees than that of revenue in most member countries, rapidly caught up; generally speaking it grew in 1962 and particularly in 1963 at an appreciably more rapid pace than income and than real gross national product. In all member countries, the effect of government measures, so far from being “anticyclical”, was everywhere—though, again, in varying degrees—“procyclical”. Deficits grew appreciably. They were financed very largely in Italy and in Belgium, and to some extent in France, by means which manifestly contributed to the expansion of internal liquidity.

These are the main reasons for the emergence of inflationary strains in the Community. It is true that other factors played a role: poor harvests and certain agricultural policy decisions in various member countries, imperfect competition, notably in certain

services, inadequate geographical or occupational mobility of labour and lagging vocational training, absence or failure of a moderating incomes policy, the "spiralling" effects of certain sliding wage scales, increase in controlled rents, weakening of the propensity to save, speculative movements (especially speculation on real estate), of late, further price increases for imported raw materials, etc. However, these factors have not been of decisive importance in determining the direction in which things have developed; some of them are, in fact, themselves closely tied up with the surplus demand situation.

## V. What must be done

All this points to excess demand as the malady which must be remedied by a sufficiently rapid stabilization programme in the countries suffering from inflationary strain: the growth rate of internal demand in monetary terms must be cut sharply. Other measures will certainly also be of great importance: faster and better vocational training is needed and distribution channels should be streamlined; steps should be taken to increase the output of certain important farm products (notably meat), highly productive investment ought to be encouraged, so as to stimulate the growth of industrial production, etc. However, quite some time must elapse before all these measures begin to bear fruit, and the inflation problem cannot wait. The main emphasis of emergency stabilization action to be put in hand now can therefore only be on measures likely to produce an overall restrictive effect. First of all, on the demand side, some measure of equilibrium must be restored. It is therefore important to ensure that measures desirable to increase supply in the longer term should not be so conceived that their immediate effect will be to further stimulate the expansion of demand directly or indirectly. They must be kept within the bounds set by the policy curbing the growth of demand.

The time factor is of great importance: if the internal price and cost trend in Italy, France and the Netherlands is not stabilized between now and the end of 1964 and if definite progress is not made towards improving the current external payments situation, especially the trade balance vis-à-vis the other Community countries, by means of a check on internal demand, internal balance will be a lost cause in Belgium, and the German economy will slide into internal disequilibrium for a second time. Were this to happen, it is clear that, far from contributing to restored Community stability, trends in these two countries would render a stabilization policy in the other member countries much more difficult even than it is already.

## VI. Anti-inflation policy : the outlook in the member countries

All the member countries have introduced a policy designed to combat inflation, with the exception of the Federal Republic, where the need for this has not yet been felt, but where precautionary measures have nevertheless been taken.

In Germany, the growth of Federal expenditure has been kept down to 6 % for 1964 and the expansion of state spending on new housing cut, while the Bundesbank recently resumed its policy of encouraging exports of short-term capital. Most recent reports and forecasts concerning 1964 show, however, a very distinct tendency for business activity to gather pace. The surplus on foreign trade might well reach some DM 8 000 million for the full year. In addition, it would seem that industrial investment expenditure, the trend of which was very calm in 1963 and even actually declining for a short time, has been caught in a new and vigorous upswing. Wage improvements in 1963 did not match those for 1962 and this factor, coupled with a substantial increase in the rate of private saving, has helped to keep the expansion of private consumers' expenditure quite moderate. The movement of wages should remain quiet until the end of 1964, when a spate of increases is to be expected. The labour market is again severely strained. Although the growth of internal supply has gathered momentum—real gross national product could well outstrip the 1963 figure by some 5 % to 6 %—it would seem that deterioration of the price climate has already clearly set in.

After cutting back the expansion of bank credit in February 1963 and raising the minimum reserve ratio ("coefficients de trésorerie"), the French Government adopted in September a stabilization programme which has since been progressively amplified and in certain respects strengthened.

In the field of budget policy, these measures involve curbing the growth of government expenditure for the rest of 1963, the floating of a government loan of FF 2 000 million to facilitate the financing of the "impasse", the withdrawal from the budget of certain investment items and their financing by specialized public credit establishments, the reduction from FF 7 000 million to FF 4 700 million of the "impasse" in the 1964 budget, renunciation of any supplementary budgets in 1964, the phasing of certain public expenditures in 1964 in the light of economic, seasonal and regional conditions and possibilities and limitation—in relation with the growth of the gross national product—of the expansion of public spending in 1965, with the "impasse" being kept down to FF 4 700 million. The "impasse" is to be financed from loans to a large extent in 1964 and wholly in 1965. Measures in the field of credit policy include a 10 % ceiling on the expansion of bank credit from the end of February 1963 to the end of February 1964 (the further increase authorized from then until the end of September 1964 is fixed at 4.5 %) the raising of bank rate from 3.5 % to 4 %, more stringent hire purchase terms, a number of provisions designed to encourage long-term saving, and the progressive reorganization of arrangements to finance housing construction so that long-term savings may replace rediscountable medium-term credit as a source of funds. The Government has also decided to shorten national service, to add to the labour supply by stepping up vocational training and hiring more foreign manpower, to advance the dates of scaling down customs duties and to introduce direct control of prices and trading margins.

The latest analyses and forecasts show that the stabilization policy has already borne fruit and that further results are to be expected. In the last months of 1963 the

expansion of general public expenditure and of private consumers' expenditure lost a little momentum. For some time already, the pace of industrial investment had in any case been weaker. Since the growth of internal supply remained lively—industrial production was 8.5 % up in the fourth quarter of 1963 on the same 1962 figure—and since imports increased very fast and price-pegging measures became effective, the upward price trend tended to fall off. Strain on the manpower market, however, remained very acute. The balance of current payments with countries outside the franc area clearly appeared to be weakening further; the same applies to the overall balance of payments, although a slight surplus was maintained thanks to net inflows of capital.

The further outlook for 1964 points to a fresh slackening in the expansion of private consumers' expenditure and to the maintenance of no more than a slow growth rate in industrial investment. The growth of production, while remaining fairly brisk, will probably lose some of its vigour in certain industries. For the whole of 1964, an increase in the real gross national product of 5 % is at present thought possible. Although the expansion of imports might be a little less lively than it has been so far, the deficit on the trade balance will again increase, if rather more slowly : exports are growing fairly steadily, but at a less lively pace. Again, the balance between supply and demand can only be achieved again through higher prices. It is true that the upward price trend might slow down further—provided always that no further spurt of wage rises supervenes in the course of the year—but there can scarcely be any question of stability, even relative stability, in 1964. The most that can be hoped for is the restoration of relative equilibrium at some time in 1965.

In Italy, too, measures have been taken to combat upward price trend. For example, credit policy has been reorientated along more restrictive lines since May 1963, after the Central Bank had still intervened on a large scale in support of the capital market. Excess tax revenue of Lit. 80 000 million between July and September 1963 has been used to cut the Treasury deficit. Efforts have been made to boost tax revenue by expediting the settlement of tax disputes; the turnover tax (IGE) has been raised for certain luxury goods, a special tax on the purchases of new automobiles and motor-boats instituted, and the fuel tax increased. It is true that the revenues accruing from these last two measures will not be used to reduce the Treasury deficit but to finance certain supplementary investment expenditures. The Government's draft budget for 1964/65 provides for a smaller increase in expenditure than in the preceding budget—12 % instead of 18 %—and for a reduction of about Lit. 100 000 million in the budget deficit, bringing it down to Lit. 696 000 million. To inject more life into the security market, taxes at source on dividends have been adjusted to leave a choice between the rate of 30 % if the taxpayer remains anonymous and 5 % if the name is given. Credit policy has become more restrictive : the Italian commercial banks have been prevented from taking up further credits abroad. In addition, arrangements governing hire purchase sales are to be made more stringent. To this must be added measures affecting supply : reduction in the length of national service, encouragement of imports of certain foodstuffs, tax

benefits designed to stimulate industrial investment, measures to encourage the production of certain agricultural items (olives and sugar-beet), or to streamline distribution channels, and the freezing of rents. The Government has embarked on conversations with the trade unions with a view to moderating the upward wage trend.

In fact, the expansion of internal demand seems to have lost some momentum in the last months of 1963 and early in 1964. The upward price trend has become a little slower, owing partly to the fact that harvests of vegetables, olives and other fruits have been better than in the previous year. In the fourth quarter, industrial production was 8 % up on the level reached a year earlier. Although the import boom has weakened slightly, merchandise imports were none the less up about 20 % in the fourth quarter of 1963 on the same 1962 figure.

For the whole of 1963 the deficits on the trade balance and on the overall balance of payments were \$2 500 million and \$1 200 million respectively. In comparison with 1962, the deterioration was \$1 100 million on the trade balance and \$1 300 million on the overall balance. The decline in official gold and foreign exchange reserves was less than the balance-of-payments deficit; from the end of 1962 to the end of 1963, the reserves fell by \$434 million, to a figure of \$3 057 million; this was because the Italian banks ran down their net foreign exchange holdings over the same period by \$650 million by increasing short-term borrowing abroad. Once the commercial banks' short-term foreign indebtedness ceased to grow—i.e., since September 1963—official reserves declined at the average rate of \$125 million per month until the end of February 1964, despite certain American purchases of lire which served to slow down losses to some extent.

In spite of the measures taken so far, the business outlook holds out no hope of a sufficiently rapid reversion to stability and equilibrium in the balance of payments. Although it has lost some momentum since last year, the growth in particular of private consumers' expenditure, and of public expenditure is still tending to outstrip that of real internal supply. The growth of gross fixed asset formation seems likely to weaken. All in all, real gross national product will probably be 5 % higher in 1964 than in 1963. Even if imports were to slow down further and exports made a rather better showing, there would, in view of the heavy deficit, be no immediate improvement at all in the trade balance. There will be further heavy deficits on the balance of current payments; the prospects at present are that the overall balance of payments will close with a deficit of something between \$1 000 million and \$1 500 million, depending on outgoing capital movements. To finance this deficit, Italy has obtained credit promises from the United States, from the Bundesbank, the Bank of England and from the International Monetary Fund.

In conclusion, it is fair to say that although in Italy trends towards the re-establishment of equilibrium have undeniably become manifest, and will persist, recovery is taking

too long, particularly in view of the effects on the other Community countries of the inflation and the continuing high deficits on the Italian balance of payments.

In the Netherlands, where the expansion of exports and very heavy demand in the building sector clearly spurred on business activity in the second half of 1963, with vivifying effects on consumption and investment, labour market strains have by no means eased, despite forecasts to that effect, and very heavy wage increases for 1964 were agreed to in October 1963. The Government has adopted a series of measures designed to slow down the expansion of demand, so as to forestall a spiral movement with a further spate of wage rises in 1965. For example, government investment expenditure has been cut by Fl. 100 million, or 5 % of the spending budgeted for in 1964; initially the plan was to postpone spending by 6 months, but later this period was extended to 12 months, expiring in October 1964. Investment expenditure by local authorities is to be reduced in the same manner and by the same percentage of the 1964 programmes. Local authorities' loan issues, up to the middle of 1964, have been limited to 91 % of loans placed between mid-1962 and mid-1963. Tax rules governing depreciation in building (except housing) and capital goods investment have been stiffened. The taxes on fuel and cigarettes and on motor vehicles not powered by petrol engines have been increased, and this will bring an extra Fl. 200 million into the Exchequer in 1964. The expansion of bank loans to the private sector has been limited to 4 % for the period from September to December 1963, and to 5 % for the period from January to April 1964. Bank rate has been raised from 3.5 % to 4 %. Regulations governing hire purchase sales have been made more stringent, national service has been cut, certain prices have been pegged and a ban on resale price maintenance agreements is in the offing.

None the less internal demand is still likely to expand vigorously. Workers on average will be earning 16 % more in 1964 than in 1963, so that the boom in consumer expenditure is bound to persist. In addition, the upswing in industrial investment will continue at a fairly rapid pace into the second half of the year. Then, however, under the pressure of dwindling profitability and shrinking liquidity—the result of contracting profit margins combined with official price controls and a restrictive credit policy—industrial investment will tend to fall off.

Although internal supply is also growing faster—all in all, growth of the real gross national product in 1964 as compared with 1963 could well reach 5.5 %—only a substantial deterioration in the balance of current payments will make it possible to achieve equilibrium between demand and supply: at present a deterioration of Fl. 1 500 million is expected for 1964 as compared with 1963. In view of the pull of internal demand and the fact that sharply rising costs are pricing some Dutch items out of the market, exports will increase with distinctly less vigour: imports, on the other hand, will rise very rapidly. Despite a direct government policy designed to curb increases, prices will again rise strongly; their average level at the consumer stage in 1964 will be 7 % up on 1963.



The present outlook suggests that equilibrium will not be re-established before 1965, and even then only on the condition that a new heavy wave of wage increases for 1965 is avoided in the autumn. A decline in investments—with all its effects and repercussions—could be the key to stabilization.

In Belgium, where exports rose steeply in the course of 1963—as did the national budget deficit—industrial investment grew and strain developed on the labour market, the upward wage trend also accelerated. The result was an increase in the rate of expansion of private consumers' expenditure. Faster growth of internal demand continued into 1964 as well. It is true that the growth of supply also gathered pace; none the less the economy betrayed increasing signs of strain.

Since the middle of 1963 the chief measures adopted by responsible Belgian authorities have been the following: a reduction—with effect from the first quarter of 1964—in commitment approvals ("crédits d'engagement") covering public investment in the extraordinary budget; action for a similar limitation of expenditure by local authorities; introduction of certain rules for the letting of public contracts (price ceilings); a decision, when special terms are being accorded for industrial investment (under the 1959 industrial promotion laws), to adopt a more selective approach; raising in two stages of Bank rate (altogether from 3.5 % to 4.25 %); "moral suasion" to induce the banks to moderate their rate of credit expansion; limitation of the expansion of bank credit from February 1964 for the rest of the year to about 10 %; limitation of the expansion of mortgage credits; introduction of more stringent rules governing hire purchase; more intensive action to hire foreign workers and encourage persons drawing old-age pensions to join the labour force, a stricter price policy and the pegging of certain foodstuffs prices.

Despite these measures, in Belgium too the prospects for the development of internal demand remain too expansive when related to the probable development of supply (the real year-to-year growth rate of the gross national product could be 4 % to 4.5 %). In addition, Belgium will almost certainly once again be exporting much more. None the less, the balance of current payments is tending to deteriorate, firstly because imports are climbing again and secondly because of a deterioration in the balance of investment income. The upward trend in prices is continuing at the faster rate which set in in the second half of 1963.

In the Grand Duchy of Luxembourg, the recession provoked by the weakness of the steel market has given way to an unmistakable recovery. The rising price trend continues, mainly as a result of higher import prices, though heavier wage costs are also playing a role. The shortage of manpower, which has already been acute for several years, has again worsened considerably, a situation which the establishment of new industries in the Grand Duchy has done nothing to alleviate. In addition, the public authorities are spending much more, mainly on improved salaries. The Government

is endeavouring to achieve stabilization by stipulating priorities for public investment, by imposing more stringent conditions for the granting of building loans, by encouraging foreigners to work in Luxembourg and by pegging certain prices.

## VII. Conclusions

A study of the outlook for 1964 in the various member countries points to the following conclusions for the Community as a whole : internal disequilibrium will persist, although some trends towards restored balance at a later date in France, the Netherlands and Italy are already discernible and others are likely to develop; Belgium, and to an even greater extent the Federal Republic of Germany, will suffer further from inflation exported by neighbours; prices will continue to rise, at a slower pace perhaps in France and in Italy, but faster in Belgium and considerably faster in the Netherlands; in Germany there is the danger of considerable upward price movements re-emerging; the competitive position of the Community countries, particularly Italy, but also the Netherlands and France, will again deteriorate (for this reason, there will be a further increase—although it will be smaller than in 1963—in the deficit on the Community's trade balance with non-member countries despite the recovery of world business); a deficit on the Community's general balance of current payments which, in 1964, could be of the order of \$500 to \$600 million.

In many respects, these prospects are disturbing. By no stretch of imagination can they be made to tally with the economic objectives of the Treaty, notably with those spelled out in Articles 2 and 104.

If these trends follow their logical course—and they are bound to do so unless further energetic action is undertaken—it becomes clear that certain Member States are liable to run into grave balance-of-payments difficulties. To prolong the present situation by the use of international credits cannot by itself lead to a trend towards the re-establishment of better balance. Failing energetic stabilization measures, the danger that structural disequilibria in the balance of payments will eventually emerge—disequilibria which would manifestly constitute a serious obstacle to long-term growth—is bound to become much more serious. Dangers of a recession would be much greater and the ordinary instruments of economic policy would no longer be available to cope with them.

An energetic and co-ordinated stabilization operation on the other hand involves none of these dangers; it is true that it could slow down real economic growth for a short period, although in fact for the most part it would neutralize only excess demand, thus stemming upward price movements. But in the long term, it alone would re-establish the

conditions which are absolutely essential for sufficiently rapid—and balanced—growth. Any recession hazard could easily be dealt with, since the Governments would have adequate means at their disposal to stimulate demand should the need arise.

Action to re-establish equilibrium must make use of those instruments which are best suited in the present circumstances to mop up surplus demand. What is needed in the first place is a more stringent budget and finance policy, plus action to limit the expansion of credit: in other words overall measures tolerating only a very moderate extension of liquidity from internal sources.

To achieve really effective co-ordination of Community action to re-establish equilibrium, it is vital for the member countries to agree on minimum quantitative criteria. These are needed to fix the time by which the new state of equilibrium must be achieved, but also in dealing with certain components of internal demand.

It would perhaps be appropriate to fix quantitative criteria for an acceptable global increase in liquidity, for instance, the percentage growth of real gross national product. Liquidity growth should not be allowed to exceed this ceiling. The theoretical and practical problems which a short-term stabilization operation encounters make it doubtful whether this line is worth pursuing. In fact it is hard to see how the various definitions of liquidity used in the six countries can be reduced to a common denominator and even if they could, the economic importance of liquidity varies widely from country to country, because of differences of structure and fairly wide disparities in the way it has developed so far. In addition, the velocity of circulation can vary so widely at such short notice that it would be very difficult to adjust to it in advance.

None the less, in the following recommendations, certain criteria have been selected in the field of public budget and finance policy, which, if applied, would not only curb demand directly and indirectly, but would also help to “contain” liquidity. To this must be added the effects of the deterioration of the balance of payments in the countries where this has occurred. It will be the task of credit policy to exert variable pressure—in relation with the requirements of stabilization policy—on the other major source of liquidity: loans to the private sector. In this sphere, quantitative restrictions, adapted, of course, to specific conditions in the country concerned, are quite feasible and appropriate. However, wrongly applied, credit policy might simply lead to more borrowing abroad, thus defeating its own ends; the international balance-of-payments situation must also be taken into consideration. Therefore, in the following recommendations, only one general rule has been laid down: in all the member countries suffering from inflationary strain—they have moreover without exception already applied curbs to a greater or lesser extent—credit policy must be made as restrictive as the stabilization objectives require.

On the question of budgetary expenditures, a uniform year-to-year growth rate of 5 % has been fixed as a ceiling. This rate corresponds approximately to the average over a period of several years of the growth of the Community's real gross product. It is obvious that where a country is at any given time suffering or is likely to suffer from "overheating", an anticyclical budgetary policy demands that expenditure should lag slightly behind the real growth of gross national product expected for the current year. For incomes policy, it is the productivity criterion which has been chosen.

These criteria could not be used as a permanent guide to economic policy. In a long view, they can be defended neither by economic theories nor by wealth distribution arguments. They can only be used in emergencies and for a limited period as rules of stabilization policy. They are to be seen as upper limits, within which the various member countries, each according to its own stabilization requirements, should, or even must, remain.

At this point it is useful to stress once again the importance of action to re-establish and safeguard equilibrium : inflationary strain—and above all strain of variable intensity in different parts of the Community—is not only very harmful economically and socially to the Member States considered individually, but represents above all a serious obstacle to the Community as a whole in the achievement of its objectives.

TABLE 1

*Percentage share of intra-Community trade in  
total external trade of the member countries*

*(in %)*

Year	Germany (F.R.)	France	Italy	Netherlands	B.L.E.U.
<i>Imports</i>					
1958	25.8	21.9	21.4	41.9	46.6
1959	29.0	26.8	26.7	44.4	47.1
1960	29.9	29.4	27.7	45.8	47.9
1961	31.3	31.5	29.4	49.2	50.6
1962	32.5	33.6	31.5	50.2	51.2
1963	33.3	35.8	32.8	51.6	52.6
<i>Exports</i>					
1958	27.3	22.2	23.6	41.6	45.1
1959	27.8	27.2	27.5	44.3	46.3
1960	29.5	29.7	29.5	45.9	50.5
1961	31.7	33.5	31.4	47.6	53.3
1962	34.0	36.8	35.0	49.2	56.8
1963	37.3	38.2	35.5	53.4	60.8

TABLE 2

## Intra-Community trade (1)

Year	Germany (F.R.)			France			Italy		
	Imports \$ %	Exports \$ %	Balance \$	Imports \$ %	Exports \$ %	Balance \$	Imports \$ %	Exports \$ %	Balance \$
1962 I	937.4 (2)	1 096.5	+ 159.1	639.7 (2)	669.1	+ 29.3	461.8	377.7	- 84.1
II	953.7 (2)	1 128.2	+ 174.5	609.2	677.2	+ 67.9	444.8	402.7	- 42.1
III	991.0	1 088.4	+ 97.5	590.9	628.2	+ 37.3	468.4	411.7	- 57.8
IV	1 113.1	1 199.3	+ 86.2	683.3	737.1	+ 53.8	516.3	435.7	- 80.6
Total	3 995.1	4 512.5	+ 517.3	2 523.2	2 711.6	+ 188.3	1 891.3	1 624.4	- 266.9
1963 I	951.0 + 1.6	1 555.2 + 5	+ 204.3	715.8 + 12	696.4 + 4	- 19.4	551.9 + 19	418.1 + 11	- 133.8
II	1 052.3 + 10.3	1 309.7 + 16	+ 257.4	793.5 + 30	795.6 + 18	+ 2.1	613.3 + 38	430.6 + 7	- 182.7
III	1 090.6 + 10.1	1 341.4 + 23	+ 250.8	737.2 + 25	735.2 + 17	- 2.0	631.1 + 35	462.3 + 12	- 168.9
IV	1 105.1 - 1 (2)	1 504.2 + 25 (2)	+ 399.1	879.6 + 29	864.3 + 17	- 15.3	678.7 + 33	484.0 + 12	- 194.7
Total	4 341.9 + 8.7	5 453.1 + 20.8	+ 1 111.6	3 216.1 + 23.9	3 091.5 + 14	- 34.6	2 474.8 + 30.9	1 792.3 + 10.3	- 682.5
Difference : 1963 as compared with 1962			+ 594			- 223			- 416

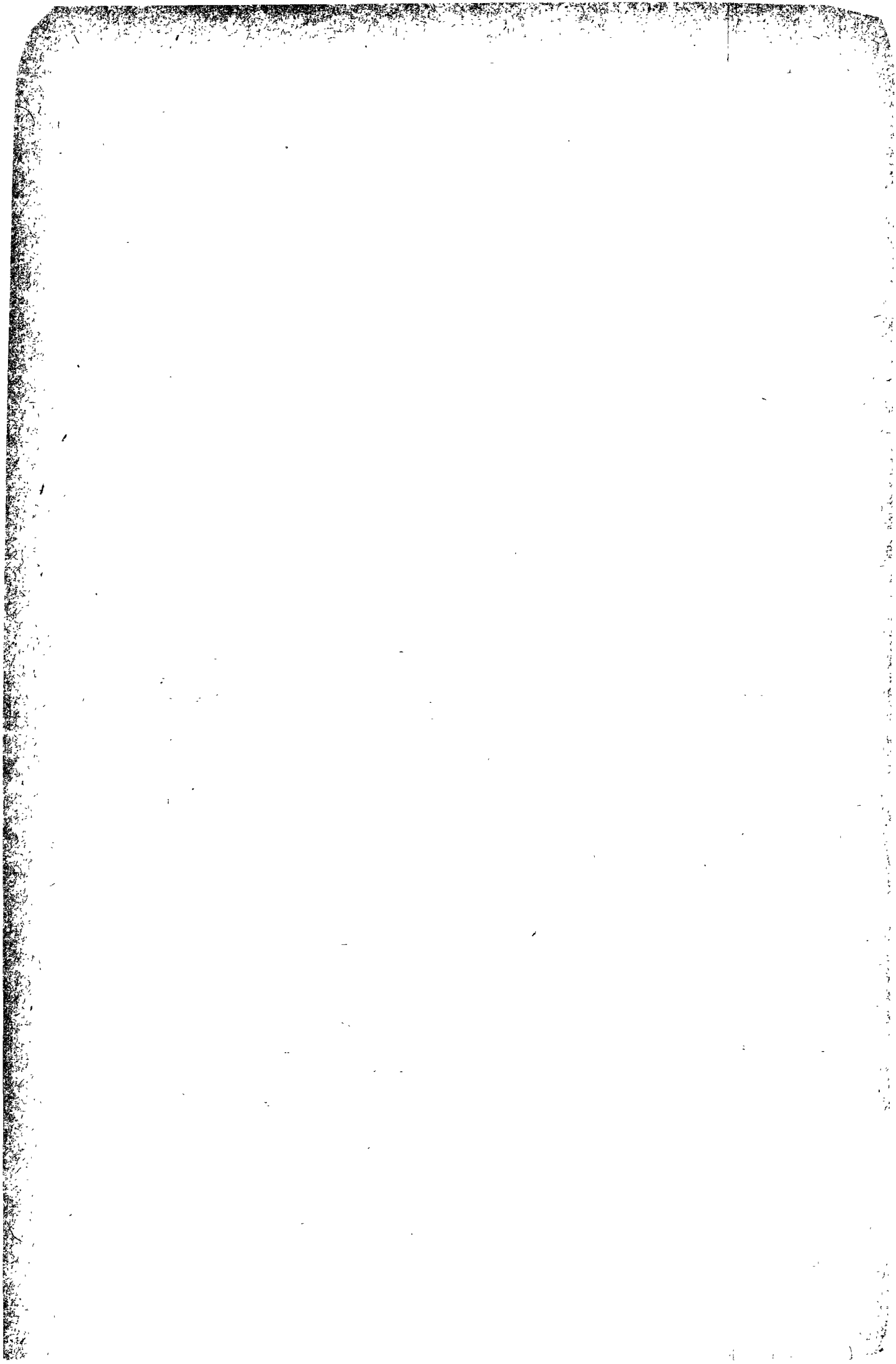
Table 2 (cont'd)

Year	Netherlands			B.L.E.U.			EEC	
	Imports \$ %	Exports \$ %	Balance \$	Imports \$ %	Exports \$ %	Balance \$	Imports \$ %	Exports \$ %
1962 I	686.4	542.8	- 143.5	577.2	581.7	+ 4.4	3 302.6 <sup>(2)</sup>	3 267.9
II	661.1	548.9	- 112.2	564.0	618.0	+ 54.0	3 238.8 <sup>(2)</sup>	3 374.9
III	646.2	548.2	- 97.9	550.6	579.7	+ 29.4	3 247.0	3 256.4
IV	689.2	616.1	- 73.2	625.4	679.6	+ 54.2	3 622.7	3 663.5
Total	2 683.0	2 256.0	- 427.0	2 323.9	2 458.4	+ 134.5	13 416.4	13 562.9
1963 I	699.9 + 2	590.0 + 9	+ 109.9	598.8 + 4	646.9 + 11	+ 47.2	3 517.3 + 6	3 505.6 + 7
II	775.6 + 17	661.7 + 21	- 113.9	673.5 + 19	764.7 + 24	+ 91.2	3 908.2 + 21	3 962.2 + 17
III	768.3 + 19	685.9 + 25	- 82.4	653.9 + 19	730.8 + 26	+ 76.9	3 881.1 + 19	3 955.6 + 21
IV	838.2 + 22	709.7 + 15	- 128.5	743.1 + 19	802.7 + 18	+ 59.6	4 244.7 + 17	4 362.9 + 19
Total	3 082.0 + 14.9	2 647.2 + 17.3	- 434.8	2 680.9 - 15.4	2 941.0 + 19.6	+ 260.1	15 705.6 + 17.1	15 925.2 + 17.4
Difference : 1963 as compared with 1962			- 8			+ 126		

<sup>(1)</sup> Absolute figures in millions of dollars; year-to-year growth rate in %.

<sup>(2)</sup> No adjustment has been made to take account of changes in methods of computing imports statistics made early in the year in Federal Germany and France.

<sup>(3)</sup> Excluding an adjustment to Federal Germany figures, referring to the whole of 1963 but concentrated in the fourth quarter.





EUROPEAN ECONOMIC  
COMMUNITY

Economic Policy Committee

**Opinion of the Economic Policy Committee on recent  
trends in the economic situation in Community countries**

Brussels, 10 April 1964

On 6 and 7 April 1964 the Economic Policy Committee examined the recent trends in the economic situation in Community countries. It sought, in particular, to estimate the effects of stabilization measures taken by the Governments of the Member States in the last few months. It was pleased to note that in general the Governments had modelled their short-term economic policy on the opinions rendered by the Committee at its meetings of 14-15 October 1963 and 27-28 January 1964. It considered, however, that further steps should be taken or the existing measures intensified in most of the countries.

At present the main objective of short-term economic policy continues to be not only to check the spread of inflationary tendencies in the Community, but also to prevent the position of the Community as a whole vis-à-vis non-member countries from deteriorating under the combined effect of a too rapid rise in production costs and an over-lively expansion of internal demand. The Committee considered that in most of the Member States this aim continued to call primarily for a policy to restrain the expansion of total internal demand. In pursuing this policy, use must be made of those instruments which, in the present circumstances, would prove most effective in adjusting the various elements of overall internal demand to the conditions of economic balance. As the Committee had recalled at its previous session, first and foremost there was a need for a stricter policy on public expenditure in the widest sense and a policy to limit the expansion of credit. The Committee also felt it necessary to emphasize once more the need for the Member States to pursue without delay an effective incomes policy. It stressed, finally, that it was indispensable to co-ordinate closely and efficiently within the Community framework any measures taken by individual Member States.

The Committee went on to examine the proposal submitted by the Commission to the Council of the European Economic Community for a recommendation to be addressed by the Council to the Member States, in pursuance of Article 103 of the Treaty of Rome, on the necessary steps to restore the Community's internal and external balance. The Committee found that this proposal broadly coincided with its own views expressed in previous opinions and during the current session of 6-7 April 1964.