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The economic situation in the Community

Quarterly survey

Commission of the European Communities
Directorate-General for Economic and Fiancial Affairs
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COMMISSION OF THE
EUROPEAN COMMUNITIES

The Economic Situation in the Community

MARCH 1975

This issue contains the text of the communication to the Council by the Commission of the European Communities, of 17 March 1975, concerning the adjustment of the economic policy guidelines for 1975. It also contains the two documents which the Commission is submitting to the Council with this communication:

- *"Summary account of the economic policies pursued in 1974";*
- *a "Report on the application of the Council decision of 18 February 1974 on the attainment of a high degree of convergence of the economic policies of the Member States of the European Economic Community and the conformity of the policies pursued with the objectives set".*

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Brussels, 17 March 1975

A. Communication of the Commission to the Council concerning the adjustment of the economic policy guidelines for 1975.

FOREWORD

1. Pursuant to Article 2 of the Council Decision of 18 February 1974 concerning the achievement of a high degree of convergence of the economic policies pursued by the Member States, the Council has undertaken to adapt, in the first quarter, the economic policy guidelines for the current year to the new requirements of the economic situation. To this end, and pursuant to Article 1 of the same Decision, the Commission hereby transmits this Communication to the Council.

2. The Commission is also submitting to the Council:
— a summary of the economic policies followed during the past year, in application of Article 2 of the above-mentioned Council Decision;
— a report on the implementation of this decision and the degree to which those policies conformed with the objectives established, in accordance with Article 12.

3. Discrepancies in the economic situation and in economic policy among the countries of the Community have never been as pronounced as at present and a more balanced situation can only be attained in the medium-term. Thus, the appropriate measures and decisions to achieve this balance should be included in the fourth medium-term economic policy programme of the Community which is now being prepared.

I. THE ECONOMIC OUTLOOK

Interdependence between economies

1.1. Economic policy, for the member countries in 1975, is confronted by exceptionally severe difficulties. The problem of combating both unemployment and inflation at the same time, which is already serious, must in future be dealt with in the new international environment created by the increase in the price of energy. The growing interdependence of all the industrial countries in the West has been highlighted by the synchronisation in the main industrial countries of the surge in economic growth in 1973 and then of the general weakening of activity since the middle of 1974.

...particularly close between member countries

This interdependence is particularly close between the member countries. It is even more pronounced for intra-Community trade which for most of these countries runs to at least 50% of their total trade and for certain countries even more, and which for the whole Community, corresponds to more than 10% of world trade. But also it assumes great importance as far as the movement of labour is concerned as well as for monetary and financial relations, particularly in the field of investment and the establishment of joint enterprises in partner countries. A more active coordination of economic policies appears from now on essential to attain simultaneously the objective of reducing unemployment, which goes hand in hand with as complete a utilisation of resources available in the Community as possible, and that of a reduction in the rate of inflation. However satisfactory the various member countries are in their demand management policies and in reducing inflation, their actions will have repercussions on their partner countries at least as great as would any measures designed to encourage exports or restrict imports. The problems with which member countries are faced are indeed extremely difficult. But they can best be resolved, even on a basis of strictly national interests, only if each of the countries, on the basis of continuing cooperation, takes account of the effects which its own economic policy can have on the other members of the Community.

...but differences in trends

1.2. In fact, disparities among the industrial countries and especially among the member countries have increased, at least until last autumn, with regard to the general level of prices and the balance of payments situation. The differences can be explained by a number of factors: initial disparities in structural positions, the variable degree of dependence on oil imports, the strength and timing of anti-inflationary measures, the behaviour of the two sides of industry and, finally, the effectiveness of certain adaptive mechanisms. Experience in the last few years has shown that balance of payments disequilibria cannot be dealt with solely by means of floating exchange rates.

The most recent developments have, moreover, displayed the limits to any procedure for recycling or financing balance of payments deficits if they are not associated with an adjustment in real terms.

Solidarity

and social consensus

1.3. In this adjustment process, the Community countries are closely bound together. Starting from different positions, they have recently established the basis for a greater convergence in the development of their respective economies. This process will however have to be consolidated, since the world trade outlook remains very uncertain in view of the weakness of the economies of the main trading partners of the Community and the disturbances in the international monetary system. Imbalances have reached a stage such that the readjustment cannot be made rapidly or effortlessly. It requires therfore determined action by the authorities with broad social backing.

World Recession

...followed by a slight recovery

1.4. The deterioration in the economic situation of most developed countries outside the Community has accelerated considerably since last summer. The economic downturn will probably persist in the next few months and it is difficult to determine when and to what extent the expected upturn in production and trade will take place. Even under the most favourable conditions, the foreseeable lags in the effects of the reflationary measures announced in certain countries, in particular the United States, lead to concern that world business will not pick up until towards the end of the year. Since the confidence of investors and consumers at international level will probably be restored only very gradually, it is possible that a considerable volume of resources will remain unused and that by the end of the year unemployment will have reached post-war record levels. Despite the fact that the OPEC countries continue to step up imports, the expansion in world trade in 1975 will probably not exceed 2% in volume.

Worsening of economic conditions in the Community

1.5. Since last summer overall production in the Community has been declining, weakened by the slackening of external demand and the markedly slower development of internal demand (particularly investment). Although the seriousness varies amongst the Community members, no country is completely spared. It is true that there are now signs of improvement in a number of member countries, but, given the steady fall in orders on hand and the time required for adjusting stocks of finished products to demand, there is no reason to expect that production will start rising again in Community countries before the autumn. For that, certain preconditions are required: changes in the growth of wages and prices to permit a gradual improvement in profits and in the propensity to invest, recovery in the residential construction sector and a less cautious attitude on the part of consumers. However, such are the differences between the situations obtaining in each sector, and in each country in the Community, and so weak is the expected contribution of external demand, that the recovery is bound to be limited in scale.

...but possible slight improvement in the second half of the year

All in all, the growth rate in the aggregate gross domestic product in real terms for all member countries should scarcely reach 1½% in 1975, as against a little less than 2% in 1974.

Worrying employment situation

1.6. There has been a widespread and marked deterioration of the national labour markets in the Community; the number of unemployed has increased by more than a million in the last twelve months. At the beginning of 1975, the seasonally adjusted rate of unemployment was running at about 3½% of the active population, although this figure hides significant discrepancies between member countries (see Table III). At the same time, more and more workers are working shorter hours. Since the unemployment is partly structural in nature and since the job vacancies do not react immediately to an upturn in economic activity, there is hardly any hope of a reversal of the current trend before the end of the year.

Inflation fed by internal costs

1.7. In most member countries, slackening demand pressure, declining import prices, as well as the policies adopted, have helped to curb inflation. However, the growing underemployment of the factors of production is hampering any improvement in productivity, and the wages spiral is slowing down in only a few countries. Consequently, any deceleration in the rate of price increases will probably be limited.

Persistence of varying rates of inflation...

Furthermore, given the disparities between countries as regards the intensity and effects of the upsurge in wage costs, there will probably continue to be major differences in rates of inflation, which, over recent months, have ranged from 6% to about 24% (see Table IV).

...and differences in countries external positions

1.8. Despite the improvement in the terms of trade, the external disequilibria of the countries in the Community remain very pronounced. Most member countries in deficit have, in recent months, been able to reduce appreciably their non-oil deficits or even to record 'non-oil' surpluses. Nevertheless, the uncertainties overshadowing world trade and consequently export development as well as the difficulty of checking oil imports any further are such that several of these countries may not be able to achieve any more substantial progress towards restoring external equilibrium before the end of the year. For 1975 as a whole, the total deficit of these countries may, nevertheless, be reduced fairly substantially (from $ 24 000 million in 1974 to some $ 18 500 million in 1975). On the other hand, the external balances of the countries in surplus, and mainly the Federal Republic of Germany and the Netherlands, should scarcely change. In total the current balance of payments deficit of the Community which reached $ 14 000 million in 1974 could fall to a level between $ 8000 million and $ 9000 million in 1975.

II. GUIDELINES FOR ECONOMIC POLICY

a) General guidelines

Economic policy priorities

2.1. In 1975, the Community will have to resolve some major policy problems:

— the reduction in unemployment, the fight against inflation and the correction of the balance of payments;

— the progressive reduction of divergent trends which threaten its cohesion.

Inter-relationship between short-term economic policies

Regarding the latter necessity, the deficit and surplus member countries bear a joint responsibility. Without being negligible, the Community's room for manœuvre in this area is, nevertheless, limited.

Three groups of countries

2.2. The present situation does not permit the member countries to be classified according to general criteria. Nevertheless, three groups of countries can be distinguished, on the basis of their external positions and the intensity of the inflationary pressures to which they are subject.

Restrictive policies in the countries with heavy deficits

2.3. As far as the countries with heavy deficits (United Kingdom and Italy) are concerned, it is important that they should, while maintaining overall restrictive policies, vigorously support the necessary transfer of resources if they are to bring about a lasting improvement in their external accounts; such a transfer of resources should be into the export sector, and, internally, into those investments yielding the highest return in the long-term and which are most urgent from the point of view of regional policy and the support of employment. This process requires a moderation in the rise of the standard of living. If such moderation is not shown, inflation will continue to effect economic activity and employment. Moreover, the prospect of bringing about a lasting improvement in their balance of payments would become extremely uncertain and those countries would have increasing difficulty in borrowing abroad to finance their excessive expenditure on consumption.

The disequilibria are also very pronounced in Ireland but that country is, at the present time, subject to external factors and has, at the same time, such a high level of unemployment and underemployment that its position must be considered quite exceptional.

Expansionary measures in the countries with large surpluses

2.4. The member countries with large balance of payments surpluses (the Federal Republic of Germany and the Netherlands) have already introduced budgetary and monetary measures to stimulate activity. These measures will only have the desired effect if they are given the support of all economic groups, with managements availing themselves of investment incentives and trade unions forgoing excessive wage claims. If it becomes evident in the months ahead that these groups are not responding sufficiently to the reflationary programmes, additional means will have to be found and applied promptly in order to reinforce the earlier measures without giving a further impetus to inflation at an advanced stage of the upswing in activity.

Intermediate position of other member countries

2.5. Other member countries are in a situation between these two groups on both the external and internal fronts, especially as far as prices are concerned. Their current balances of payments notably, are moving towards the elimination of surpluses (Belgium) or are improving, more or less rapidly, (Denmark and France). Owing to uncertainties in the world economic situation and to the danger of an insufficient slowdown in the rise of prices, the overall tenor of economic policy must remain cautious for these countries.

Support of investment

2.6. The conjunctural recovery and the mopping up of unemployment will only last if progress is also made in slowing down rises in costs and prices and modifying the economic structure. Thus an appropriate investment support policy, where necessary with the help of Community means, appears essential in all member countries. However, the nature and extent of its rôle should be varied particularly according to the needed redistribution of income and demand in the different groups of countries and in their regions. In general, greater selectivity of economic policy is required especially to prevent the waste of resources entailed in the unconditional support of declining sectors. But it is necessary to encourage spontaneous adjust-
should be given to enterprising spirit namely by giving clear guidance as to the new demands (public transport, energy production, technology capable of reducing oil consumption, scientific research, etc.). To this end, greater encouragement should be given to enterprising spirit namely by giving clear guidance as to the type of development to be undertaken.

Active policies on employment and to protect incomes

2.7. To improve the employment situation, specific and concerted policies with the main objectives of increasing the mobility of labour to the benefit of expanding sectors, and of establishing effective arrangements for vocational training and retraining, are also needed, where necessary with the help of Community means. In addition, changes should be made in some member countries in the system of social security, particularly unemployment insurance arrangements, so as to provide the unemployed with suitable benefits. In general an effective method of protecting the incomes of the least well-off social groups would permit further concentration of effort on the restructuring made necessary by the energy crisis.

Financial solidarity

2.8. The process of eliminating the main balance of payments disequilibria must be gradual. An orderly financing of deficits should, thus, be arranged while waiting for the adjustments in real flows to be realised. This would avoid the danger that the deficit member countries would be driven to take protectionist measures likely to retard the recovery of world trade. The Community instruments of financial solidarity have an important rôle to play in this context, jointly with international instruments and with the capital markets. In addition the Community must take and press at the international level for those measures necessary to avoid any damage to the orderly development of world trade.

b) Guidelines for the individual countries

Denmark

3.1. In Denmark, the current phase of near-stagnation is likely to persist throughout most of the year. Unemployment might rise further for some months before becoming stable at a high level. The principal problem for economic policy makers will be to mitigate the effects of the slowdown in economic activity on the employment level without endangering the improvement already under way in foreign trade and domestic equilibrium. The authorities should therefore continue to help reduce the pressure of costs, which is still heavy, but without ruling out possible recourse to selective and gradual action to restimulate activity. The policy measures to be implemented should be adjusted in the light of the degree of moderation shown by the two sides of industry.

3.2. In the budgetary field, the easing of personal taxation has already provided an appreciable stimulus, as have the measures taken in the construction sector; this may have set the stage for a more moderate rise in wages and salaries. If this prospect is fulfilled and if at the same time the balance of payments on current account continues to improve, some of the proposed cuts in intended expenditure could be cancelled in order to sustain the level of economic activity.

3.3. In the monetary field, domestic liquidity has increased at a slightly faster pace during recent months. A further relaxation of monetary policy, and particularly of credit policy in order to improve the financial situation of enterprises, would depend on the success of any incomes policy and on developments in public finance.

Federal Republic of Germany

3.4. Since the middle of last year economic growth in Germany has steadily weakened and has increasingly diverged from the guidelines laid down by the Council. The Federal Government decided, last December, to launch a programme to encourage private and public investment and to get the unemployed back to work. Powerful stimuli should be provided by the sharp increase in the public authorities' borrowing requirement, which is partly due to the tax and family allowances reforms; the deficit in 1975 should be some DM 50,000 million, as against DM 25,000 million in 1974 (5% and 2½% of gross domestic product respectively). At the same time as the Federal Government took these measures, the Bundesbank appreciably relaxed its monetary policy.

3.5. These measures together should bring about a gradual upturn in the economy. Indeed there are already some signs of a recovery in business confidence. Although it is very difficult to evaluate the strength of this improvement, the annual gross domestic product growth rate could reach 3 to 4% by the end of the year. The employment situation should improve. The increase in prices should further slow down, although the foreign balance will remain high.

3.6. In the event that the economic upturn were delayed, it would be right to reexamine the economic impact of the budgetary measures which have been adopted. In the monetary field the goal adopted by the Bundesbank will stimulate expansion while continuing to act as a brake on prices. The Bundesbank should maintain this approach during the months ahead and encourage the continued fall in interest rates in the banking sector, especially if the upward movement of prices goes on slackening.

France

3.7. In France, the current period of economic stagnation is likely to be followed by a gradual upswing during 1975. The labour market situation will probably improve. Fresh progress will no doubt be made in reducing disequilibria. Thus the rise in consumer prices will continue to slow down during the year; it will probably be less than the annual rate of 10% recorded in recent months. Also the trade balance could reach equilibrium before the end of 1975, but some caution is still needed in assessing the openings for exports provided by France's main trading partners.

3.8. The cautious economic policy stance recommended in the Annual report on the economic situation in the Community[1] remains essential so as not to endanger what has been achieved in the field of prices and external equilibrium. Accordingly, the upswing of economic activity depends as much on the growth of investment—particularly to stop a further run-down of stocks—as on export growth.

3.9. The 1975 Finance Act forecasts a slight surplus of the order of FF 500 million. It is desirable that the outturn of the budget should not depart too far from this neutral line. Should the revival in economic growth be slow in materializing, it would be appropriate to consider fiscal measures, for example the deferral of the collection of company taxes.

3.10. The present stance of monetary policy, without being especially restrictive, seems well suited to the current economic situation.

Ireland

3.11. In Ireland the level of economic activity may remain depressed until the end of the year. The labour market situation will scarcely improve in the coming months. The rate of increase in prices will remain among the most rapid of the Community. In this period of slow growth the balance of payments on current account is likely to go on improving. Economic policy should sustain employment through specific measures which do not accentuate the internal push of costs.

3.12. On the incomes front, the wage and salary increases for 1975 written into agreements concluded last year are already very high. It is therefore important that the new national pay agreement does not result in excessive increases, especially in the industries already suffering from special difficulties.

3.13. The 1975 budget presented on 15 January 1975 provides for a very high net borrowing requirement (equivalent to some 13% of gross domestic product); notwithstanding that, the increase in public capital expenditure implies little growth in real terms and appears to be too small when regard is had to the foreseeable development of employment. Therefore budgetary policy should have as its objective the restriction of public consumption.

3.14. Monetary policy, although largely dependent on external factors, should remain cautious in view of the growth in liquidity which will be brought about by the monetary financing of the budget deficit.

Italy

3.15. In Italy, the fall-off in economic activity, which began towards the middle of last year, will no doubt continue until the summer, owing to the persistent

[1] O.J., 28.XI.1974 - C 149.

weakness of private consumers' expenditure and the even greater weakness of investment. But there is a chance that total demand will pick-up somewhat towards the end of 1975. The upward movement of prices during the year, though still very vigorous, will be slower than in 1974. The balance of payments deficit on current account will be significantly lower than the level of last year.

3.16. Short-term economic policy faces a difficult problem: the fight against inflation and the improvement in the external position must remain the prime objective; but it is also most important to stop, and gradually reverse, the process of recession. The solution to this problem requires close cooperation with the two sides of industry, especially in the context of the negotiations to be opened towards the end of the year for the renewal of numerous collective agreements.

3.17. In the field of budgetary policy, the Council directive of 17 December 1974 on the granting of medium-term financial assistance requires the 1975 Treasury deficit to be held to Lit 8 000 000 million and the increase in total Government expenditure to 16%. Within these limits, expenditure linked with investment must be raised. It will be easier to observe the ceiling fixed for the Treasury deficit if the fight against tax evasion is stepped up.

3.18. As regards monetary policy, a ceiling of Lit 24 700 000 million has been laid down in the above-mentioned Council Directive for the growth of total lending during the period from 1 April 1975 to 31 March 1976. Within this ceiling, which must certainly not be exceeded, but which, it seems desirable, should be used as fully as possible, there appears to be a strong case for giving priority to financing productive investment, particularly in agriculture, residential construction, and in the energy and public transport sectors. Furthermore, the monetary authorities should support the current tendency for interest rates to fall, while seeing that these rates remain well above those ruling abroad.

Netherlands

3.19. In the Netherlands, the implementation of the important package of reflationary measures decided on last November and strengthened in February (protection of real personal incomes, support for business investment, easing of wage costs, stimulation of activity in the building sector and in the regions) should allow some increase in production in the second half of the year and curb the growth of unemployment. The rise in consumer prices during the year should not exceed 8 to 9%, the rate at which it has been running for several months. The improvement in the terms of trade, due in particular to the higher export prices of natural gas, could lead to an increase in the already considerable surplus on current account.

3.20. In recent months the upward movement of wage costs has slackened distinctly. It is now essential that this trend should continue and become more pronounced if the relative success in combating inflation is to be consolidated and also in order to contribute towards an upturn in employment and in business investment.

3.21. In the budgetary field, the measures already taken must first of all be given time to produce their full effect on economic activity and employment. For the time being, therefore, nothing need be done other than to implement these measures strictly, though this will be reflected in an appreciable increase in the net borrowing requirement, from about 1% of gross domestic product in 1974 to about 3½% in 1975. So as to combat unemployment, however, the implementation of investment expenditures provided for in the budget should be speeded up.

3.22. In the monetary field, a substantial increase in the central government deficit and a continuing balance of payments surplus would suggest that the money supply will grow sufficiently to support the recovery.

Belgo-Luxembourg Economic Union

Belgium

3.23. In Belgium, where the economic climate has deteriorated distinctly since the autumn and economic policy was relaxed at the end of last year, the growth of activity could be very small in the second half of 1975 and unemployment may become even more widespread. The upward movement of consumer prices, which remained very rapid up to February, may slacken appreciably; the external balance could also deteriorate somewhat.

3.24. In the budgetary field, the reflationary measures taken in late 1974 and early 1975, and also the appreciable rise in unemployment, will mean that the fall in the net borrowing requirement will be distinctly smaller than initially forecast. The budget must be implemented in such a way as to help promote the recovery of investment.

To this end, clear priority should be given to the major job-creating investment programmes already planned under the budget. In addition, the authorities should, if necessary, promote business investment in priority sectors through speeding up the removal of value-added tax which is still levied on investment.

3.25. The measures to combat unemployment in the budgetary field should go hand in hand with the maintenance of the recent tendency to ease monetary policy. In this respect the money supply should be allowed to increase sufficiently and the conditions should be created for a further drop in interest rates. However, a slower rate of increase in wage costs is an important condition for achieving the desired improvement in the labour market situation.

Luxembourg

3.26. In Luxemburg where the recent fall-off in new orders is likely to continue, especially in the iron and steel industry, activity may slow down during the first half of 1975. The rate of growth of consumer prices should fall. The surplus on external account will probably give way to an appreciable deficit.

3.27. As taxable incomes will not grow on the scale expected earlier, there will be a deterioration in the net budgetary position.

3.28. In order to maintain activity in building and construction, credit restrictions could be eased, but care should be taken to avoid the resurgence of inflationary strains.

United Kingdom

3.29. The prospects for the British economy seem to be virtual stagnation in activity between now and the end of the year, continued unemployment, further rapid rises in prices and wages, and a slight lowering in the substantial deficit on current account.

3.30. Reducing the external deficit should remain one of the principal aims of economic policy in 1975. To achieve this it is essential to contain the growth of private consumption in real terms. This implies little change in real incomes. In particular, care should be taken to avoid increases in incomes designed to offset anticipated price rises.

3.31. Given the impact of the upsurge in prices and wages on public authority spending and assuming that policies remain unchanged, the public sector net borrowing requirement must be expected to grow in the 1975/76 financial year. Vigorous efforts should therefore be made to reduce the share of the public sector deficit in GDP, put at some 8% for 1974/75. To this end, the implementation of the budgetary policy announced last November to make substantial cuts in suubsidies to nationalized industries is important. In addition an adjustment of certain indirect taxes to price movements could be considered.

3.32. The present line of monetary policy should be maintained. In order to assist with the financing of the external deficit, interest rate policy should preserve the relative attractiveness of the London money market.

III. CONCLUSIONS

The Commission requests the Council to adopt the guidelines defined above and to invite Member States to adhere to them in the elaboration of their economic policy.

TABLE I

Changes in the principal macro-economic aggregates [a]

Country	Gross domestic product (Volume)			Consumer Prices [b]			Number of Unemployed [b c] (Annual average-thousands)			External balance [b d] (as % of G.D.P.)		
	Percentage change on the average of the preceding year											
	1973	1974	1975	1973	1974	1975	1973	1974	1975	1973	1974	1975
Denmark	3.8	1.5	1	9.3	15.3	14	20	45	70	– 2.3	– 3.6	– 1.8
Germany (Fed. Rep.)	5.3	0.6	1.5	7.1	7.3	6	273	583	850	2.7	3.9	3.7
France	6.0	3.8	2.5	7.2	12.8	11	450	545	740	0.7	– 1.5	– 0.8
Ireland	7.2	1.5	1	11.4	17.0	20	66	65	85	– 6.0	– 12.9	– 9.7
Italy	5.9	4.0	– 1	10.8	19.1	19	668	560	750	– 2.0	– 5.4	– 2.7
Netherlands	4.0	2.0	2	9.0	10.3	10	117	143	170	2.9	2.2	2.4
Belgium	5.4	4.3	1.5	7.1	12.5	11.5	96	102	155	3.0	0.5	0.3
Luxembourg	7.5	4.7	– 1	6.1	9.5	8.5	—	—	—	7.7	1.8	– 6.0
United Kingdom	5.3	– 0.7	2	8.6	15.0	18	630	633	800	– 1.3	– 4.2	– 3.0
Community	5.5	1.8	1.5	8.2	12.6	12.5	(2 320)	(2 676)	(3 600)	+ 0.8	– 0.5	+ 0.1

[a] 1973 : actuals; 1974 : estimates; 1975 : tentative forecasts by the services of the Commission.
[b] On a national accounts basis.
[c] As a result of disparities in definition, the statistics of unemployment cannot be compared between countries, but only reflect developments within each country.
[d] Goods, services and factor incomes, excluding unilateral transfers, private and public; the balance of these transfers, for the whole of the Community amounted to approximately $ 9.000 million in 1974.

TABLE II

Industrial production[1]

(% change on preceding period) [2]

Country	1973	1974						
	IV	I	II	III	IV	Oct.	Nov.	Dec.
Germany (Fed. Rep.)	− 0.1	− 0.6	+ 0.3	− 2.4	− 4.2	− 2.3	0	− 4.2
France	+ 2.9	+ 1.4	+ 0.4	+ 0.3	.	− 1.1	− 2.2	.
Ireland	+ 0.9	+ 6.5	− 2.2	− 0.3	.	.	.	.
Italy	+ 1.4	− 0.4	+ 1.3	− 2.1	− 7.6	− 4.5	− 9.0	− 2.2
Netherlands	+ 3.1	− 0.1	+ 0.5	+ 2.1	.	+ 1.1	.	.
Belgium	+ 2.3	+ 6.9	+ 1.9	− 4.8	.	− 2.5	+ 1.0	.
Luxembourg	+ 4.9	+ 3.5	− 2.7	− 1.1	− 5.1	+ 0.5	− 6.2	− 7.1
United Kingdom	− 1.6	− 6.1	+ 5.2	+ 1.3	− 2.1	+ 0.9	− 0.5	− 4.3
Community [3]	+ 1.0	− 1.3	+ 1.5	− 0.7	.	− 2.4	− 1.6	.

[1] Excluding construction, food, beverages and tobacco. Ireland : mining and manufacturing industries. For Denmark no comparative data available.
[2] Calculated on the basis of the seasonally adjusted indexes of the Statistical Office of the European Communities. Ireland : OECD figures.
[3] Estimates.

TABLE III

Unemployment
(thousands)
(Seasonally adjusted figures)

Country	1973		1974							1975
	III	IV	I	II	III	IV	Oct.	Nov.	Dec.	Jan.
Denmark	20.0	18.7	20.0	34.0	54.3	76.0	77.5	79.0	71.5	95.8
Germany (Fed. Rep.)	295.0	376.6	431.6	560.6	721.4	840.4	833.6	881.6	805.5	698.5
France	409.2	424.3	421.6	436.1	499.4	639.1	595.5	646.1	675.8	691.7
Ireland	66.2	65.2	66.5	67.2	71.6	81.8	75.8	81.5	88.0	97.1
Italy	988.2	970.7	973.0	989.8	1 014.6	.	1 023.9	1 019.8	.	.
Netherlands	117.2	118.1	126.0	134.5	150.8	163.5	159.2	163.3	167.7	169.0
Belgium	106.9	108.0	106.6	109.7	119.9	138.2	133.0	137.9	143.7	151.9
Luxembourg										
United Kingdom	593.8	541.8	575.3	620.7	664.9	666.3	673.0	675.2	650.7	699.1

Quarterly figures = monthly averages.
End of month, except : Denmark : monthly average of weekly count;
United Kingdom : mid-month figures;
Ireland : figures for last Friday of month.

Source: SOEC.

TABLE IV

Consumer Prices

(Percentage increase on preceding period) [1]

Country	1973	1974							1975	Jan. 74 to Jan. 75
	IV	I	II	III	IV	Oct.	Nov.	Dec.	Jan.	
Denmark	3.7	3.9	3.9	3.8	3.8	1.3	1.4	0.6	0.5	14.0
Germany (Fed. Rep.)	2.9	1.9	1.6	0.7	1.6	0.5	0.7	0.3	0.9	6.1
France	2.6	4.2	4.0	3.2	3.0	1.2	0.9	0.8	.	14.5
Ireland	2.9	5.0	4.7	4.3	4.7	.	.	.	.	.
Italy	2.7	5.4	5.2	6.0	6.2	1.9	1.9	0.8	1.3	24.1
Netherlands	2.0	3.2	2.2	2.6	2.5	1.3	0.7	0.4	0.6	10.7
Belgium	2.5	3.8	4.4	4.1	2.6	0.8	1.1	0.7	1.1	15.6
Luxembourg	2.3	3.5	2.4	2.0	2.9	0.9	1.2	0.8	0.6	11.0
United Kingdom [2]	3.5	4.6	5.9	2.1	5.3	2.0	1.8	1.4	2.6	19.9

[1] Quarterly figures; change between ends of period.

[2] Retail prices.

National sources.

TABLE V

Trade balance

Million Eur

(Seasonally adjusted figures)

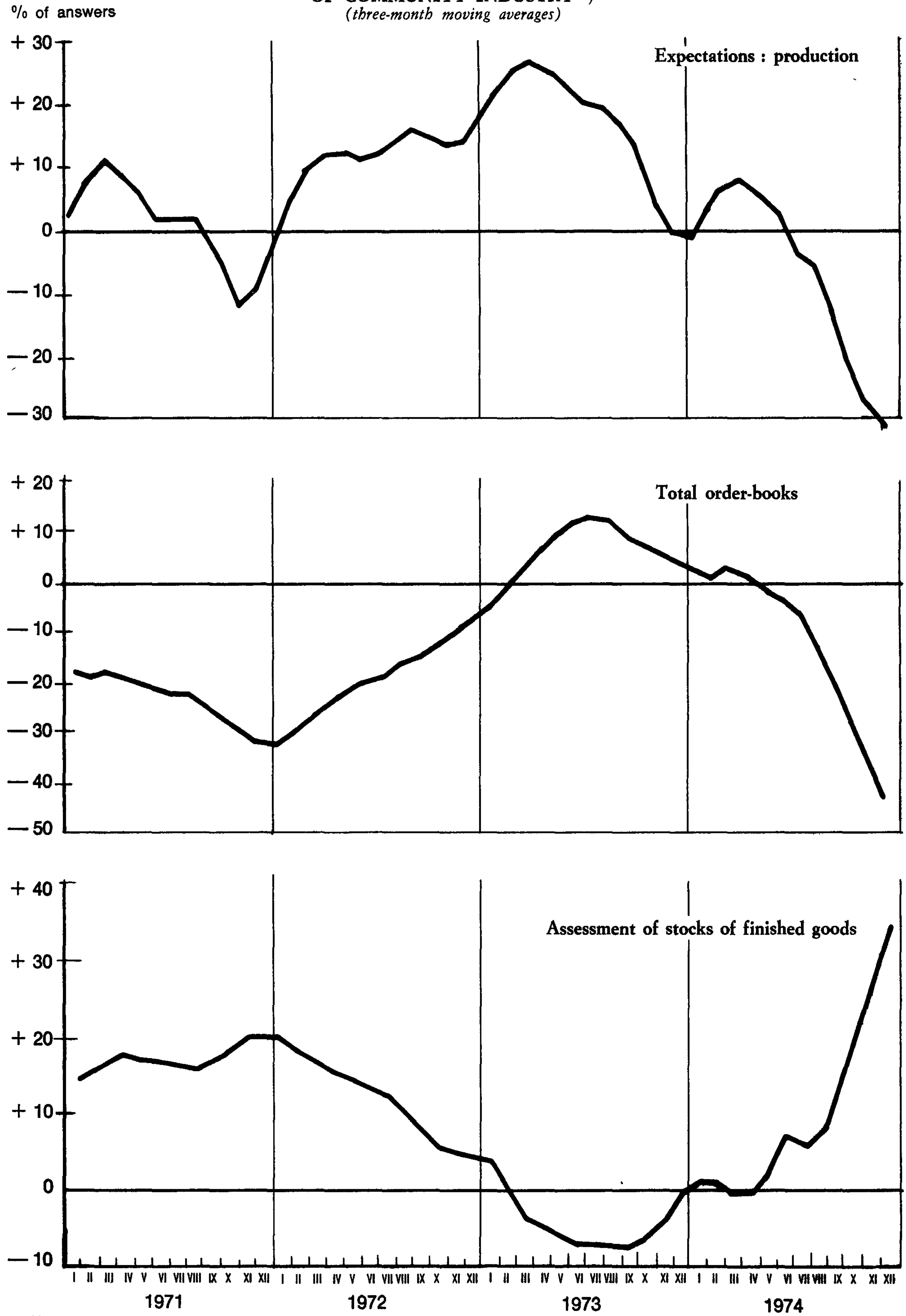
Country	1973		1974							1975
	III	IV	I	II	III	IV	Oct.	Nov.	Dec.	Jan.
Denmark	− 117	− 105	− 210	− 192	− 132	− 90	− 92	− 75	− 102	.
Germany (Fed. Rep.)	+ 997	+ 1 015	+ 1 457	+ 1 310	+ 1 185	+ 1 345	+ 1 158	+ 1 228	+ 1 649	.
France	− 70	− 139	− 508	− 571	− 558	− 389	− 639	− 287	− 241	− 312
Ireland	− 59	− 44	− 87	− 126	− 124	− 59	− 99	− 39	− 39	− 74
Italy	− 506	− 488	− 962	− 1 102	− 992	− 657	− 831	− 606	− 534	.
Netherlands	− 102	− 30	− 25	− 37	− 73	.	− 180	.	.	.
B.L.E.U.	+ 30	+ 38	− 63	− 58	− 77	.	+ 23	+ 59	.	.
United Kingdom	− 699	− 1 020	− 1 236	− 1 674	− 1 201	− 1 319	− 1 160	− 1 689	− 1 108	.

Quarterly figures = monthly averages.

Source: SOEC.

RESULTS OF THE BUSINESS SURVEY [1] OF COMMUNITY INDUSTRY [2]

(three-month moving averages)



1) *Excluding construction, food, beverages and tobacco.*

2) *Original Community.*

Brussels, 17 March 1975

B. Summary account of the Economic Policies pursued in 1974.

(forwarded by the Commission to the Council in accordance with Article 2 of the Decision of 18 February 1974)

FOREWORD

In the new situation created by the energy crisis the economic policies pursued in the Community in 1974 failed to improve significantly the conditions of equilibrium or achieve a greater convergence of the various economies. Work on defining a common energy policy and a common approach to balance of payments problems ran into difficulties, and delays occurred. As regards the member countries' demand-management policies, rates of inflation differed widely from country to country partly because the Governments did not all act with the same degree of promptness or effectiveness. In several countries, monetary policy was the main stabilization instrument, although it probably curbed the propensity to invest to an undesirable extent. Throughout the year budgetary policy in most deficit countries was not sufficiently restrictive or was even reflationary, while in the other countries the operation of built in stabilizers played a large part in the greater stimuli released by budgetary policy in 1974. In addition, it often proved impossible to modify the structure of the public administrations' budgets so as to ensure a better income distribution or to safeguard the most essential investments. Finally, the various economic groups have not, generally speaking, adjusted their demands to the worsening economic situation, and this seems to have aggravated the deterioration in the labour market and delayed the adjustment of production to the new pattern of demand.

I. BUDGETARY POLICY

1.1. As a result of the slowdown in economic activity which occurred during the year, budget revenue in several countries in the Community increased less than forecast, particularly in Germany, Denmark and Ireland. In the other countries, revenues again exceeded the levels budgeted for, thanks to the greater—but purely nominal—increase in incomes and, in the case of France and Italy, to higher taxation introduced during the year.

1.2. Expenditure in all countries, however, continued to exceed expectations, though to differing degrees. The overall expansion in current expenditure, spurred on by rising costs, exceeded the growth in capital expenditure, which bore the brunt of attempts to restrict expenditure. Furthermore, the downswing in the conjunctural situation often necessitated additional expenditure, particularly in the form of unemployment benefits. The resulting built-in stabilization effect helped somewhat, particularly in Germany and Denmark, to sustain economic activity.

1.3. Most Member States used budgetary policy to help regulate the conjunctural situation. In Germany, the automatic reflationary effect of budget execution, effective throughout the year, was backed up by certain measures designed to sustain activity. In December 1973, tax measures which had hampered industrial investment and residential construction had already been dropped and a supplementary programme of expenditure was adopted in February 1974. It was decided, in the summer of 1974, to reform the structure, and the new system came into force in early 1975. The timing of this measure is relatively favourable as far as the conjunctural position is concerned. In addition to these measures, a programme of expenditure—still rather cautions—to assist regions suffering from high unemployment was adopted in September, and followed in December by the granting of a direct business investment premium, a new public investment programme and the introduction of a premium to bring unemployed workers back to work.

1.4. In the Netherlands and in Belgium, the budgetary policies pursued in 1974 also had a reflationary effect. In the Netherlands, the energetic programme for sustaining the conjunctural situation provided for in the draft budget and expanded in November 1974 strengthened this effect for 1975. In Belgium, however, direct taxation cuts in the autumn to assist tax-payers in the lower and middle income brackets have been more than offset by the increase in indirect taxation and by the earlier collection of tax on the income of the self-employed and of corporation tax. The expenditure provided for in the 1975 budget and the decision to implement the entire investment programme should, however, contribute towards sustaining economic activity from the beginning of 1975 onwards. Similarly, the higher taxes and the increased expenditure provided for in the Luxembourg budget should help maintain economic activity.

1.5. Of the countries with heavy balance of payments deficits, France and Italy adopted restrictive budgetary policies—although the latter's deficit remained very large. In Italy, the growth in expenditure was kept within strict limits; if there had not been an exceptional transfer of appropriations to the sickness funds designed to cover the debts of the hospitals, the growth in expenditure would have been no greater than 10%. The increase in indirect taxation, although offset by a slight easing of direct taxation decided last summer, accentuated fiscal buoyancy. In France, the budget eventually yielded a small surplus, mainly accounted for by the special tax levy introduced in June 1974; if there had not been a considerable and exceptional increase in the Government's provisional advances to the local authorities against future tax accruals, the surplus would have been very large.

1.6. In Denmark too, efforts were made throughout the year to use budgetary policy as a means of curbing demand and thereby reducing the current-account deficit. In May, indirect taxation was increased in order to slow down the rise in consumers' expenditure. Nevertheless, the increase in tax revenue was smaller than in the previous year and this meant that, in contrast with the substantial surplus budgeted for, there was in fact a net borrowing requirement.

1.7. In Ireland and the United Kingdom, however, budgetary policies were given a reflationary bias and will not, therefore, help to remedy the divergent price trends and balance of payments situations in the Community. In Ireland, expenditure grew at a more rapid rate and revenue at a slightly lower rate than forecast, with the net borrowing requirement amounting to almost 12% of the gross domestic product. A considerable proportion of the deficit was financed by credit from abroad. In the United Kingdom, the initial budgetary provisions for the 1974/75 financial year aimed at reducing the deficit, but were amended in July and November 1974 by provisions to lighten taxation, mainly on VAT and corporation tax, whilst rapidly rising costs boosted expenditure. The end-of-year deficit is, therefore, expected to be very much greater than the previous year's.

TABLE I

Developments in budget surpluses or deficits

Country	1973		1974	
	Forecast [1]	Outturn [2]	Forecast [1]	Outturn [2]
Denmark (Dkr '000 m)[4]	+ 4.4 (5)	+ 5.5	+ 3.8 (5)	− 2.2
Germany (Fed. Rep.) (DM '000 m)	− 2.0 (5)	− 2.2	− 13.0 (5)	− 19.0
France (FF '000 m)	0.0 (3)	+ 4.8	+ 0.1	+ 2.0
Ireland (£ Ir m) [7]	—	− 209	− 313	− 339
Italy (Lit '000 m)	− 4 560 (8)	− 7 731	− 6 940 (8)	− 7 569
Netherlands (Fl '000 m)	− 2.3	− 0.7	− 2.0	− 2.2
Belgium (Bfrs '000 m)	− 91.1	− 79.9	− 83.2	− 89.0
Luxembourg (Lfrs '000 m)	− 0.7	+ 2.3	− 1.1	+ 2.2
United Kingdom (£ stg m) [6]	− 3 996	− 2 222	− 1 525	− 3 930

[1] Draft budget
[2] Probable outturn
[3] Disregarding the easing of indirect taxation (about FF 7.500 m) which was decided after the Finance Bill had gone to Parliament.
[4] and [6] 1973/74 and 1974/75 financial years.
[5] Forecasts made in June/July of the corresponding or current year.
[7] The 1973 forecast was drawn up in terms of the 1973/74 financial year.
[8] Initial cash forecasts.

Source: Commission services.

II. MONETARY POLICY

2.1. For most of 1974 all the member countries committed their monetary policies to the fight against inflation. This resulted in occasional liquidity shortages whenever interest rates were high. There are several reasons why these policies have not yet slowed down to any appreciable extent the rate of price increases:

(a) Monetary policy measures are felt only after a certain time lag.

(b) The restrictive policies pursued by the various countries were not properly synchronized. At a time when the monetary authorities of the Member States, after the obligation to support the dollar had been removed, gained more scope for manœuvre, it was, however, only in the Federal Republic of Germany and in the Netherlands, that restrictive measures were introduced up to the spring of 1973. In Italy and France the restrictive nature of monetary policy was not

TABLE II

Developments in the monetary situation

	Money supply [1]						Short-term bank credit			Interest rates					
	Annual growth rates, %									Short-term [3]			Long-term		
	1972 [2]		1973 [2]		1974		1972 [2]	1973 [2]	1974	1972 [2]	1973 [2]	1974 [2]	1972 [2]	1973 [2]	1974
	M1	M2	M1	M2	M1	M2									
Denmark	17.1	15.0	10.0	12.7	5.9 (2)	8.9 (2)	12.5	15.4	7.1 (2)	6.0	8.5	9.5 (4)	10.4	12.2	14.6 (6)
Germany (Fed. Rep.)	14.4	16.9	1.8	13.8	10.9 (2)	5.2 (2)	18.8	6.2	8.7 (4)	6.7	11.9	8.4	8.6	9.7	9.4 (7)
France	14.9	18.6	9.7	14.3	16.3 (4)	17.5	18.8	– 0.8	17.8 (5)	7.3	11.2	12.0	8.4	9.8	11.9 (4)
Ireland	16.0	18.2	7.1	25.7	2.1 (4)	17.5 (4)	33.7	22.9	15.5 (4)	7.6	13.5	14.0 (4)	10.3	13.5	15.5 (6)
Italy	17.3	18.2	24.5	23.3	15.6 (5)	19.6 (5)	19.5	17.2	24.0 (8)	6.1	8.2	17.5	7.3	7.4	11.4 (4)
Netherlands	17.6	11.9	– 0.2	22.0	8.4 (4)	21.2 (4)	15.2	34.5	26.6 (4)	3.2	8.8	7.0	7.5	9.0	9.0 (7)
Belgo-Luxembourg Economic Union	14.2	17.5	8.4	14.6	8.7 (4)	10.2 (6)	20.2	19.5	10.6 (6)	3.7	7.2	9.0	7.2	7.8	9.0 (7)
United Kingdom	14.2	25.4	4.5	28.5	8.3 (2)	11.9 (2)	57.1	11.5	15.0 (6)	6.3	9.5	6.8	9.6	12.5	15.7 (5)

[1] M1 : note and coin in circulation plus demand deposits. M2 : M1 plus near-money.
[2] December.
[3] Interest rate on overnight loans; Denmark : 91 day certificates of deposit of the Nationalbank.
[4] November.
[5] October.
[6] September.
[7] January 1975.
[8] August.
Source: Commission services.

strengthened until much later in the year. The timing in the other countries varied between the two extremes.

(c) As inflation rates have increased, the control of the phenomenon has become all the more difficult. The effects of the restrictions were felt only during the second half of the year, mainly in the form of a fall in employment in most member countries. To a large extent, this is because firms and individuals based their pricing and their income objectives on the expectation that inflation would continue or even accelerate. Since the expansion in liquidity has not taken place, money demand has not been sufficient to guarantee full utilization of the production factors in question. Consequently, the restrictive monetary policies initially had a heavier impact on employment than on inflation itself.

(d) In a number of countries, the restrictive monetary policies pursued have lacked proper support from other stabilizing instruments, particularly in the budgetary field.

2.2. Until the autumn, two major monetary stances were observed in the Community. Certain countries, namely the Federal Republic of Germany and the United Kingdom, did not tighten their restrictive policies relative to the previous year. The authorities were more concerned with limiting their effects and introduced cautious measures to ease the situation. In other countries, however, not until 1974 did the monetary policy reach its most restrictive, the main feature often being the tightening of quantitative limits on the expansion of bank credit, particularly in Italy, France, Belgium and Denmark.

2.3. Only towards the end of the year did the monetary policies in all the Member States again converge, becoming more flexible. Very broadly speaking, the Community arrangements for supporting exchange rates facilitated coordination of the policies of the Member States participating in the scheme.

2.4. In most Member States, the money supply expanded less in 1974 than in 1973. However, on a year-to-year basis, the growth rates of the money supply in its narrow definition (M1) again tended to accelerate during the second half of the year in the countries which did not tighten further their restrictive monetary policies in 1974.

2.5. The changes in interest rates reflect the monetary policies pursued. Although the rates were generally high, the trends from country to country were well out of phase. For instance, interest rates in Italy, Belgium and France made up by the autumn the leeway resulting from the increases recorded in 1973 by the other countries. Increases, in some cases large increases, in the discount rate supported the dear money policy pursued in these three countries and in Denmark. By way of contrast, short-term interest rates in Germany, the Netherlands and the United Kingdom had already reached their maximum levels during the first six months of the year. Declining interest rates in the autumn in the United States allowed the countries of the Community sufficient freedom of action to relax their own interest rate policies. Towards the end of the year and in early 1975, the short-term interest rates were tending to ease down in all member countries. Between the middle of December 1973 and the end of January 1975 the discount rate was reduced in six member countries.

2.6. Throughout almost the whole of 1974 capital-market rates were rising or stabilizing at high levels in all the countries. Since savers expected the rates to increase further and since, in a number of countries, the return on short-term investments was higher than long-term interest rates, there was at times a good deal of unrest on a number of financial markets. After short-term rates fell in the second half of the year, the structure of capital market rates reverted to a more normal situation. But it was only towards the end of the year that long-term rates fell in most Community countries.

III. EXCHANGE-RATE POLICY

3.1. In 1974, the international monetary system suffered major disturbances. Exchange rates of all Community currencies fluctuated markedly with respect to the dollar, but most showed a marked tendency to strengthen in terms of that currency. Thus the currencies of those five countries which continued to take part in the Community system appreciated by about 10% against the dollar; the French franc which left the "snake" in January 1974 appreciated against the dollar by 5%, and the pound sterling by 1%. On the other hand the Italian lire depreciated nominally by about 8%.

3.2. Weighted exchange rates have behaved differently from nominal rates (see graph). The five currencies in the Community "snake" have appreciated less markedly, given the importance of trade between those currencies. The lira, the pound sterling and the Irish pound depreciated while, in the second half of the year, the French franc regained some of the ground it lost in the first half-year.

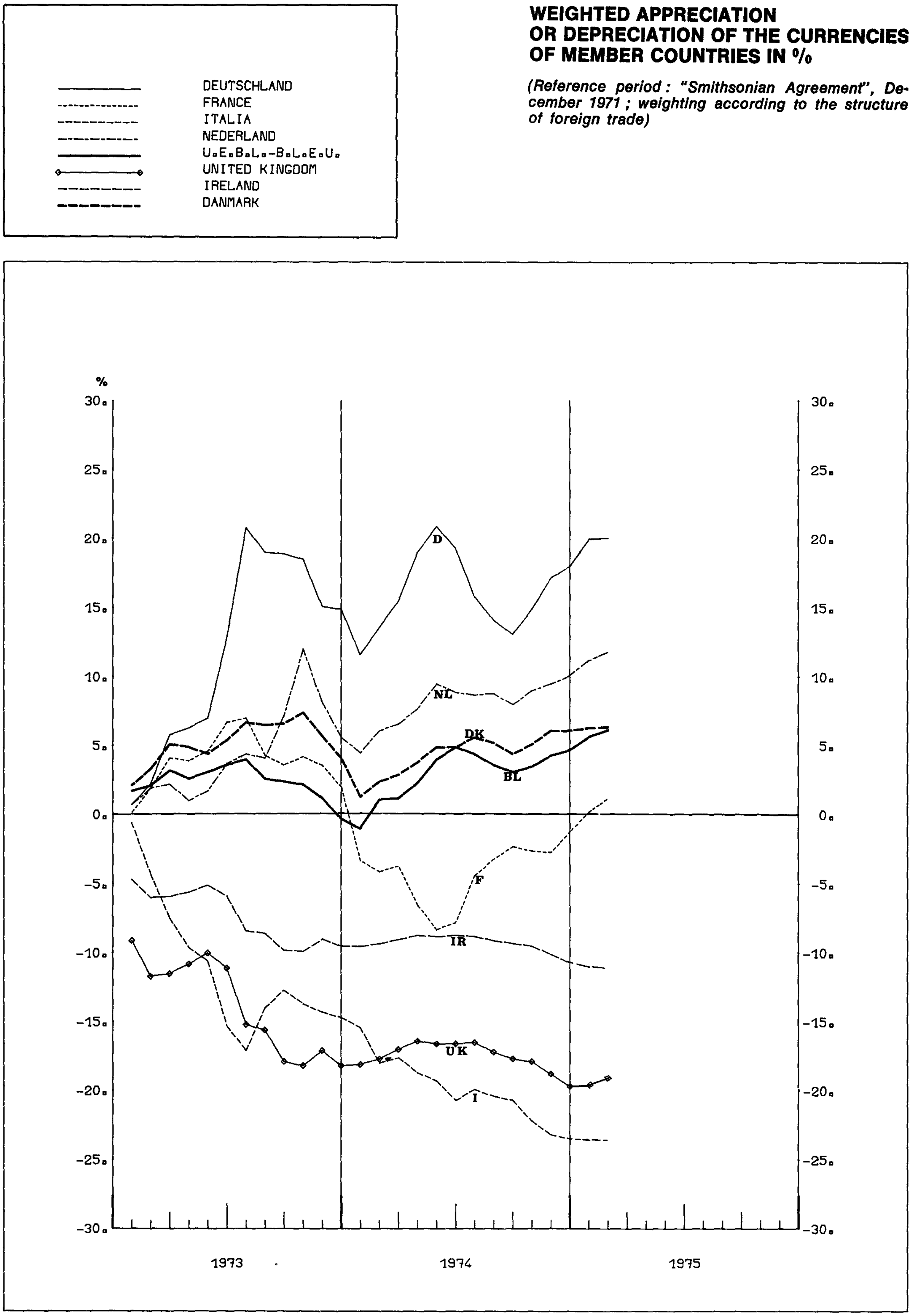
3.3. Among most Community currencies, the divergent exchange-rate movements reflected the trends in balance-of-payments positions. On the one hand, the Federal Republic of Germany, the Netherlands, and the Belgo-Luxembourg Economic Union showed considerable current account surpluses ($ 10,000 million in all), despite the negative effect of the increase in the price of oil on their trade balances. On the other hand, the United Kingdom, Italy, France, Denmark and Ireland suffered severe deterioration in their current accounts, and their overall deficit reached nearly $ 24,000 million.

3.4. Developments in the current balances show very clearly that, at least until now, changes in exchange rates within the Community have not brought about the hoped-for results. This can be explained by the fact that conjunctural policy, in the surplus countries as well as in the deficit countries, has given a greater priority to internal problems than to external disequilibria. Certain governments, after some delay, have tried to reorientate their internal policies in this respect.

3.5. Despite what has happened to current balances, the official reserves of the member countries have not varied much, the only exception being those of Denmark, whose reserves fell 30% during the year. The other member countries managed to compensate largely for their current deficits or surpluses by capital inflows or outflows. In certain countries, official exchange-market intervention has also helped to moderate exchange-rate movements.

WEIGHTED APPRECIATION OR DEPRECIATION OF THE CURRENCIES OF MEMBER COUNTRIES IN %

(Reference period: "Smithsonian Agreement", December 1971; weighting according to the structure of foreign trade)



IV. INCOMES POLICY

4.1. All the Governments in the Community attempted to regulate income growth and distribution, but most of them did so without reference to a clearly defined incomes policy and, generally, employing traditional demand-management instruments. A number of them preferred to rely more on prices policy measures, either temporarily freezing prices, as in Denmark and Italy, or controlling the increase in prices by various means: required prior announcements of price increases in Ireland, Belgium, the Netherlands, Italy and the United Kingdom; selective ad hoc measures in France; subsidies for companies in Denmark to offset the effects of wage increases; food subsidies and subsidies to nationalized undertakings in the United Kingdom. On the whole, the results were rather disappointing, as this type of intervention failed to neutralize the factors pushing prices up. In addition, the public authorities were seldom able to exert any great influence on the agreements negotiated between the unions and managements. Only in the United Kingdom and the Netherlands were real attempts made to lay down a pattern for income growth which was compatible with the overall objectives fixed; in the United Kingdom this took place within Stage Three and later within the "Social Contract" and in the Netherlands in accordance with the Special Powers Act, which allows the Government to lay down the rules under which increases can be decided by collective agreement.

4.2. In a number of countries income redistribution considerations also played a role. For instance, in Denmark and in Germany the tax reforms which were adopted in July and September respectively but which only came into force in 1975 included provision for higher tax-exempt allowances and the introduction of a new tax scale. In other countries, particularly Ireland, the Netherlands and the United Kingdom tax measures were also introduced to lighten the tax burden on the lowest incomes. Indeed, in November, the Netherlands Government announced an actual reduction in wage and income taxes as of April 1975. In Italy an exception was made to the measures adopted in July to restrict domestic demand, namely by raising the basic tax-free allowance.

4.3. Social transfers were also increased in most countries in an attempt to provide better protection for certain sectors of society against the effects of inflation; this was the case in Belgium, Ireland, France, the Netherlands and the United Kingdom. In particular, nearly everywhere retirement and widows' pensions and minimum guaranteed earnings were raised.

4.4. The deterioration in the employment situation induced the public authorities in most countries to raise unemployment benefits and in some cases to extend the maximum periods of compensation.

4.5. The authorities were in addition anxious to encourage saving. Compulsory savings arrangements became operational in Denmark in the autumn for certain income brackets and the amounts of saved income qualifying for tax-exemption were increased in Belgium in July.

TABLE III

Some indicators of the growth of incomes, prices and costs

(Increases as % of preceding year values)

	GNP in value		Change in terms of trade as %		Price of National Expenditure		Wage and Salary Bill		Wage and Salary Bill as % of National Income		Wage and Salary Bill per unit of output		Real wage per head [1]	
	1973	1974	1973	1974	1973	1974	1973	1974	1973	1974	1973	1974	1973	1974
Denmark	15.0	15.0	+ 1.9	− 14	9.9	17.6	14.7	21.1	71.7	74.9	10.5	19.3	4.4	5.8
Germany (Fed. Rep.)	11.5	7.2	− 2.8	− 8	6.8	8.5	13.5	9.8	69.5	71.6	7.8	9.1	5.6	4.7
France	13.6	13.7	+ 1.9	− 18	7.1	13.5	15.1	19.8	67.0	69.9	8.6	15.4	4.9	3.6
Ireland	20.0	9.5	+ 7.5	− 15	12.3	16.9	18.4	19.7	64.2	68.5	10.4	17.9	4.4	1.7
Italy	17.0	19.0	− 10.0	− 18	12.6	19.8	20.0	23.5	64.7	67.1	13.3	18.6	6.5	1.2
Netherlands	12.5	11.1	− 1.0	− 6	8.4	11.8	14.2	15.2	69.8	71.8	9.8	11.3	4.8	4.6
Belgium	13.4	15.0	+ 2.0	− 4	7.7	12.6	14.9	18.5	65.6	67.6	9.0	13.6	6.5	4.5
Luxembourg	19.7	12.0			8.0	12.7	13.6	19.8	70.0	74.5	5.7	14.2	4.7	7.1
United Kingdom	13.1	11.9	− 14.7	− 15	9.5	16.1	14.1	18.3	76.8	81.2	8.4	16.1	3.0	1.8
Community	13.3	12.2	− 5.7	− 14	8.5	13.4	15.0	16.5	69.5	71.7	9.0	14.2	4.9	3.3

[1] Change in wage and salary bill per employed person, corrected by the change in the price of private consumption.

Source: SOEC and estimates by Commission services.

TABLE IV

Wage costs in industry per unit of gross value added at constant prices

(Including construction)

	% increase on preceding year						1970-1974 % increases in national currency	1970-1974 % increases in Eur [1]
	Figures in national currency			Figures in Eur [1]				
	1972	1973	1974	1972	1973	1974		
Denmark	4.0	8.8	18.5	3.0	8.8	18.5	46	44.5
Germany (Fed. Rep.)	4.6	6.9	8.8	9.2	12.4	12.5	32	50
France	6.4	7.6	14.5	6.4	7.6	5.8	39	28.5
Ireland	8.5	8.9	18.5	3.5	– 6.8	13.5	54.5	20.5
Italy	5.5	12.4	17	4.4	– 2.6	4.7	55.5	19.5
Netherlands	3.0	9.7	11	5.7	11.2	14.7	32.5	43
Belgium	7.1	7.9	13	10.0	7.9	13	40	43.5
United Kingdom	9.7	7.5	26	4.7	– 8.2	21.1	60	25
United States	1.2	3.1	8.7	– 6.6	– 10.5	8.1	14.5	– 8.5

[1] Calculated on the basis of figures in national currencies, adjusted for exchange rate variations in relation to the Eur.

Sources: Estimates by Commission's departments.

Brussels, 17 March 1975

C. Report on the application of the Council decision of 18 February 1974 on the attainment of a high degree of convergence of the economic policies of the Member States of the European Economic Community and the conformity of the policies pursued with the objectives set.

FOREWORD

This report is hereby transmitted to the Council pursuant to Article 12 of the Council Decision of 18 February 1974 on the attainment of a high degree of convergence of the economic policies of the Member States of the European Economic Community. The Commission is required by this provision to present each year to the Council, for examination at its meeting in the first quarter, a report on the application of the abovementioned Decision and on the conformity of the policies pursued with the objectives set.
This report is hereby also transmitted to the European Parliament.

I. APPLICATION OF THE DECISION

1.1. No more than a summary assessment of the application of the Decision of the Council of 18 February 1974 is possible. In fact 1974, and in particular the first six months, must be considered as a running-in period, especially as the Council Decision was not finally adopted until the second half of February. It should also be borne in mind when assessing the results that there were no longer any valid medium-term forecasts for 1974 and that the Decision on the adjustments in the economic policy guidelines for 1974 was taken only on 4 July 1974. Moreover, to attain a high degree of convergence of policies, the member countries must not only comply with agreed procedures but also show the unambiguous political resolve and perseverance which have frequently been lacking in connection with the implementation of consultation machinery.

1.2. After these general reservations, some initial comments concerning procedure can now be made:

1.2.1. Article 1 has only been applied since mid-1974. Since then the Council has met each month.

1.2.2. Article 2, which relates to the Council session to be held in the first quarter, was not respected, as the Council did not meet until June to examine the economic situation of the Community and adopt the Decision adjusting the economic policy guidelines for 1974. The Commission had transmitted the relevant communication to the Council in the second half of March.

1.2.3. Article 3 was applied as planned, notably as regards changes in the net borrowing requirements.

1.2.4. In accordance with Article 4, a report was adopted in the autumn and published in the Official Journal.

1.2.5. Article 5, which states that the annual report must be brought to the attention of the national parliaments, has been implemented more in form than in substance and in varying ways in the Member States. It does not appear that this document has had much influence on debates within the national parliaments.

1.2.6. Article 6 will be implemented in 1975, in the course of which a fourth medium-term economic policy programme will be drawn up.

1.2.7. Article 7, on prior consultation on the parities of currencies, was not implemented in a positive way. In fact no country in the "mini-snake" took steps necessitating such consultation. The other currencies were floated prior to the Council Decision.

1.2.8. The provisions of Articles 8 and 9 concerning the methods and bodies for consultation on economic policies were applied only in part. This relates as much to monetary policy as to general economic policy.
The coordinating group on short-term economic and financial policies failed to provide the expected stimulus towards the attainment of a high degree of convergence. Given the existing difficulties and the problems which will arise in the future, the coordinating group should be given a special role in the joint discussion of policies, notably by effective prior discussions.

1.2.9. Article 10 on requests for consultations was not invoked in 1974.

1.2.10. Article 11 on the procedures to be applied in the event of a Member State's policy departing from the guidelines laid down by the Council was not formally invoked in 1974. Reference should nevertheless be made to the many consultations held on the situation in Italy, although these were organized on other legal bases, notably Article 108 of the EEC Treaty.

II. CONFORMITY OF THE ECONOMIC POLICIES WITH THE OBJECTIVES SET

2.1. In all the member countries the economic policies failed by a long way to achieve the degree of effectiveness necessary to reach a high degree of convergence. Their relative failure can to some extent be explained by disturbances caused by external factors and short-run uncertainties, but also in part to internal causes, particularly the lack of whole-heartedness with which measures were undertaken, spontaneous market forces and to the lack of a broadly-based agreement on the policies which should be followed. Moreover, as the Commission has already stressed in the annual report on the economic situation of the Community[1], the coordination of economic policies at the Community level is still insufficient. This inadequacy is also to some extent responsible for the relative ineffectiveness of conjunctural policy.

[1] O.J., 28.XI.1974 - C 149.

2.2. On the one hand, differences between policies and, on the other, differences between objectives have been particularly notable in the following fields:

2.3. *Overall aspects of short-term economic policy*

2.3.1. Each country underestimated either the strength of the recession and the speed with which the economic situation would deteriorate or the seriousness of the risks of inflation. This largely explains the delay with which the surplus countries adopted policies to expand internal demand, and with which some deficit countries set about controlling the growth of domestic demand.

2.3.2. In the Community as a whole, the growth of consumption in 1974 was faster than that of investments, and this will remain so in 1975. This development is not what is required. It reflects rigidity in public expenditure and the fact that some countries pay insufficient attention to the urgent necessity of redeploying resources.

2.4. *Budgetary policy*

2.4.1. The uniformly restrictive stance of budgetary policy, as laid down by the Council for 1974, was changed by the decision of July 4th, 1974, so as to take into account especially the differing incidence of the increase in energy prices on the balance of payments.

2.4.2. Thus, among the countries called upon to practise a tighter budgetary policy, France and Italy have, during the year, taken measures of a mainly fiscal nature, which have tended to increase the budget surplus in the first of these countries, and to decrease the deficit in the latter. A restrictive stance was also adopted by Denmark, even if the balance deteriorated considerably under the automatic effect of a marked slow-down of activity. This, however, was not the case in the United Kingdom where the increase in public spending was greatly speeded up, in part deliberately, for the initially restrictive budgetary stance was relaxed twice by supplementary budgets. Also Ireland has maintained an expansionary budgetary policy.

2.4.3. Among the countries without any balance of payments constraints, the Federal Republic of Germany has allowed automatic fiscal stabilizers to contribute towards a deterioration of the balance, and adopted a consciously expansionary stance in the autumn. The Netherlands has followed a similar policy, while Belgium adopted a policy which involved both increased taxation and a cutback in public investment.

2.5. *Monetary Policy*

2.5.1. The coordination of monetary policy between the Member States was insufficient up to the summer of 1974, and especially so from the spring of 1973 onwards, a period when all the Community countries had given up supporting a fixed exchange rate for their currencies against the US Dollar and thus achieved more freedom of action in monetary policy.

2.5.2. Since the summer of 1974, monetary policy in the Community became more consistent. From then onwards, the very restrictive monetary policy which had been followed in some countries was eased, while other countries which suffered from high inflation and severe balance-of-payments deficits tightened up their policies. Since last autumn, the monetary policy in all member countries, along with that in the major non-member countries, has been, in varying degrees, more relaxed which has shown itself especially by a reduction in interest rates. However, there was no significant progress in the standardization of monetary instruments in 1974.

2.6. *Exchange-rate Policy and the Financing of Balance-of-Payments Deficits*

2.6.1. At the beginning of 1974, the French government decided to float the franc independently. From then on only four Community currencies (the Danish crown, the guilder, the Belgian and Luxemburg francs and the mark) have taken part in the Community exchange-rate system, which the Norwegian and Swedish crowns had already joined.

2.6.2. Towards the year-end, the divergencies in the rates of exchange of Community currencies against the dollar have somewhat narrowed. However, no progress whatsoever has been made towards the re-establishment of a Community exchange-rate system.

2.6.3. Faced with serious balance-of-payments deficits within the Community, the Member States have independently sought sources of finance. They have turned to the international capital market or undertaken bilateral negotiations with oil-producing countries. However, towards the end of the year, some progress in a Community approach to this problem was made when the Council Decision of 22nd March 1971 was implemented for the first time and medium-term financial assistance was granted to Italy. Furthermore, on 17th February 1975, the Council adopted the regulation on Community loans. Finally, at the international level, Member States have taken up an agreed position on the recycling of capital.

III. CONCLUSIONS

If the overall implementation of the Council Decision of 18 February 1974 turned out to be, in general, relatively unsatisfactory it is because the operational framework was often limited.

To achieve greater and durable progress towards convergent economic development in the Community, which is an essential condition for further progress, we need:

— to establish common economic policy objectives;

— to adhere rigorously to the guidelines agreed through the concerted use of national and community instruments.