

**Commission of the
European
Communities**

**Directorate-
General
for Economic
and Financial
Affairs**

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1977**

**The economic situation
in the Community**

This publication appears quarterly. Numbers 2 (June) and 4 (December) are surveys by the Commission of the European Communities of recent developments in and the outlook for the economic situation in the Community as a whole and in each of the Member States. They do not contain economic policy recommendations or guidelines, but are limited in this area to a statement of the conjunctural policy problems arising at Community level and in the various Member States. Number 3 (October) reproduces the Commission proposal for the annual report on the economic situation in the Community. This report, which the Council adopts in the fourth quarter of each year, establishes the economic policy guidelines to be followed by the Member States in the year that follows. Number 1 (March) reproduces the text of a communication by the Commission to the Council concerning the adjustment of these guidelines for the current year. It contains in addition a summary account of the economic policies pursued in the previous year, and a report on the application of the Council decision on the attainment of a high degree of convergence of the economic policies of the Member States and on the conformity of the policies pursued with the objectives set.

**COMMISSION
OF THE
EUROPEAN COMMUNITIES**

The economic situation in the Community

DECEMBER 1977

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The publication of this report is the responsibility of the Commission's departments. The writing of the report was completed on 5 December 1977.

I — The overall situation

The deterioration in the business trend in the Community, which began at the start of 1977, came to a halt at the end of the summer. The improvement in the general economic situation has nevertheless remained modest. The tendency for orders in industry to fall has not continued, there has been only limited recovery in this area, and consumer demand has been the only element in aggregate demand in which some signs of renewed buoyancy are evident. The recovery in industrial production has thus remained very slow. The number of wholly unemployed continued to increase up to September, in line with the growing numbers of young people coming on to the labour market; it subsequently levelled off. The price climate has become more favourable. The inflation rate, for the Community as a whole, has fallen below the level observed in the major countries outside the Community. The improvement in the Community's current balance of payments, under way since the beginning of the year, has continued; it has been brought about by the marked tendency for the trade deficit to fall due to the slowdown in imports.

Despite the stimulatory measures already implemented in some Member States, the economic situation in the Community during the first half of 1978 will probably continue to be marked by a continuing low level of growth in demand and production and by the possibility of a further worsening of the labour market. However, as a result of the progress expected in the fight against inflation and external disequilibria, the room for manoeuvre available for a policy of supporting activity should gradually increase over the months ahead.

A — Economic policy problems

The analysis given here ¹ of the economic situation in the Community and the short-term outlook shows clearly the weakness of underlying trends and the precariousness of the spontaneous improvement expected over the months ahead. In addition, pressures on exchange rates since the summer merely confirm the dangers which not only the Community, but also the whole world economy must face, and the need to apply an appropriate solution jointly to the difficulties involved.

The fairly broad agreement which has just been reached within the Community on the economic policy objectives to be pursued in 1978 ² and on improving coordination of economic policies ³ may to an appreciable extent help to restore economic trends and bring them back into line with the objectives of lasting growth laid down in the fourth medium-term economic policy programme.

In 1977, and more particularly after the summer, several Member States adopted economic policy measures (notably in the budgetary area) whose direct effects in stimulating economic activity may be summed up as follows:

Country	Scale of the measures. as % of GDP
Federal Republic of Germany	1.5 %
France	0.8 %
United Kingdom (financial years 1977/1978 and 1978/1979)	1.5 %
Netherlands	0.8 %
Belgium	0.5 %

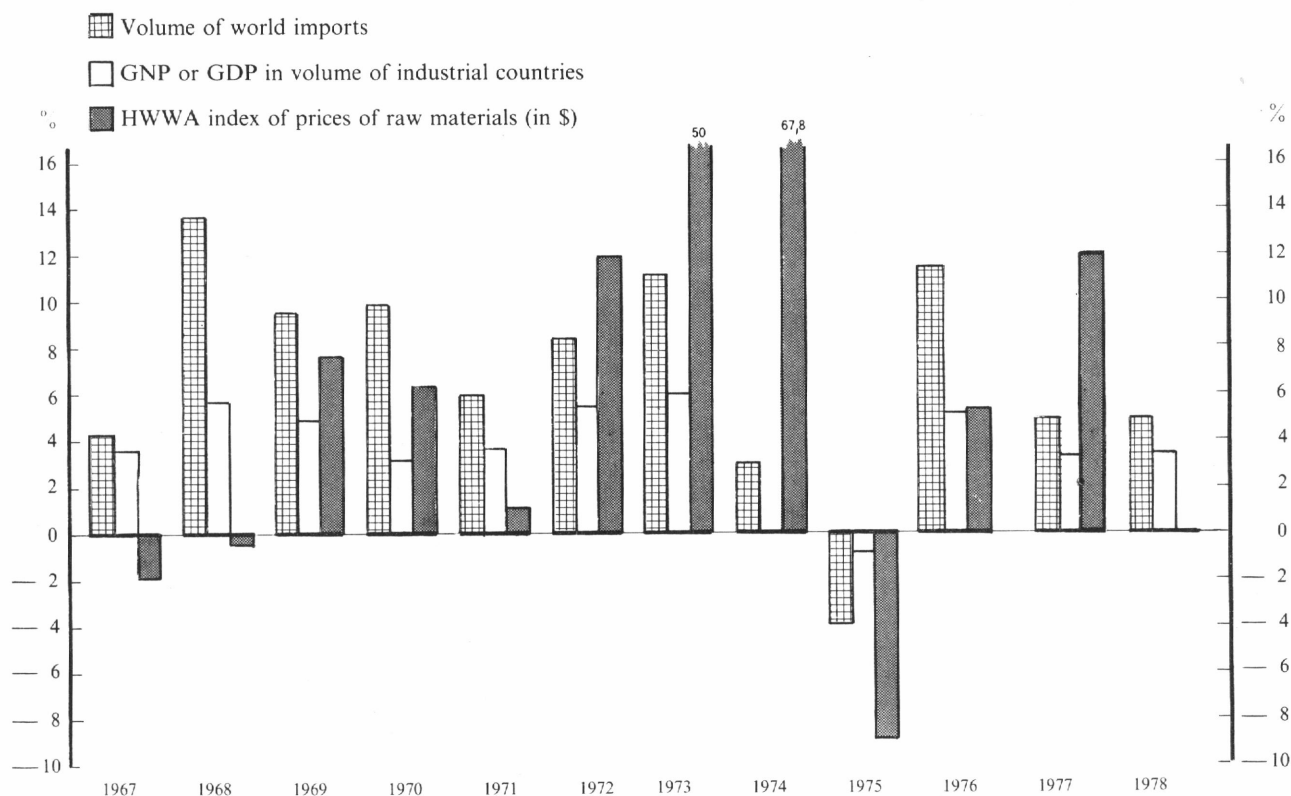
¹ See the following chapters on the Community as a whole and each Member State in particular.

² See Quarterly Survey No 3/1977. The text of the Commission Communication to the Council, of which this document consisted, was approved with some amendments at the Council meeting on 21 November 1977.

³ See Commission Communication on improving coordination of national economic policies (doc. COM(77)443 final of 5 October 1977). During an exchange of views on this document at the Council meeting of 21 November, all the delegations expressed their desire to see greater economic and financial cooperation between Member States.

Production, world trade, and prices of raw materials

(Annual rates of change)



Source: HWWA and departments of the Commission.

In so far as the measures announced by the Member States are implemented without delay, the chances of achieving a growth rate of the order of $3\frac{1}{2}\%$ for Community real gross domestic product in 1978, compared with $2\frac{1}{2}\%$ in 1977 (see Table 1 below), will improve. This rate is admittedly below the $4-4\frac{1}{2}\%$ target adopted by the Community with a view in particular to halting the deterioration in the labour market. However, it would already imply a considerable recovery in underlying trends during the year, so as to achieve a growth rate of the order of 4% at the end of 1978.

The prospects of some slowdown in world economic activity and trade in 1978 does in any case underline the need to achieve a sharp increase in the growth of demand within the Community between 1977 and 1978, by means of additional measures to support activity. The problem arising in this connection is twofold:

- A considerably faster growth of domestic demand in the "strong" Member States is a necessary condition for improving not only the employment situation in these countries, but also the aggregate results for the Community as a whole;
- This condition is, however, insufficient for the objective of overall growth to be effectively achieved.

It is therefore important that the "weak" Member States can also, in so far as progress is achieved in the recovery process, contribute to the desired improvement in the Community economy.

A correlation must be maintained between progress in reducing inflation and external disequilibria and the gradual utilization of the room for manoeuvre thus obtained so as to pursue more ambitious growth and employment objectives. It presupposes close cooperation within the Community between the two sides of industry, the development of appropriate active policies to meet the structural and social problems of the Community, and a greater degree of cohesion so as to allow progress to be resumed towards the achievement of economic and monetary union.¹ It also implies, on the external front, a development of the dialogue aimed at ensuring adequate growth of world trade and averting the ever-increasing threat of protectionism.

¹ In its Communication to the European Council on the outlook for economic and monetary union (doc. COM(77)620 final of 16 November 1977), the Commission put forward the following conclusion: "The pursuit of economic and monetary union would make a decisive contribution towards achieving the common goal of stability and growth. It would strengthen Community cohesion at a time when the prospects of a new enlargement are beginning to open up. Achieving it would be a key factor in re-establishing order in the international monetary system".

TABLE 1

Development of main macro-economic aggregates

Country	Gross domestic product (volume) % changes					Number of unemployed as a % of labour force ¹				
	1970- 1974	1975	1976	1977	1978 ²	1970- 1974	1975	1976	1977	1978 ²
Denmark	2.8	- 1.1	4.8	1.0	1.5	1.3	5.0	5.1	6.2	6.5
FR of Germany	3.6	- 2.6	5.6	2.8	3 ¹ / ₂	1.1	4.1	4.1	4.0	4.1
France	5.1	0.1	5.2	2.7	3.6	2.7	4.2	4.4	5.1	5 ¹ / ₂
Ireland	3.4	0.4	3.2	5.5	5	5.9	7.9	9.4	9.4	9 ¹ / ₂
Italy	4.1	- 3.5	5.6	2.1	3.3	(5.2)	(5.6)	(5.9)	(7.0)	:
Netherlands	4.7	- 1.2	4.6	2.4	2.2	2.1	4.0	4.3	4.2	4.7
Belgium	5.2	- 2.0	3.0	2.8	2.5	2.3	4.5	5.9	6.7	6.4
Luxembourg	4.1	- 8.4	2.7	1.0	1.3	0	0.2	0.4	0.5	1.0
United Kingdom	2.5	- 1.7	1.6	0.4	3.7	2.8	3.9	5.2	5.9	6.8
Community	4.0	- 1.8	4.6	2.3	3.3	(2.8)	(4.4)	(4.9)	(5.5)	(5.8)

Country	Implicit consumer prices % changes					Balance on current account (S '000 million)			
	1970- 1974	1975	1976	1977	1978 ²	1970- 1974	1975	1976	1977
Denmark	7.9	8.8	8.5	10.5	10 ¹ / ₂	- 0.5	- 0.5	- 1.4	- 1.7
FR of Germany	5.8	6.3	4.4	3.8	3 ¹ / ₂	3.3	4.3	3.7	2.1
France	8.3	11.6	9.9	9.5	8 ¹ / ₂	- 1.1	- 0.1	- 5.8	- 3.3
Ireland	10.8	21.3	17.0	13.7	9	- 0.3	0.0	- 0.3	- 0.4
Italy	8.7	17.6	17.5	18 ¹ / ₂	13 ¹ / ₂	- 1.0	- 0.6	- 2.8	1.3
Netherlands	8.0	10.3	9.2	7.0	6 ¹ / ₄	1.0	1.7	2.5	1.1
Belgium	6.3	12.1	8.9	7.1	6.5	1.0	0.3	- 0.4	- 0.2
Luxembourg	6	10.7	9.8	6.8	5.0	1.0	0.3	- 0.4	- 0.2
United Kingdom	9.8	23.5	15.3	15.3	11.2	- 1.2	- 3.8	- 2.5	0.3
Community	7.8	12.9	9.9	9.6	7.9	1.1	1.3	- 7.5	- 0.9

¹ Until 1976 the unemployment rate indicated in parentheses includes for Italy figures supplied by the Ministry of Labour rather than ISTAT. Because of an important change in definition in the unemployment statistics published by ISTAT, data for 1977 is not comparable to previous year.

² Forecast under unchanged policy assumption

Source: EUROSTAT and departments of the Commission

B — The economic situation in the Community

1. Recent developments

After a moderate expansion during the first half of the year, **exports** to non-member countries tended to slow down in the summer. The increase in the third quarter expressed in annual terms, seasonally adjusted and calculated in EUA, was nevertheless 10%. The main reason for this seems to be the slackening of economic activity in all the industrialized non-member countries, but especially in the countries of Western Europe. By contrast, exports to the United States, where the loss of momentum in the economy has been less marked, have steadily expanded. Exports to the OPEC countries have also continued to make gains, though not quite at the

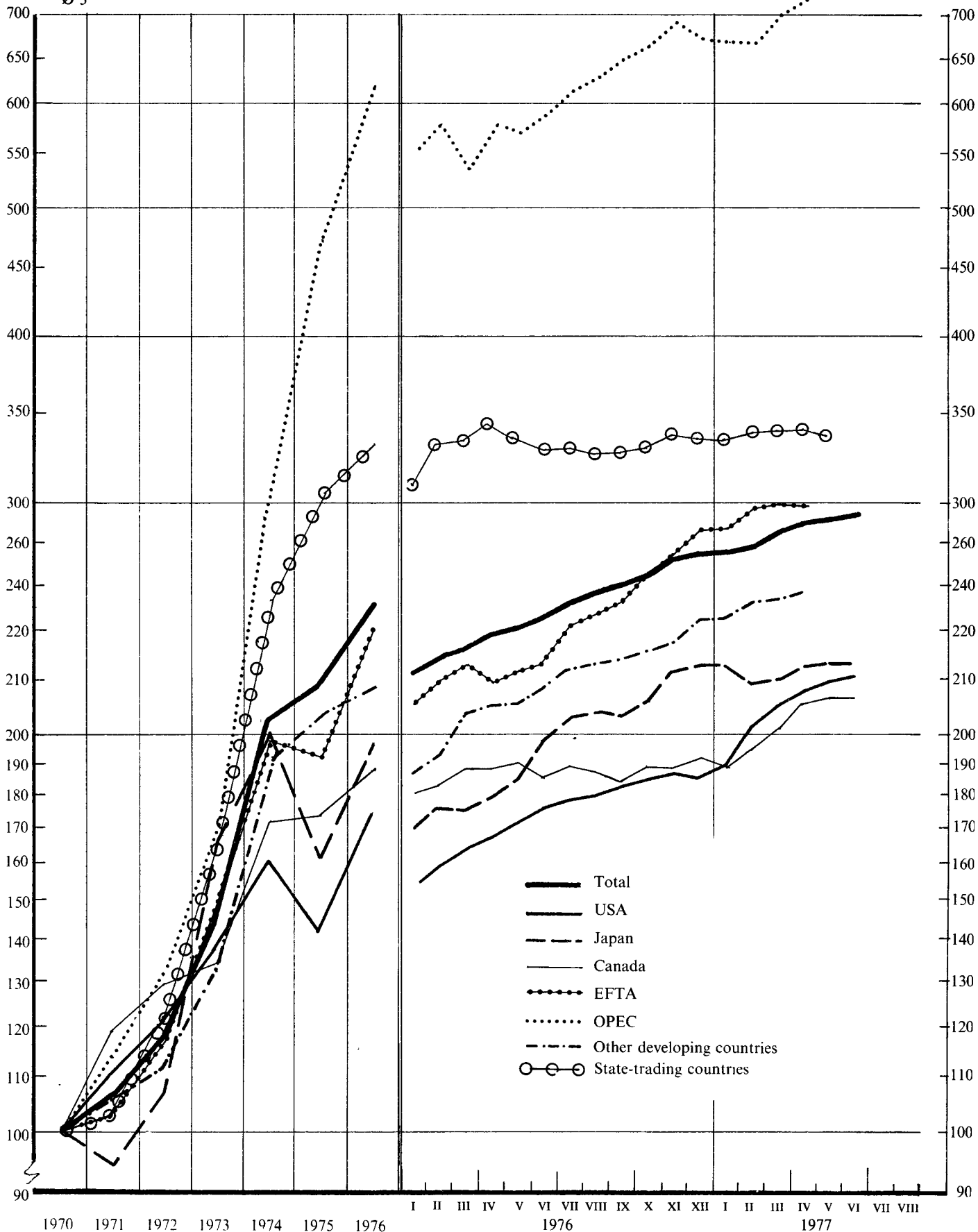
rapid pace previously achieved. Demand in the developing countries has been rising moderately in recent months, but purchases made by the State-trading countries may well have actually contracted in volume terms. For the full year, the expansion of Community exports to non-member countries in volume terms should exceed 7%, a rate slightly higher than the growth rate of the export markets.

Internal demand has scarcely begun to show an improvement, following the changes in economic policy imposed by different Member States during the summer, particularly in the field of budgets. However, fixed **investment** has hardly increased at all in the second half of the year. In

Exports of the Community to the principal non-member countries and groups of countries

(Values in EUA)

1970 = 100
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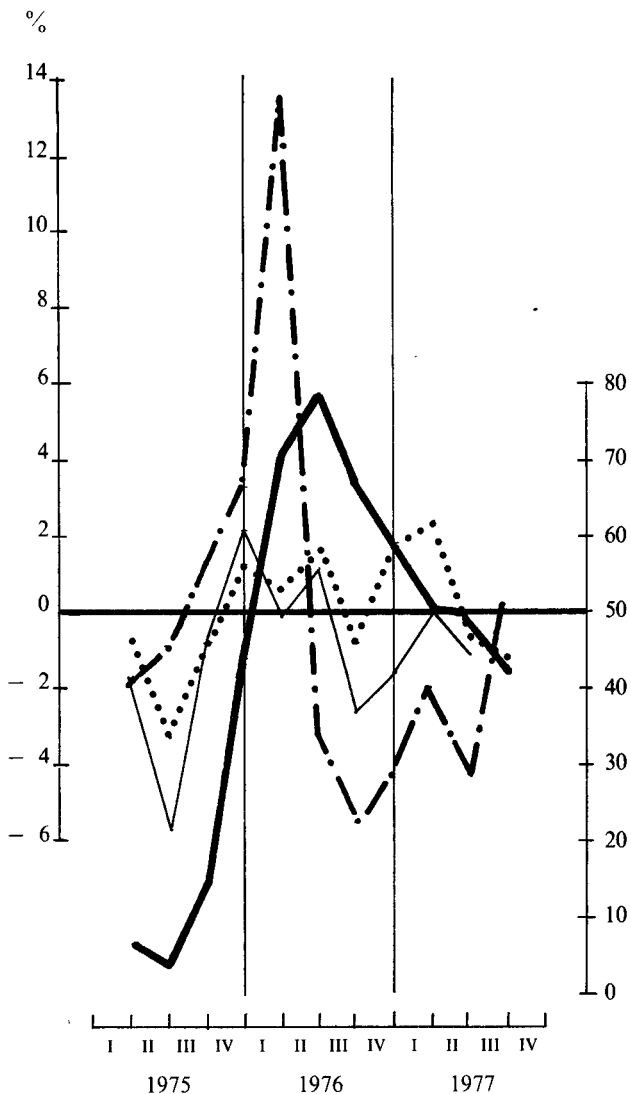


Source: EUROSTAT.

GRAPH C

Indicators of investment activity

- Production in the investment goods' industries ¹
- Diffusion index (sixteen sectors of the investment goods' industries) ²
- . - Building permits (residential) ³
- Production in the building and civil engineering sector ⁴



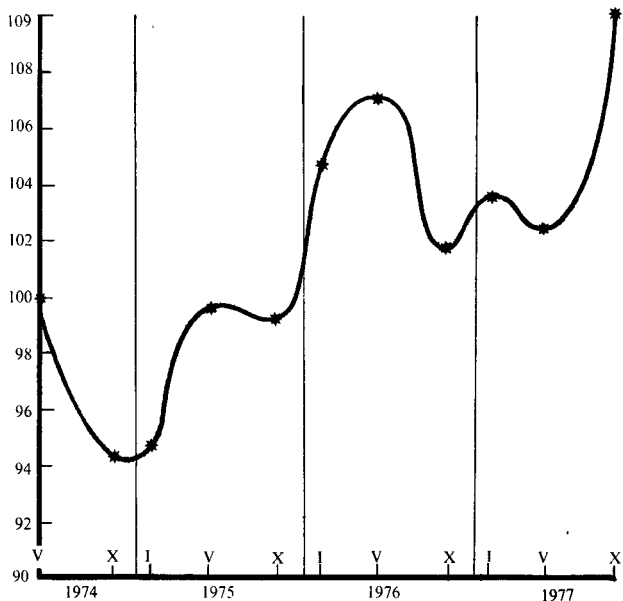
- ¹ Seasonally adjusted index of production (percentage change from preceding quarter).
- ² Positive balances in the production outlook in the investment goods' industries, as a percentage of the 16 sectors taken into consideration. Quarterly averages of seasonally adjusted data. Cf. right-hand scale.
- ³ Excluding Ireland, Italy and the United Kingdom. Percentage change from preceding quarter; seasonally adjusted data.
- ⁴ Seasonally adjusted index of production. Excluding Denmark, Ireland and Italy. Percentage change from preceding quarter.

industry, in particular, many firms were working even further below capacity by the middle of the year than previously, and profits have also recently ceased to improve, so that managements are hesitating to commit funds to investment in additional capacity, despite the further decline in borrowing costs. But the improvement in the availability of funds has no doubt prevented a further slackening of activity in residential construction. With regard to public works, only recently have there been signs of a recovery in some Member States.

In the Community as a whole, private **consumption** seems to have regained a little vigour since last summer. Retail sales have risen again in several member countries, but new registrations of motor-cars have tended to mark time. The strengthening of private consumption is notably attributable to the rather lower saving ratio in several member countries, but without doubt also to an improvement in transfer incomes.

GRAPH D

Index of European consumers' confidence



The index of European consumers' confidence is compiled by taking the arithmetic average of the weighted balances of answers to questions asked about the five following topics in the survey carried out three times a year in the Community: general economic situation in the past and the future, past and future financial situation of households, appropriate time to make purchases.

Source: Commission's Departments.

Industrial production had remained weak from the spring onwards — according to Eurostat's seasonally adjusted index, production had fallen back in July to the average 1976 level — but in September, this supply component began to move ahead in several member countries. However, the overall rate of capacity utilization has shown very little improvement.

TABLE 2
Development of industrial production
(% change on preceding period)

(Seasonally-adjusted figures)

Country	1973	1974	1975	1976	1976		1977					Sept. 1976- Sept 1977
					III	IV	I	II	III	Aug	Sept.	
Denmark	:	:	- 5.7	10.4	0.1	- 0.5	2.1	- 5.6	3.5	11.7	- 2.2	- 1.0
FR of Germany	7.9	- 1.1	- 7.2	7.9	0.4	1.6	2.0	- 0.1	- 2.2	- 0.9	0.0	- 0.6
France	7.3	3.0	- 8.2	8.8	0.7	1.6	2.6	- 2.4	- 1.7	0.8	1.0	- 2.1
Ireland	10.3	3.0	- 7.1	8.6	3.3	0.8	1.2	3.9	:	:	:	:
Italy	9.6	4.7	- 10.2	12.7	0.5	6.5	2.2	- 6.4	- 3.6	- 0.2	1.8	- 4.5
Netherlands	6.1	3.4	- 5.0	8.0	1.5	1.0	0.2	0.3	- 2.1	- 1.7	2.7	- 1.9
Belgium	6.3	4.0	- 10.4	8.4	0.1	2.3	- 0.4	0.3	:	4.3	:	:
Luxembourg	12.0	3.8	- 22.9	6.6	- 3.5	0.4	2.3	2.8	- 4.7	- 1.7	0.6	- 7.7
United Kingdom	9.1	- 2.2	- 4.8	1.0	0.1	1.4	3.1	- 2.3	- 0.4	0.1	- 0.8	0.7
Community	8.0	0.9	- 7.5	7.7	0.6	2.2	2.2	- 2.0	- 2.1	0.0	0.4	- 1.8
Consumer goods	7.3	- 2.6	- 4.9	10.2	1.3	2.3	1.4	- 3.8	1.2	0.9	0.8	0.0
Intermediate goods	8.9	2.1	- 10.1	9.3	1.2	2.4	2.1	- 2.4	- 2.4	- 0.3	- 0.4	- 3.3
Investment goods	6.8	6.1	- 4.8	- 0.1	- 0.8	2.3	2.3	- 0.8	- 1.8	- 0.1	- 0.2	- 0.1

Data not available
Source EUROSTAT

TABLE 3
Development of unemployment

Country	1973	1974	1975	1976	1976				1977			
					I	II	III	IV	I	II	III	Oct.
a) Unemployment rate ¹												
Denmark	0.6	1.9	4.7	4.8	4.9	4.6	4.7	4.8	5.6	5.8	6.0	6.1
FR of Germany	1.0	2.2	4.2	4.1	4.6	4.1	4.0	3.9	3.8	3.9	4.0	4.0
France	1.8	2.3	3.9	4.4	4.4	4.4	4.3	4.3	4.5	4.8	5.2	5.1
Ireland	6.0	6.2	8.7	9.9	9.6	9.9	10.0	9.8	9.6	9.6	9.6	9.4
Italy	5.3	5.1	5.7	6.0	5.8	6.0	6.1	6.1	6.3	6.5	7.3	7.6
Netherlands	2.4	2.8	4.2	4.5	4.5	4.4	4.7	4.4	4.1	4.1	4.4	4.4
Belgium	2.9	3.1	5.3	6.8	6.4	6.6	7.0	7.1	7.2	7.4	7.9	8.2
Luxembourg	0.0	0.0	0.2	0.4	0.3	0.4	0.3	0.4	0.5	0.5	0.6	0.6
United Kingdom	2.4	2.4	3.8	5.4	5.0	5.3	5.8	5.5	5.5	5.5	6.1	5.9
Community	2.5	2.9	4.3	5.0	5.0	5.0	5.1	5.0	5.1	5.2	5.7	5.7
b) Vacancies ²												
Denmark	60.7	14.7	0.8	1.6	1.5	1.9	1.6	1.5	1.2	1.2	1.0	1.1
FR of Germany	219.6	59.0	21.3	22.3	19.4	22.8	22.4	24.7	25.0	22.8	22.0	23.0
France	65.7	44.6	12.3	12.9	11.6	13.0	13.8	13.1	12.2	9.6	9.7	9.7
Netherlands	58.8	55.4	25.0	21.5	19.7	23.0	18.9	24.5	27.1	26.8	27.4	29.0
Belgium	12.4	12.3	1.9	1.5	1.5	1.4	1.4	1.5	1.5	1.3	1.0	0.9
United Kingdom	69.0	50.9	16.7	8.3	8.6	8.2	7.8	8.8	10.9	11.4	10.0	10.5

¹ Number of registered unemployed as % of civilian labour force. Seasonally adjusted data. As definitions are not uniform, unemployment rates are not comparable from country to country.

² Number of vacancies as a % of the number of unemployed persons.

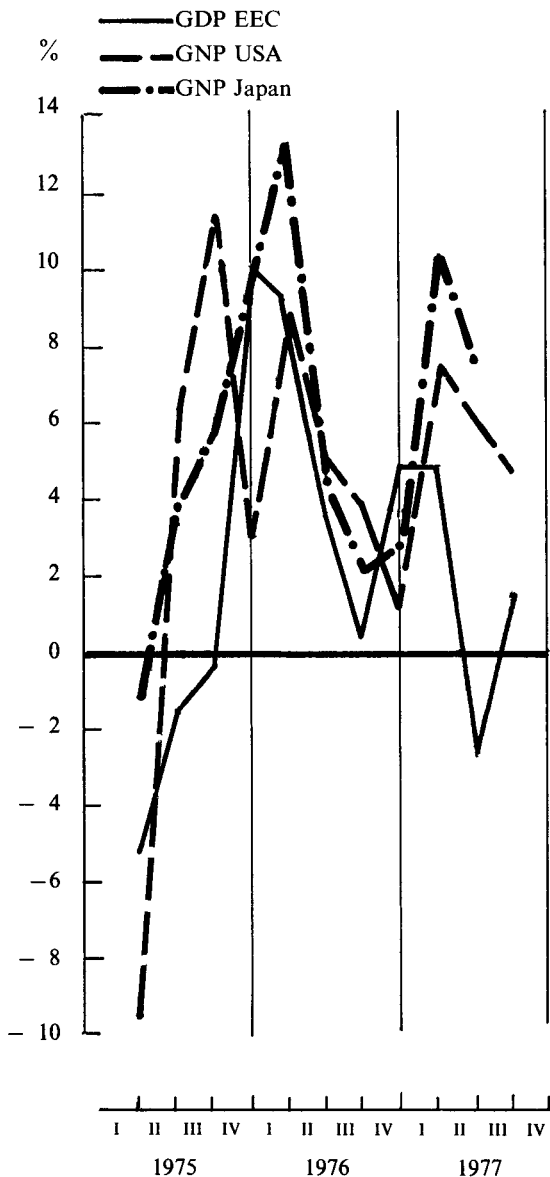
Source EUROSTAT

The services sector and agriculture will grow at only a moderate rate so that the growth of the Community's real gross domestic product is unlikely to reach a figure of more than 2.5% in 1977.

GRAPH E

Growth of the volume of GNP/GDP in the USA, Japan and the EEC

(% change on the previous quarter, expressed as an annual figure seasonally adjusted)



Source: National statistics and departments of the Commission.

Since early 1977, employment in the Community has fallen short of the level recorded during the 1975 recession. In view of the increase in the labour force, this

has necessarily entailed higher unemployment. The seasonally adjusted figure of six million wholly unemployed in the Community for September 1977 is a new record but it did not show an increase in October. The unemployment rate for the civilian labour force was 5.7%, compared with 5% in October 1976. Compared with last year, the number of unemployed persons under 25 as a proportion of the total figure for the wholly unemployed increased in all the member countries, except Belgium. In July 1977 it was more than 37.5% — two million persons — in the Community taken as a whole. Again in the Community as a whole, the number of women unemployed is 43%, and this figure is tending to rise. The number of workers on short time has also climbed steeply in all the Community countries, practically back to the level reached in the 1975 recession. It would seem, however, that this movement came to a halt in the early autumn.

Intra-Community trade, which earlier in the year was helping to boost economic activity, has steadily slowed down since, reflecting the widespread weakness of demand in the Community. At the same time, the trade deficits of several member countries with the other Community countries have shrunk — France and the United Kingdom are cases in point. Indeed, Italy's trade deficit with the other member countries gave way to an appreciable surplus at the beginning of the third quarter.

As a result of slackening internal demand and the availability of North Sea oil, Community imports from non-member countries, showed a decline since the second quarter, the reduction being more marked in real terms. Purchases from the developing countries, having increased mainly because raw materials prices have increased, have been drifting downwards since the springtime. Imports from the OPEC countries have contracted. By contrast, purchases from the industrialized non-member countries, particularly the United States, have continued to expand slowly in certain member countries.

The Community's trade deficit with non-member countries, which had reached a peak early in the year, has fallen steadily ever since. While the trade surplus of the Federal Republic of Germany has still been tending to rise slowly, the position of the deficit countries has shown a consistent improvement. Indeed, in the United Kingdom and in Italy, the trade balance has been in surplus. This was also achieved in France in September and October. On the other hand, the trade balance deficit of the Netherlands and Denmark, countries whose competitive position has apparently deteriorated, has hardly contracted at all. The same applies for Ireland, the only country in which domestic demand has been growing at an appreciable tempo.

The upward price movement has slowed down since the spring in the Community. However, in the autumn, consumer prices generally rose a little faster than during the summer; expressed in annual rates, the increase for the months from August to October was about 6%, compared with 7.2% in the preceding three-month

TABLE 4
Development of consumer prices

Country	% change on preceding year												Oct. 1976- Oct 1977
	1973	1974	1975	1976	1976		1977						
					III	IV	I	II	III	Aug.	Sept	Oct	
Denmark	9.3	15.3	9.6	9.0	1.5	3.9	1.1	3.2	2.5	0.9	1.1	3.5	12.8
FR of Germany	7.0	7.0	5.9	4.6	0.1	0.5	1.9	1.4	0.5	- 0.1	- 0.1	0.1	3.8
France	7.3	13.6	11.7	9.6	2.3	2.6	1.6	3.1	2.4	0.5	0.9	0.8	9.5
Ireland ¹	11.3	17.0	20.9	17.9	1.5	4.2	3.8	3.8	1.1	:	:	:	13.5 ²
Italy	10.8	19.2	17.0	16.7	2.8	6.4	4.7	3.8	2.5	0.9	1.3	1.3	16.4
Netherlands	8.1	9.8	9.9	8.9	0.7	2.5	0.7	2.9	0.6	0.5	0.6	0.4	5.3
Belgium	6.1	12.7	12.8	9.2	1.9	1.7	2.0	1.6	1.5	0.3	0.7	0.2	6.5
Luxembourg	6.1	9.5	10.8	9.8	1.6	1.8	2.3	1.6	0.7	- 0.2	- 0.2	0.4	5.4
United Kingdom	9.2	16.0	24.2	16.5	2.3	4.6	5.0	4.5	1.6	0.4	0.6	0.4	14.0
Community	8.2	13.0	13.8	11.3	1.8	3.3	3.1	3.1	1.6	0.5	0.6	0.7	(10.3)

¹ Quarterly indices

² August 1976-August 1977

· Data not available

Source EUROSTAT

period, whereas in the first half of 1977, the corresponding rate has been nearly 12%. The consumer price upsurge having slackened, particularly in certain countries where inflation had been very high, such as the United Kingdom, Ireland and, to some extent, Italy, the range of inflation rates has also narrowed a little. In their efforts to combat inflation, these three countries will certainly have benefited from the return of relatively stable exchange rate conditions. For all of the member countries, the

prices of finished products in general seem to have increased relatively little, while in general, the increase in food prices has exceeded the average price increase. The disparity between rates of price inflation nonetheless remains very wide. In October they ranged from 3.8% for the Federal Republic of Germany to 16.4% for Italy.

In general, there was no vigorous expansion of the **money supply** in 1977. There has, however, been some evidence in

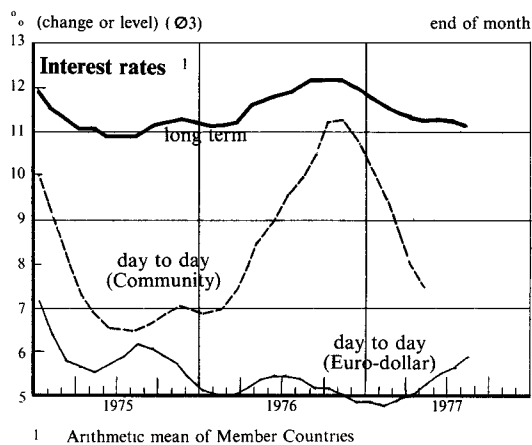
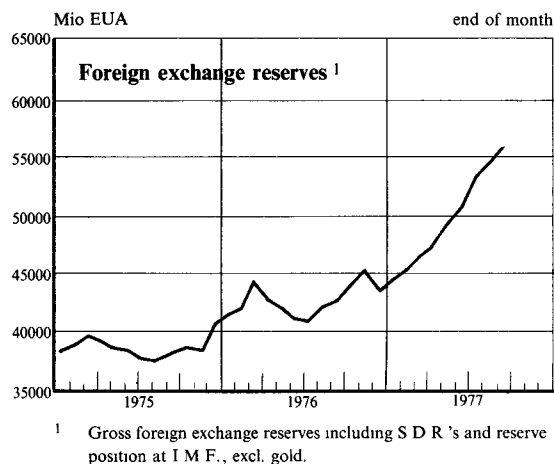
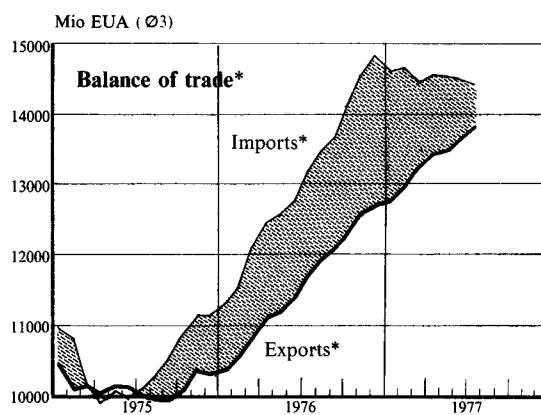
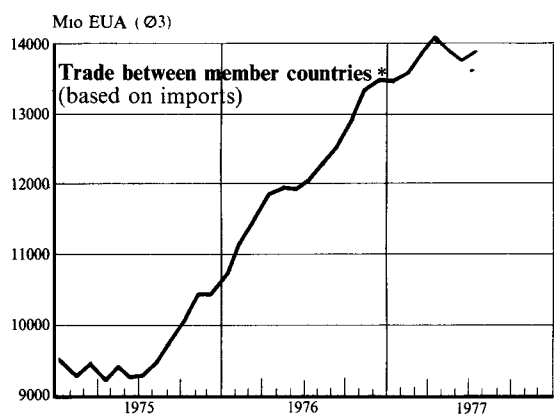
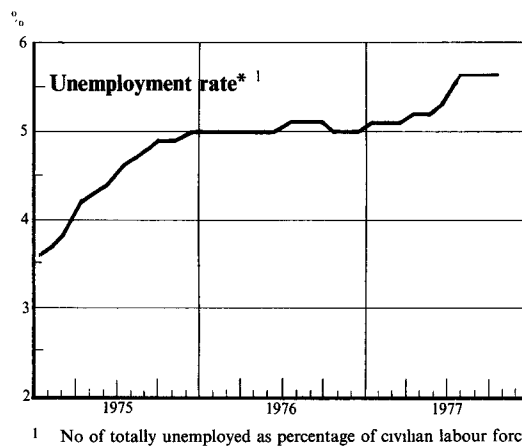
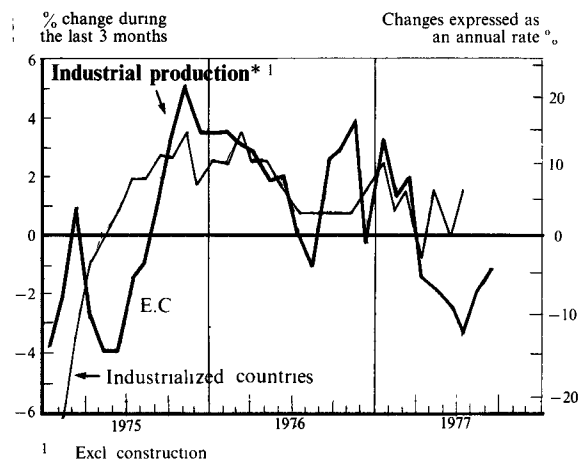
TABLE 5
Development of balance of trade

(Seasonally adjusted. \$ million)

Country	1973	1974	1975	1976	1976				1977		
					I	II	III	IV	I	II	III
Denmark	- 1 584	- 2 306	- 1 348	- 3 188	- 663	- 726	- 819	- 981	- 835	- 859	- 868
FR of Germany	12 976	20 260	15 448	12 994	3 075	3 131	3 314	3 473	3 451	4 106	3 744
France	- 1 428	- 7 141	- 1 894	- 8 291	- 1 460	- 1 480	- 2 400	- 2 951	- 2 518	- 2 121	- 1 487
Ireland	- 684	- 1 211	- 609	- 857	- 274	- 163	- 207	- 214	- 333	- 276	- 206
Italy	- 5 661	- 11 042	- 3 161	- 6 216	- 1 370	- 1 747	- 1 179	- 1 920	- 1 511	- 945	- 102
Netherlands	- 431	- 145	- 745	- 1 170	122	- 598	- 241	- 453	- 672	- 689	- 472
BLEU	369	- 1 580	- 868	- 779	- 256	- 262	- 209	- 52	- 345	- 305	- 87
United Kingdom	- 8 555	- 15 985	- 9 642	- 9 370	- 1 617	- 2 395	- 2 635	- 2 723	- 2 331	- 2 124	- 987
Community ¹	- 4 585	- 20 554	- 4 370	- 19 446	- 3 295	- 4 780	- 5 071	- 6 299	- 5 905	- 3 650	- 590

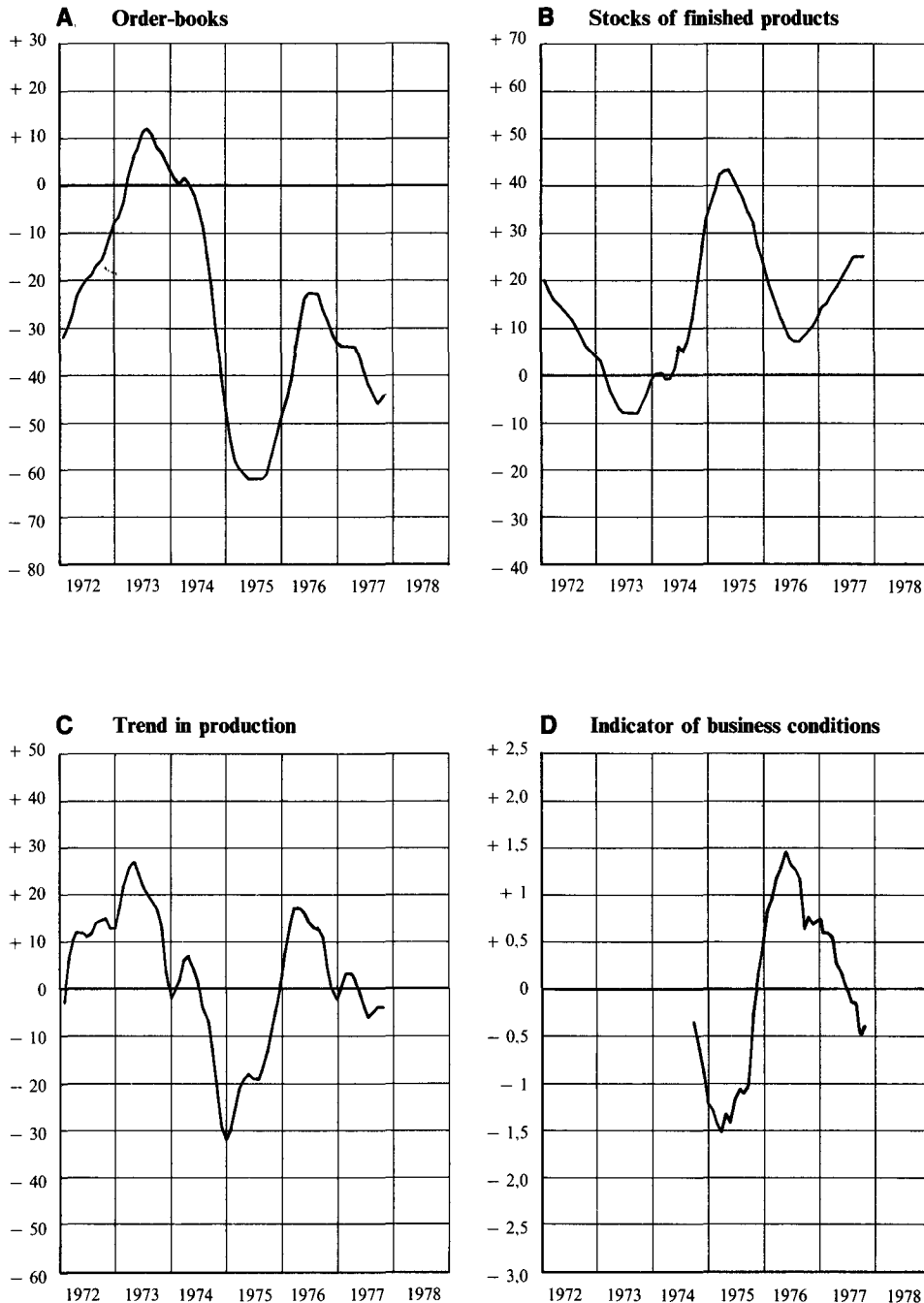
¹ Community + Extra-Community trade

Source EUROSTAT and departments of the Commission



* Seasonally adjusted figures.
 Ø3: Three month moving average.
 Source: services of the Commission.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



NOTE:

These charts are based on answers to questions in the EEC business survey.

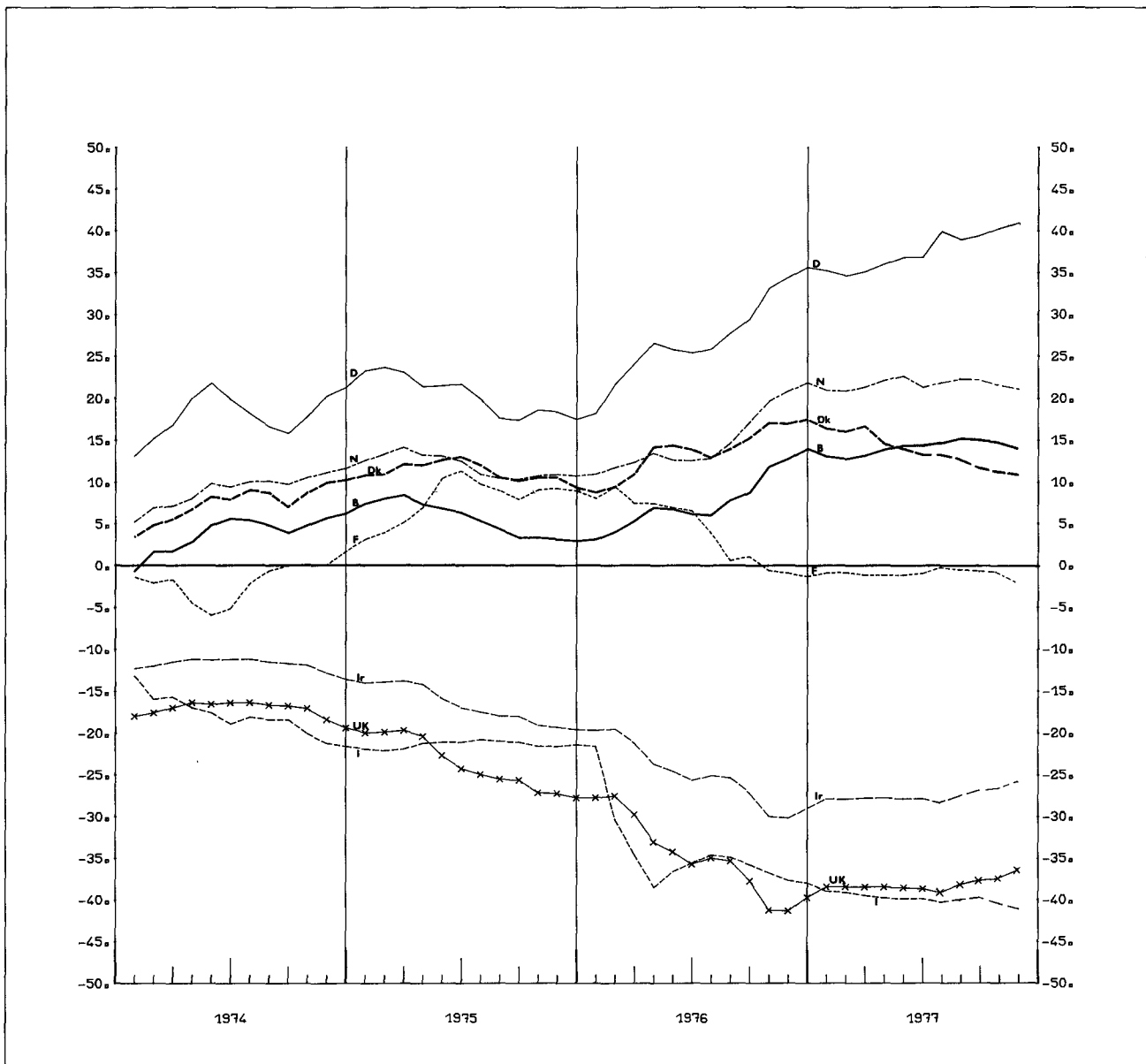
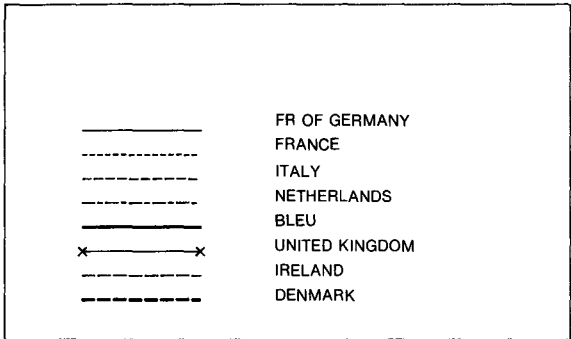
Graphs A, B and C show a three months moving average of the difference between "above normal" and "below normal" answers to the following questions:

- a) Do you consider that your present total order-book is, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- b) Do you consider that your present stocks of finished products are, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- c) Do you think that over the next three or four months your firm's seasonally adjusted production trend will be:
 - (1) up
 - (2) unchanged or
 - (3) down?

Graph D presents an indicator of industrial business conditions, based on a principal component analysis of the answers to four questions in the monthly business survey. These are the above three questions together with a question on the recent trend on production.

Exchange rates

(weighted change in % since first quarter 1972; weighting according to structure of exports)



recent months in the large countries that the rates of growth are beginning to gather momentum once again. In the United Kingdom, this is mainly due to very heavy inflows of capital swelling the exchange reserves, which have climbed from a figure of \$ 4 100 million early in the year to \$ 20 200 million by the end of October. The contribution of general government to boosting the money supply has been much smaller this year than in 1976. The growth of bank lending to the private sector has been quite firm in recent months in a number of Member States.

Short-term **interest rates** generally tended to drift downwards until the autumn, and official discount rates were also reduced. However, in the middle of November, the bank rate was raised in the Netherlands, the first increase in an official rate in the Community since the autumn of 1976. This adjustment was followed at the end of

November by an increase of 2 points in the Minimum Lending Rate of the United Kingdom and in the beginning of December by an increase in the discount rate in Belgium. Long-term capital rates in general tended to lag behind short-term rates in the downward movement, and in some countries showed no change at all.

The development of **exchange rates** during the second half of 1977 was marked by the stability or appreciation of most of the Community currencies, in direct contrast with the weakness of the US dollar. Above all the mark and the pound sterling sustained the pressure of the increase. The German currency regained its strong position in the "Snake" during November and so brought the other currencies to their lower intervention limits. Since the month of November, the British authorities have withdrawn their massive intervention which had aimed to prevent the appreciation of the pound.

TABLE 6
Development of key indicators

Community	Unit	1970-1974 average ^{3 4}	1975 ⁵	1976 ⁵	1977 ⁵	1978 ⁵
Gross domestic product, volume	% change	4.0	- 1.8	4.6	2.3	3.3
Gross domestic product in volume per person in employment ¹	% change	3.7	- 0.4	4.9	2.4	3.2
Total employment (number of persons) ¹	% change	0.3	- 1.4	- 0.3	- 0.1	0.1
Unemployment ⁶	as % of labour force	(2.8)	(4.4)	(4.9)	5.5	5.8
Compensation of employees per wage and salary earner	% change	13.5	16.6	12.8	11.5	10.3
Price index of private consumption ²	% change	7.8	12.9	9.9	9.6	7.9
Current account balance	\$ '000 mio	1.1	1.3	- 7.5	- 0.9	2.3

¹ Domestic concept

² National accounts concept

³ Geometric mean of the change from 1969 to 1974, unemployment and current account balance: arithmetic mean over the five years

⁴ Source: EUROSTAT

⁵ Estimates of Commission's Departments

⁶ The unemployment rate indicated in parentheses incorporates for Italy until 1976 data supplied by the Ministry of Labour rather than ISTAT

2. Outlook

During the first half of 1978, Community **exports** to non-member countries should show some moderate growth. Sales to the industrialized countries could well grow slightly faster; demand from the United States will probably remain firm and it is likely that the purchases being made by the other developed countries will stop declining. In fact, economic activity should speed up a little in the main developed countries in the first half of 1978, as compared with performances in the second half of 1977. But no firm forecast can yet be made as to the scale of this tentative recovery or of its impact on the actual volume of world trade. The volume of exports to State-trading countries could also expand a little, for the

first time since 1975. By contrast, exports to the OPEC countries and without doubt also to the developing countries will probably not grow quite as fast.

In coming months, final **internal demand** should grow a little more vigorously in the Community taken as a whole. In the Federal Republic of Germany, in France, in the United Kingdom and in the Netherlands, official measures approved or planned should help to boost activity. In the other member countries, there is for the time being little prospect of a better business climate. In general, **stocks** in dealers' and manufacturers' hands, which in several sectors have built up to excessive levels, will probably tend to inhibit activity.

Selective measures to spur fixed **investment**, adopted in most of the Member States, combined with a persistent improvement in the availability of funds, should show some results. As the results of the last surveys of investment expectations in industry in the Community suggest, fixed investment should increase a little more in 1978 than it did in 1977. The scale and complexity of the legal arrangements and administrative formalities to be complied with may, however, hinder the execution of big schemes, especially in the energy sector. The recovery in public investment will probably be relatively slow, except

in the Federal Republic of Germany, where a substantial improvement is expected.

Private **consumption** will make a moderate contribution to economic activity in coming months. The confidence of consumers in the further development of the economy, one of the effects of which will be a modest decline in the savings ratio in several Member States, should gain a little strength, not only because of the slowdown in price rises, but also as a result of taxation measures adopted by certain governments to increase the disposable incomes of households.

TABLE 7
Supply and use of resources

Community	1975 ²	1976 ³			1977 ³			1978 ³
	At current prices EUA '000 mio ⁴	Percentage change from preceding year						
		Vol	Price	Val.	Vol	Price	Val	Vol
Private consumption	674.8	3.4	9.9	13.6	2.0	9.6	11.8	3.2
Public consumption	178.3	3.2	9.0	12.5	1.7	8.7	10.5	2.5
Gross fixed asset formation	232.8	2.8	9.2	12.2	1.1	9.1	10.3	2.9
Final domestic demand (excluding stock changes)	1 085.9	3.3	9.5	13.1	1.7	9.1	11.2	2.9
Final domestic demand (including stock changes)	1 077.4	5.1	9.7	15.3	1.6	9.3	11.1	3.1
Exports ¹	283.8	9.8	9.1	19.8	5.4	8.0	13.9	6.1
Imports ¹	273.0	11.8	11.2	24.3	2.9	8.8	12.0	5.6
Gross domestic product at market prices	1 088.2	4.6	9.1	14.2	2.3	9.1	11.6	3.3
Distribution of the change in gross domestic products								
Final domestic demand (excluding stock changes)			3.1			1.7		2.9
Changes in stocks			1.9			- 0.1		0.2
External balance ¹			- 0.4			0.7		0.2

¹ Goods and services.

² Source EUROSTAT

³ Estimates by departments of the Commission.

⁴ For the definition of the European Unit of Account (EUA) see EUROSTAT - Monthly General Statistics Bulletin No 3-1977, table 753, annex

Industrial **production** should continue to expand slowly during the first half of 1978, but there is little reason to expect that firms will be operating much nearer capacity than in 1977. Unless this situation improves noticeably in the second half of 1978, Community real GDP growth is unlikely to exceed 3.5% for the full year.

The moderate expansion of economic activity and fixed investment and the slow improvement in the economic outlook will be insufficient to generate a substantial improvement on the **labour** market. Indeed, with the labour force expanding, it is not certain that the unemployment rate will not increase a little in coming months.

The upward **price** movement has been slackening, and this could well continue: factors now inhibiting inflation — slack demand, more moderate wage settlements in certain countries, a tendency for raw materials prices to rise more slowly or actually fall — are not expected to disappear in the near future. However, inflationary expectations, and the resulting changes in the behaviour of those involved in the economic process, will subside a good deal more slowly. Taking the average for 1978, consumer prices may be expected to show an increase, assuming a moderate rise in oil prices, of about 8% in the Community, compared with 9½% in 1977.

The increase in Community **imports** from non-member countries will be modest in coming months: stocks of raw materials and semi-finished products have built up enough to cover a moderate recovery in industrial activity without this generating a substantial demand for further inputs. However, domestic demand in several Member States could grow a little more vigorously, and this might well increase imports of finished products slightly.

The Community's **trade deficit** will probably contract again in the first half of 1978, so that the tendency for the

current account to improve will continue. But the decline in the deficit might be temporarily interrupted, especially if weather conditions are unusually poor or if the terms of trade suffer a decline.

Major economic policy measures

July:

— On 18 July, the Council, in accordance with its Decision of 18 February 1974, carried out the second quarterly examination of the economic situation in the Community on the basis of a Commission

TABLE 8

Main monthly indicators

Community	Year	Jan	Feb	Mar	Apr	May	June	July	Aug.	Sept.	Oct	Nov	Dec
Industrial production (1970 = 100)	1975	109.1	110.0	109.7	105.8	105.3	105.1	104.1	104.4	105.9	107.3	109.5	109.5
	1976	111.3	113.6	113.1	114.4	115.5	115.3	114.4	114.4	118.4	117.9	118.9	118.2
	1977	121.7	120.4	120.6	119.8	118.1	117.6	115.9	115.9	116.3			
Orders	1975	- 59	- 60	- 62	- 62	- 62	- 63	- 62	- 63	- 59	- 51	- 49	- 47
	1976	- 40	- 36	- 26	- 25	- 22	- 23	- 25	- 24	- 30	- 31	- 34	- 34
	1977	- 35	- 34	- 33	- 37	- 40	- 41	- 46	- 46				
Unemployment rate	1975	3.6	3.8	3.9	4.2	4.2	4.4	4.6	4.7	4.8	4.9	5.0	5.0
	1976	5.0	5.0	5.0	5.0	5.0	5.0	5.1	5.1	5.1	5.0	5.0	5.0
	1977	5.1	5.1	5.1	5.2	5.2	5.3	5.6	5.7	5.7	5.7		
Consumer prices	1975	1.4	1.0	0.9	1.6	1.5	1.0	0.5	0.4	0.8	0.8	0.8	0.7
	1976	1.0	1.1	1.0	1.5	0.9	0.4	0.3	1.8	0.1	1.3	1.0	0.8
	1977	1.2	1.0	0.8	1.4	0.8	0.7	0.3	0.5	0.6	0.6		
Wholesale prices	1975	1.6	0.3	0.4	0.2	0.7	0.1	0.2	0.9	0.5	0.7	0.6	1.3
	1976	1.2	1.5	1.6	2.3	1.5	0.3	1.1	0.8	0.9	0.9	1.3	1.4
	1977	1.4	0.9	0.5	0.9	1.2	- 0.2	- 0.1	0.1	0.6			
Intra-Community trade (million EUA)	1975	9 370	9 503	9 031	9 983	8 673	9 676	9 502	8 821	10 080	10 322	9 910	11 017
	1976	10 257	11 011	11 984	11 826	11 842	12 199	11 804	12 120	12 915	12 605	13 339	14 096
	1977	12 912	13 327	14 776	13 582	13 889	14 255	13 292	14 181				
Exports of goods (million EUA)	1975	10 309	10 188	9 842	10 443	9 837	10 213	10 301	9 570	9 981	10 354	9 972	10 809
	1976	10 201	10 165	11 442	10 950	10 976	11 664	11 602	11 850	12 347	11 905	12 619	13 420
	1977	12 142	12 651	13 974	12 961	13 367	14 147	13 313	14 085				
Import of goods (million EUA)	1975	11 097	10 253	9 621	10 591	9 487	10 039	10 434	9 808	10 715	11 055	10 733	11 693
	1976	11 024	11 247	12 401	12 669	12 238	13 004	13 059	13 474	13 870	13 611	14 773	15 219
	1977	14 521	14 216	15 303	13 949	14 353	15 407	13 772	14 151				
Trade balance (million EUA)	1975	- 787	- 65	222	- 148	351	174	- 133	- 237	- 734	- 700	- 761	- 884
	1976	- 824	- 1 082	- 959	- 1 719	- 1 253	- 1 340	- 1 457	- 1 624	- 1 522	- 1 706	- 2 153	- 1 799
	1977	- 2 379	- 1 566	- 1 329	- 988	- 986	- 1 262	- 459	- 66				
Gross official reserves (gold excl., million EUA)	1975	38 216	39 071	39 928	39 258	38 863	38 445	37 130	37 053	37 089	38 953	38 671	40 682
	1976	41 163	41 785	44 529	42 530	41 488	40 803	40 771	42 162	42 611	44 381	45 118	43 213
	1977	44 636	45 215	46 411	47 355	49 388	50 672	53 587	54 527	55 821			
Exchange rate 1 EUA = \$	1975	1 273	1 293	1 308	1 288	1 302	1 302	1 240	1 195	1 175	1 182	1 180	1 166
	1976	1 165	1 158	1 130	1 114	1 108	1 098	1 097	1 101	1 107	1 108	1 110	1 122
	1977	1 121	1 117	1 120	1 125	1 129	1 130	1 149	1 143	1 138	1 154		

Source: EUROSTAT and Commission's Departments

Industrial production: excluding building and construction, seasonally adjusted.

Orders: balance of above normal (+) and below normal (-) replies to business surveys

Unemployment rate: number of unemployed relative to civilian labour force, seasonally adjusted

Consumer prices: percentage change from preceding month

Wholesale prices: percentage change from preceding month

Intra-Community trade: on imports basis, seasonally adjusted

External trade: trade with non-member countries; seasonally adjusted.

Not available

Communication on economic policy for 1977 and the preparation of public budgets in 1978.

August

— On 28 August, the Ministers for Finance and the Governors of the Central Banks of the countries belonging to the Community exchange rate system decided to devalue the Danish and Norwegian krone by 5 % against the currencies of the other countries and to bring to a temporary end the participation of the Swedish krona in the European "snake".

October

— On 17 October, the Council examined the measures required by the present economic situation and approved the strategy for 1978 proposed by the Commission:

- (i) a growth rate of at least 4 to 4½ % for Community real GDP, to be achieved through an additional 1 % increase in internal demand, without entailing any increase in production costs;
- (ii) an improvement in the labour market situation through a more active employment policy, better vocational training and greater mobility of the labour force;
- (iii) reducing the inflation rate in the Community to 8 %, with the spread between extreme rates being brought down to a range of 4 to 10 %.

November

— At its quarterly meeting held on 21 November 1977, the Council of Ministers for Economic and Financial Affairs:

- (i) adopted the annual report on the economic situation in the Community and the economic policy guidelines for each Member State for 1978;
- (ii) noted, with regard to short-term credit machinery, the intention of the Committee of Governors of the Central Banks to double debtor and creditor "rallonges" and to examine the problem of an increase in quotas at the next five-yearly review due to take place before March 1979. With regard to medium-term credit machinery, the Council, on the basis of an opinion submitted to it by the Monetary Committee, expressed itself favourably disposed towards the suggestions made in this connection by the Belgian presidency in July and invited the Commission to present proposals on the matter as soon as possible;
- (iii) held an exchange of views on the Commission Communication on improving coordination of national economic policies; all the delegations expressed a desire for better coordination of Member States' economic and financial policies;
- (iv) agreed in principle on the text of the directive laying down arrangements for mutual assistance by the tax authorities of the Member States in the field of direct taxation;
- (v) agreed on a first directive on the coordination of laws to facilitate the taking up and pursuit of the business of credit institutions.

II — The situation in each of the Community countries

A. Denmark

The overall performance of the Danish economy has remained modest over the past few months. The level of activity has weakened and unemployment has increased. Prices have continued to rise rapidly and the current balance of payments has been slow to improve.

The authorities have adopted a more strict management of domestic demand by means of an increase in taxation in order to reduce imports and have taken selective measures to improve employment.

This strategy is unlikely to modify unduly the behaviour of the economy where in the coming months the growth of demand and production will remain very weak. The current balance of payments deficit should, however, be appreciably reduced.

1. Overall assessment and main policy issues

In the course of the past few months, the overall position of the Danish economy has been influenced unfavourably by the international environment. Two factors, in this respect, have played an important role: the reduction in demand from Sweden and the United Kingdom and the increase in import prices in the first half of the year. In addition, the trend towards a loss in market share for industrial products resulting from the substantial increases in costs in the past has continued. Accordingly, the balance of payments constraint has remained strong; the current account deficit has only moderated slightly and should reach some DKr 10 000 million in 1977 (or around 3½ % of GDP).

The weak level of activity, which for the year 1977 as a whole will mean a growth rate of real gross domestic product of around 1 %, has resulted in a persistent trend towards an increase in unemployment, despite the

measures taken at the beginning of the year to support employment.

Faced with these necessities (reduction in the external deficit and improvement in the employment situation) the authorities took at the beginning of September new economic measures¹ within the framework of a multi-annual² stabilization programme. These comprise a range of fiscal measures as well as policies on employment, designed to divert demand towards those areas with a low import content, by favouring public expenditure and investment at the expense of private consumption. The strengthening of taxation was achieved by means of an increase in the VAT rate which rises from 15 to 18 %, increases in excise duties as well as some higher public service charges and registration fees. So far as employ-

¹ See list in annex

² For the period 1977-1980.

ment is concerned, additional expenditure credits are provided for energy conservation, public investment projects, additional jobs in the public service, support to certain private firms and special retraining programmes.

In parallel to this voluntary adjustment process achieved by a more stringent management of domestic demand, the success of which relies on a strengthening of world demand, the authorities have become involved in an externally imposed readjustment: that of the further ¹ nominal devaluation of the currency as against the EMUA (5%) on 28th August in order to limit the effects on Danish exports to Sweden of too strong a depreciation of the currency of its second largest trade partner. The risks created by the dual orientation of fiscal and

exchange rate policy will be noticeable on the inflation front. Indeed an additional increase in consumer prices of the order of from 4 to 4½% can be expected as a result therefrom. ²

Monetary policy has remained relatively restrictive; severe restraint on domestic credit and high interest rates have prevailed despite some recent relaxation in order to encourage businessmen to borrow abroad. Over the past few months the money supply (M2) has continued to grow at an annual rate below 10%.

¹ The first two were on 18th October 1976 and 1st April 1977.

² 3% from the fiscal measures.

TABLE 1
Key indicators

Denmark	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁵	1977 ⁶
Gross domestic product, volume	% change	2.9	- 1.1	4.8	1.0
of which: industry ¹		4.0	- 5.5	7.4	2.5
Gross domestic product in volume per person in employment	% change	2.3	0.9	3.0	1.9
Total employment (number of persons) ²	% change	0.6	- 2.0	1.7	- 0.9
— Independent entrepreneurs		- 2.2	1.1	- 1.3	- 0.6
— Wage and salary earners in company sector		- 0.5	- 5.2	1.7	- 2.9
— General Government		6.5	3.1	3.8	3.0
Unemployment	as % of labour force	1.3	5.0	5.1	6.2
Compensation of employees per wage and salary earner	% change	12.5	15.0	11.7	8.0
Price index of private consumption ³	% change	7.9	8.8	8.5	10.5
Current account balance ³	DKr '000 million	- 3.2	- 2.9	- 11.5	- 10.0

¹ Excluding construction (but including repair and maintenance)

² Domestic concept

³ National accounts concept, on annual basis

⁴ Geometric mean of the change from 1969 to 1974. unemployment and current account balance: arithmetic mean over the five years

⁵ Source: Danmarks Statistik

⁶ Estimates of Commission's Departments

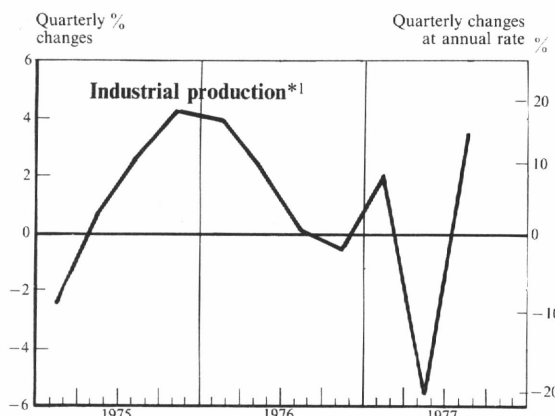
2. Recent developments

In the past few months activity in the Danish economy has been more or less stagnant, unemployment has shown a persistent upward trend, consumer prices have increased quite quickly and the balance of payments deficit, although reduced, is still high.

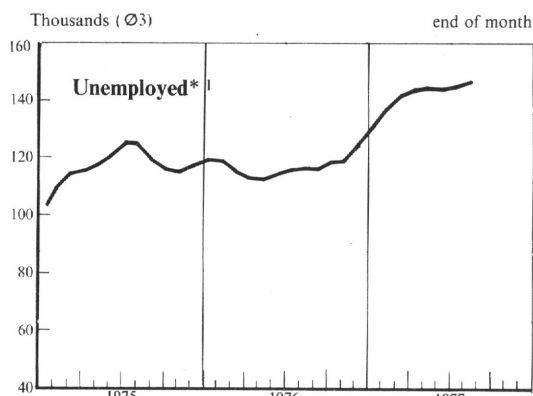
Total exports have only grown slowly (3% in value in the period August-October on the preceding three months) due to the weakness of demand in major trading partners (United Kingdom and Sweden) which could also be due to the effect of the exchange rate on competitiveness.

Domestic demand has weakened. Undoubtedly private **consumption** has progressed markedly in the third quarter (the retail sales volume index rose by 4½% on the second quarter). This development however is explained mainly by anticipatory buying in August and September before the tightening of indirect taxation.

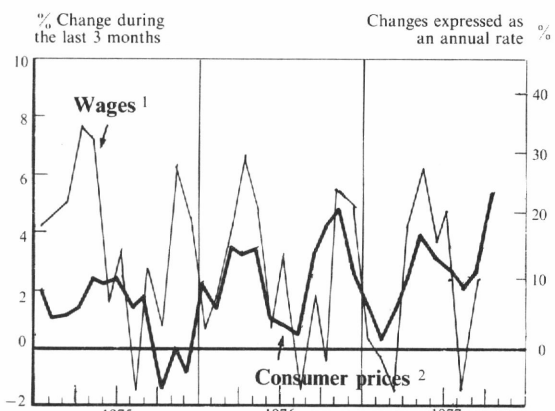
Despite a recent improvement in the trend in certain capital equipment sectors, **investment** has, on the whole, continued to falter. Despite a slight recovery in the industrial and commercial buildings sector activity has remained weak in construction. The number of housing starts fell by 10% in the third quarter.



1 Volume of sales, manuf. industry.



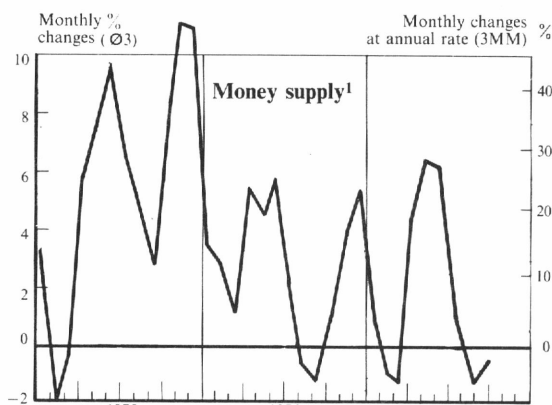
1 Insured unemployed.



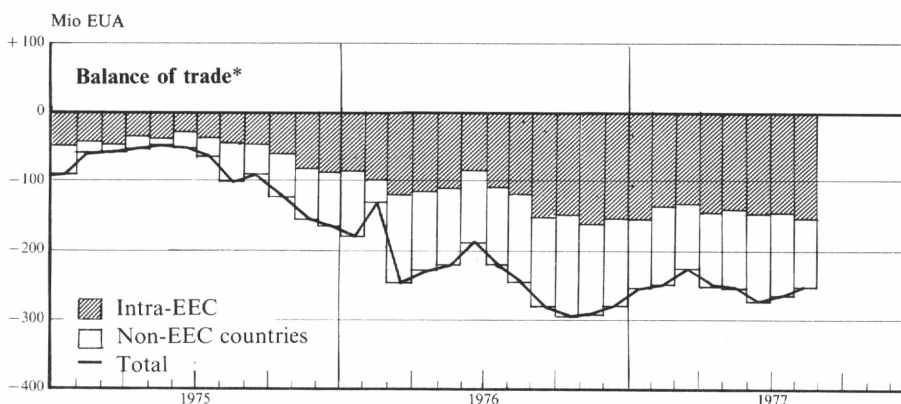
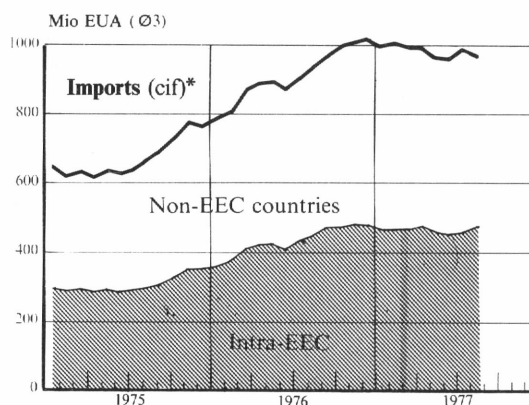
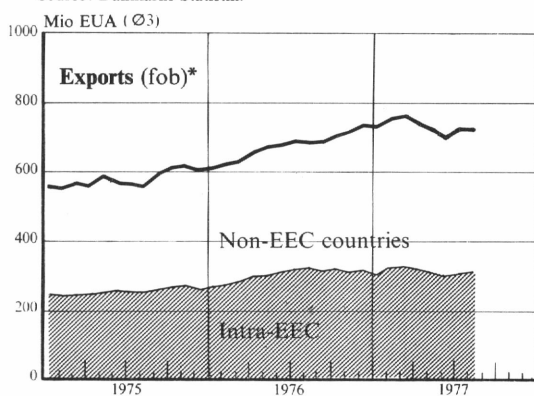
1 Hourly earnings in industry.

2 Including changes in indirect taxation, in particular the reduction in VAT from October 1975 to February 1976 and the increase in October 1977.

Source: Danmarks Statistik.



1 Money and near-money (M2).
Source: Danmarks Nationalbank.



* Seasonally adjusted figures.
Ø3: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

TABLE 2
Demand for and supply of goods and services

Denmark	1975 ²	1976 ²			1977 ³			1978 ³
	At current prices DKr '000 million	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	119.0	6.3	8.5	15.3	- 1/2	10 1/2	9 1/2	- 1
Public consumption	51.2	3.0	9.0	12.3	2 1/2	8	10 1/2	2
Gross fixed asset formation	40.4	16.3	6.7	24.1	- 3 1/2	8	4 1/2	1 1/2
— Enterprises	19.8	19.3	6.1	26.6	1	7 1/2	8 1/2	1 1/2
— Dwellings	9.4	25.4	7.5	34.8	- 15	9	- 7 1/2	- 5
— General Government	11.2	1.7	7.7	10.6	2 1/2	10	13	5 1/2
Domestic final uses (excluding change in stocks)	210.6	7.4	8.3	16.3	- 1/2	9 1/2	9	1/2
Domestic final uses (including change in stocks)	207.1	9.6	8.3	18.7	- 1	9 1/2	8	1/2
Exports ¹	69.8	2.6	8.7	11.5	4 1/2	8	13	5
Imports ¹	71.1	16.8	6.4	24.3	- 1/2	8 1/2	8	1 1/2
Gross domestic product at market prices	205.8	4.8	9.1	14.3	1	9	10	1 1/2
		Contribution to percentage change in gross domestic product						
Domestic final uses (excluding change in stocks)	210.6	7.6	—	16.7	- 1/2	—	9	1/2
Change in stocks	- 3.5	2.1	—	2.1	- 1/2	—	- 1/2	0
Balance of exports and imports ¹	- 2.3	- 4.9	—	- 4.5	2	—	1 1/2	1

¹ Goods and services

² Source: Danmarks Statistik

³ Estimates of Commission's Departments

Industrial **production** has remained depressed. Production in agriculture has progressed somewhat due in particular to a relatively favourable harvest. The employment situation has hardly changed and the unemployment rate has continued to grow: in October the seasonally adjusted figure for the numbers out of work amounted to 155 900 (or 6.1% of the labour force as against 5.9% in June). **Price** rises remain quite strong, notably as a result of dearer imports; in October the consumer price index¹ was 12.7% higher than a year earlier.

Despite a recent moderating trend, **imports** have stayed relatively high; in the period August-October they grew by 1% in value on the preceding three months. The **trade deficit**² stabilized around a monthly average of DKr 1 700 million. However, the current balance of payments deficit remained at DKr 2 600 million in the third quarter (as against 2 500 million in the second quarter). This deficit has been financed by foreign public borrowing and increasingly by private capital inflows. Long term **interest rates** have shown a slightly increasing trend. Total **foreign**

currency reserves have continued to rise; at the end of October they reached DKr 12 200, almost three times their amount a year earlier.

After the devaluation of 5% which took place on 28th August, the **Danish kroner** stayed at the top of the snake up to the end of October; since then it has moved progressively towards the middle.

3. Outlook

The general appearance of the economy is not likely to alter very much in the coming months. The growth of overall demand will remain weak. Without a recovery in world economic activity there is little reason to expect a more rapid progress of exports despite the effects of the recent devaluations of the kroner. As a result of the pressure exercised on real incomes by the increase in

¹ Which includes the impact of the increase in indirect taxation.

² Excluding ship and aircraft

TABLE 3
Main economic indicators

Denmark	Year	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec
Industrial production* (1970 = 100)	1975	106.0	102.7	94.7	103.8	100.1	101.5	107.4	101.0	104.4	109.3	105.6	111.1
	1976	108.5	112.4	117.7	112.8	114.1	119.5	111.4	117.0	118.4	110.8	116.9	117.4
	1977	116.0	114.3	122.1	105.7	108.2	118.9	107.3	119.9	117.2			
Unemployed* (1 000)	1975	102.2	107.9	115.6	118.8	114.5	111.2	116.5	121.4	123.8	122.2	121.2	125.3
	1976	127.4	122.9	117.2	114.8	112.2	115.1	118.9	115.3	117.2	119.1	120.2	121.2
	1977	134.3	142.2	141.3	146.1	143.7	143.4	145.2	149.6	148.7	151.0		
Construction*	1975	1 833	2 156	1 527	2 288	2 878	2 700	3 013	2 744	2 714	3 069	3 862	3 262
	1976	3 132	3 776	5 711	2 135	2 321	2 932	3 012	2 814	2 654	1 796	3 033	2 874
	1977	4 273	1 909	2 408	2 779	2 821							
Private consumers' expenditure* (1970 = 100)	1975	160.5	157.4	157.6	161.0	163.0	162.9	169.1	165.9	164.8	182.5	175.4	182.0
	1976	184.7	196.4	173.7	190.5	178.9	192.1	198.6	189.0	194.5	192.8	182.7	215.6
	1977	195.2	196.6	207.1	207.4	199.6	214.1	212.7	217.7				
Consumer prices (1970 = 100)	1975	151.7	152.1	153.2	153.9	155.8	156.7	157.5	158.0	159.4	155.4	157.9	158.0
	1976	158.9	160.0	167.0	167.5	169.2	168.8	168.9	170.1	174.3	176.2	178.2	178.7
	1977	178.7	178.8	181.4	183.3	186.0	186.9	188.2	189.9	191.9	198.6		
Visible imports* (million EUA)	1975	646.3	645.8	564.1	693.9	593.4	631.2	651.5	627.3	707.2	742.3	754.6	840.2
	1976	711.1	811.2	918.9	901.7	846.1	935.2	833.5	969.4	1 014.6	943.8	1 047.6	1 049.2
	1977	967.9	944.3	1 123.4	913.6	957.6	1 054.8	908.9	1 003.6	1 019.3			
Visible exports* (million EUA)	1975	562.8	574.0	540.4	615.2	549.0	605.7	560.4	547.5	569.0	675.8	582.9	605.7
	1976	614.2	598.4	650.4	646.1	683.6	697.5	661.6	719.3	694.0	663.5	759.6	737.2
	1977	728.7	736.0	824.9	745.7	675.6	743.3	679.7	750.0	743.1			
Balance of trade* (million EUA)	1975	- 83.5	- 71.8	- 23.7	- 78.7	- 44.4	- 25.5	- 91.1	- 79.8	- 138.2	- 66.5	- 171.7	- 234.5
	1976	- 96.9	- 212.8	- 268.5	- 255.6	- 162.5	- 237.7	- 171.9	- 250.1	- 320.6	- 280.3	- 288.0	- 312.0
	1977	- 239.2	- 208.3	- 298.5	- 167.9	- 282.0	- 311.5	- 229.2	- 253.6	- 276.2			
Foreign exchange reserves (DKr '000 million)	1975	5.2	5.0	5.2	5.0	4.8	4.9	4.6	4.8	5.0	5.2	5.2	5.4
	1976	5.4	5.3	7.4	7.1	6.4	6.2	4.3	5.0	3.8	4.8	4.9	5.4
	1977	6.4	7.1	8.2	11.0	11.8	12.5	11.2	10.9	12.1	13.2		
Money supply (DKr '000 million)	1975	83.9	84.5	86.5	88.8	90.7	95.0	94.8	95.4	97.6	102.7	106.3	108.5
	1976	106.3	109.2	109.6	112.2	114.0	116.2	114.7	113.2	114.6	115.8	117.7	120.9
	1977	117.2	116.7	119.4	122.5	124.3	126.8	123.6	122.8	126.2			

Not available

* Seasonally adjusted

Source: EUROSTAT (except as otherwise indicated)

- Industrial production: volume of sales in manufacturing industry (construction excl.)
- Unemployment: Number of registered unemployed
- Construction: number of dwellings authorized
- Private consumers' expenditure: Retail Sales Index, in value
- Consumer prices: Consumer price index, including VAT
- Imports: cif, exports: fob
- Balance of trade: difference between exports and imports.
- Foreign exchange reserves: Gross official reserves (excl. foreign liabilities of the National bank) position at end of month: Danmarks Nationalbank.
- Money supply: notes and coins in circulation and sight deposits at post giro accounts, commercial and major savings banks, position at end of month: Danmarks Nationalbank

indirect taxation, the volume of consumers' expenditure could experience a marked fall in the last quarter of 1977 before improving somewhat at the beginning of 1978. The development of investment should, in total, be a little more favourable due to some progress in the capital equipment sector. Construction should, on the other hand, remain depressed. In total the real growth rate of

gross domestic product in 1978 is unlikely to exceed 1½%.

Because of the recent measures, employment could improve, in particular in the public sector. However, the unemployment rate will undoubtedly rise for some time.

The tightening of taxation and the effect of the depreciation of the kroner will be reflected in a marked increase in consumer prices.

Recourse to external supply will remain limited. Since the terms of trade could improve somewhat, the trade deficit should fall. The current balance of payments position could make marked progress and the financing of the deficit and the external debt should not pose major problems in the short run.

In these circumstances, the problem which will still face the authorities will be to reconcile the primary objective of a progressive re-establishment of the external balance, which in the present economic situation implies a certain deflationary orientation, with an improvement in employment. This presupposes a fall in relative prices and costs in order to improve the competitive position of Danish production. To arrive at this objective, incomes' developments will have to be based on a strict consensus among the social partners that the limits laid down in the pay agreement of Spring 1977 should be observed equally in the private sector.

Major economic policy measures

July 1977

— The remaining tariffs as between Denmark and the other Member States were abolished with effect from 1st July.

— The credit ceiling was raised by 2 % to DKr 99 700 million from the end of June.

August

— The local authorities agreed to the government's 3-year employment programme. DKr 500 million will be earmarked in the budgets in each of the years 1978-80 for energy-saving measures, recycling and employment opportunities for school-leavers and other young people.

— The investment limits for the local authorities laid down by the central government were abolished in order to permit a higher level of investment activity at local level.

% The ceilings on the local authorities' borrowing powers were modified and fixed at 1.5 mrd DKr for 1978 so as not to permit a reduction in local taxation.

— With effect from 28th August Denmark and Norway devalued their currencies by 5 % against the other members of the European joint float, whereas Sweden devalued its currency by 10 % and retired from the joint float

— On 31st August the government and a parliamentary majority agreed on a package of measures intended to reduce the balance of payments deficit and to improve employment opportunities.

The restrictive effects of the measures adopted on 6th September amount to some 6½ mrd DKr annually during the period 1978-80. The principal components are:

— A rise in the rate of VAT from 15 % to 18 % with effect from 3rd October (estimated net effect 3.4 mrd DKr p.a.).

— An increase in taxation on tobacco and alcohol (estimated effect 1.0 mrd DKr p.a.).

— Higher taxes on petrol, gasoline and fuel oil (estimated effect 0.7 mrd DKr p.a.).

— Increase of registration tax on cars (estimated effect 0.5 mrd DKr p.a.).

— Rises in postal and rail charges (estimated effect 0.4 mrd DKr p.a.).

— Other excise taxes and fees (estimated effect 0.6 mrd DKr p.a.).

— Minor increase in personal income tax allowances for 1978.

The employment programme adopted consists of increases in public net expenditures and amount to some 10½ mrd DKr over the period 1977-1980:

— Measures to support specific activities in private enterprises.

— Programmes for retraining unemployed workers.

— Partial refund to employers of wage payments during prolonged sickness of employees.

— Extension of and increase in depreciation allowances.

— The carrying out of public investment projects.

— Measures to stimulate energy-saving investment and processes.

September

— Nationalbanken raised the quota applied for mortgage credits for 1977 by 2.5 mrd DKr to a total of 32.5 mrd DKr so that the 4 quarter allocation would amount to 7.5 mrd DKr.

— The ceiling on mortgage credits granted for owner-occupied houses was raised to 500 000 DKr and to 440 000 DKr in the Copenhagen metropolitan area and in the rest of the country respectively

November

— The credit ceiling was raised by 3 % to DKr 102 800 million from the end of October. The increase, of which the banks had already overdrawn 1 mrd DKr, will be granted as a priority for industrial investments.

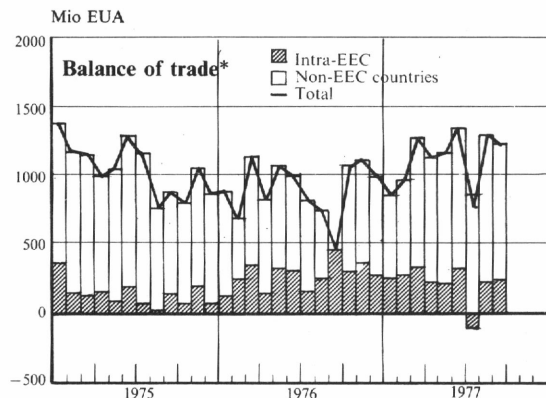
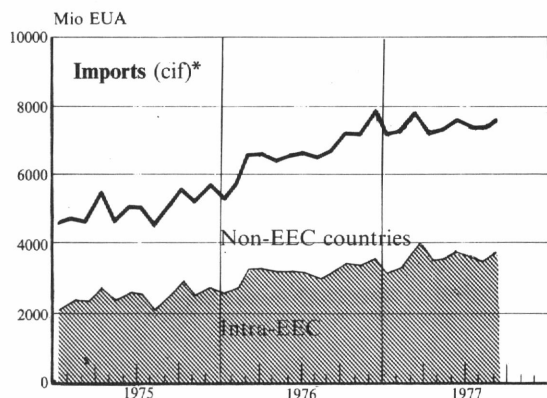
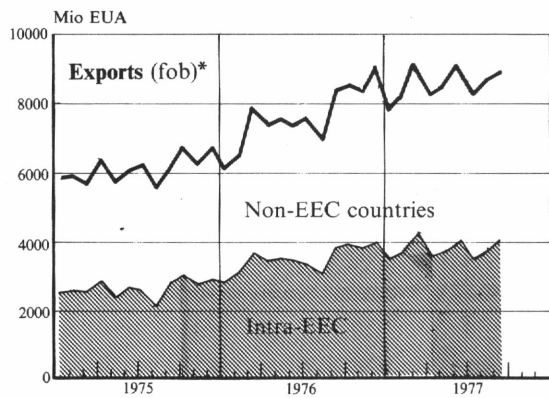
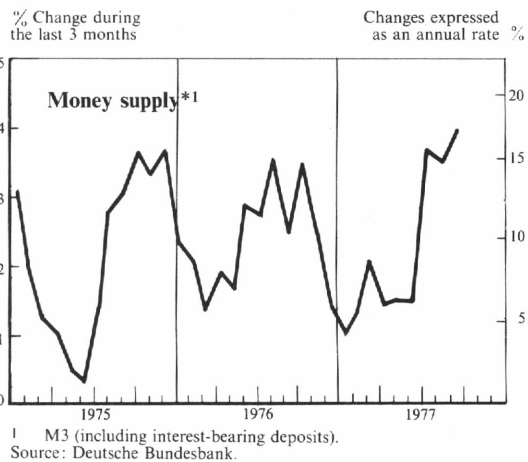
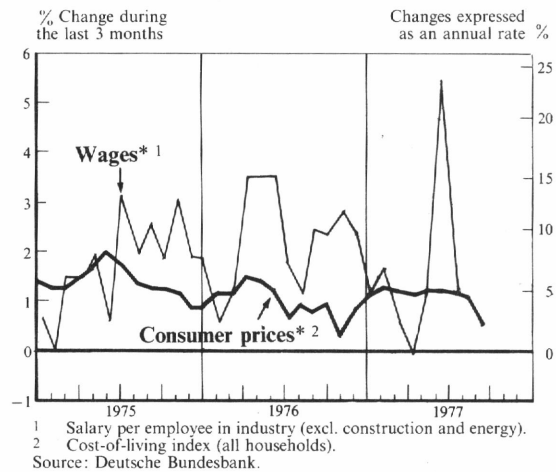
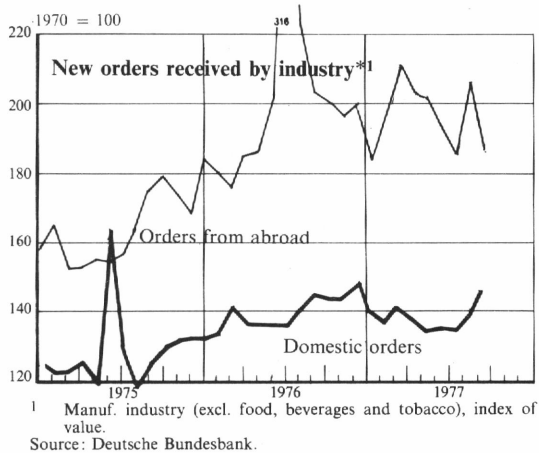
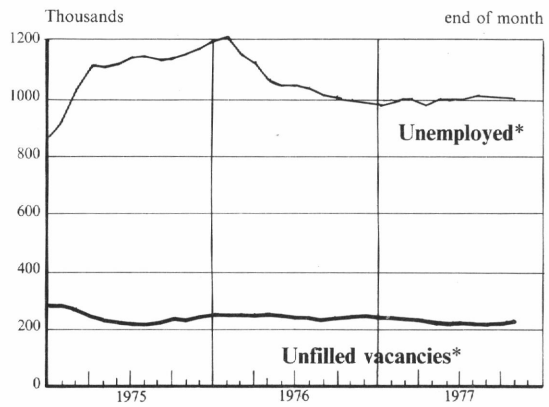
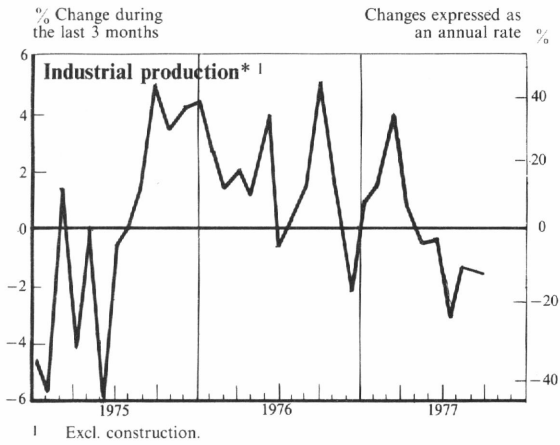
B. Federal Republic of Germany

In the Federal Republic of Germany, economic activity has been marking time since the spring. Private consumption has picked up recently and the generally subdued propensity to invest has strengthened a little, but the growth of export demand has slackened further. The situation on the labour market has failed to improve while the rate of price increases has continued to decelerate.

Because of the sluggish trend of demand, the Federal Government approved tax concessions in the autumn to boost private consumption and business investment. These measures have improved the growth prospects for next year but they will probably not be sufficient to bring down unemployment.

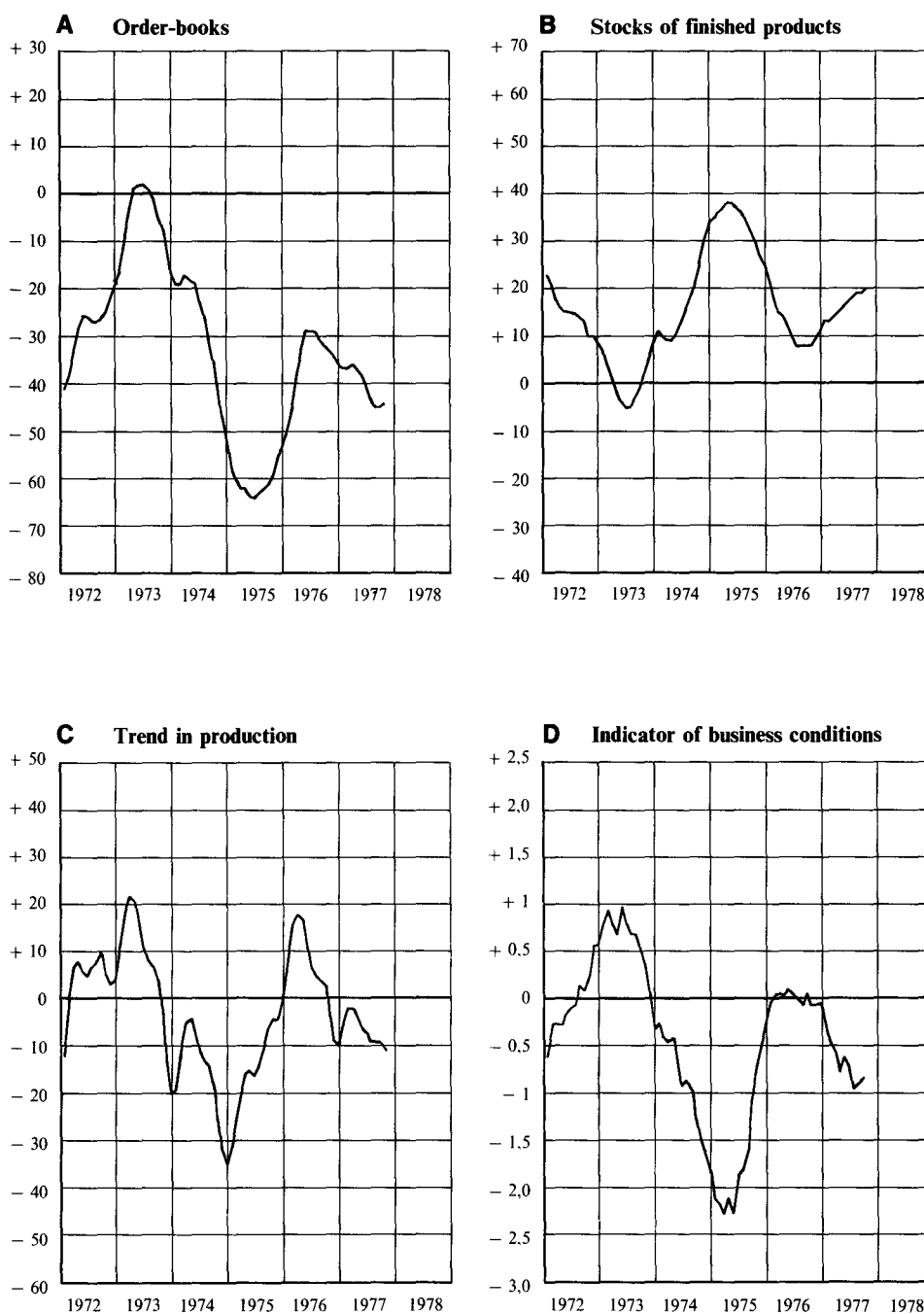
The growth prospects for 1978 also depend on how soon and how completely certain obstacles to the flow of private and public investment can be removed. Progress in combating unemployment can, however, be made only if the two sides of industry bear in mind the requirements of the economy as a whole and contribute to an improvement in the general economic climate through moderate wage settlements.

Federal Republic of Germany



*: Seasonally adjusted.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



NOTE:

These charts are based on answers to questions in the EEC business survey, carried out in the Federal Republic of Germany by the IFO-Institut.

Graphs A, B and C show a three months moving average of the difference between "above normal" and "below normal" answers to the following questions:

- a) Do you consider that your present total order-book is, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- b) Do you consider that your present stocks of finished products are, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- c) Do you think that over the next three or four months your firm's seasonally adjusted production trend will be:
 - (1) up
 - (2) unchanged or
 - (3) down?

Graph D presents an indicator of industrial business conditions, based on a principal component analysis of the answers to four questions in the monthly business survey. These are the above three questions together with a question on the recent trend on production.

1. Overall assessment and main policy issues

Since the spring, economic activity in the Federal Republic of Germany has been largely static. Domestic demand picked up after the summer holiday period, particularly where private consumer spending is concerned, but this probably did not offset the continued slackening in the growth of export demand. Although in recent months industrial production has shown a tendency to improve, this is not true of the situation in the labour market. At 3% at the most, real growth in 1977 will fall appreciably short of the rate aimed at early in the year.

So far the outlook for autonomous growth next year is not particularly favourable. However, budgetary policy will have a noticeably expansionary impact on the national economy. Following successive reductions in the budget deficits in 1976 and 1977, the public sector deficit will increase in 1978. Public expenditure will rise much more sharply than in 1977. Federal government spending is to go up by over 10% in 1978. Thanks to the multiannual investment programme adopted in the spring, public investment in particular will start to expand again vigorously. In addition, a tax-relief programme was

adopted in the autumn; of the total of almost DM 11 000 million involved, DM 9 300 million is designed to boost private consumption and DM 1 700 million to encourage business investment. In the period from 1978 to 1981, a total of over DM 4 000 million is to be made available to promote energy-saving investment in housing.

The environment created by monetary and credit policy will also permit a more favourable economic trend. By October, interest rates on the capital market had fallen to 6%, a level not reached since 1964.

However, there is little chance of growth in 1978 being sufficient to bring down unemployment significantly. The brunt will probably continue to be borne by workers who have inadequate skills or whose availability for work is restricted. Training and retraining efforts should therefore be stepped up to increase labour mobility. However, a major improvement in the labour market situation can be achieved only if employers and unions are guided by the requirements of the economy as a whole and endeavour in the years ahead to make the factor of production, "labour", more attractive again by means of moderate wage settlements.

TABLE 1
Key indicators

FR Germany	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁵	1977 ⁶
Gross domestic product; volume	% change	3.6	- 2.6	5.6	2.8
of which: Industry ¹		3.3	- 6.1	7.7	3.0
Gross domestic product in volume per person in employment	% change	3.7	0.8	6.6	3.1
Total employment (number of persons) ²	% change	- 0.1	- 3.4	- 0.9	- 0.3
— Independent entrepreneurs		- 2.5	- 3.1	- 3.5	- 3.3
— Wage and salary earners in company sector		- 0.6	- 4.5	:	0.2
— General Government		3.8	2.0	1.5	:
Unemployment	as % of labour force	1.1	4.1	4.1	4.0
Compensation of employees per wage and salary earner	% change	12.4	7.9	7.6	6.9
Price index of private consumption ³	% change	5.7	6.3	4.4	3.8
Current account balance	DM '000 million	9.7	10.6	9.2	5.0

¹ Excluding construction

² Domestic concept

³ National accounts concept, on annual basis

⁴ Geometric mean of the change from 1969 to 1974, unemployment and current account balance arithmetic mean over the five years

⁵ Source: Federal Statistical Office "National Accounts", Series 18 Revised results 1960-1976

⁶ Estimates of Commission's Departments

No data available

2. Recent developments

The expansion of **merchandise** exports continued to slacken distinctly. In value terms, exports in the third

quarter were only 2.5% higher than in the same period last year. The fall-off was especially apparent in trade with other Community countries, mainly owing to a

TABLE 2
Demand for and supply of goods and services

FR of Germany	1975 ²	1976 ²			1977 ³			1978 ³
	At current prices DM 000 million	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	574.6	3.6	4.4	8.2	2.9	3.8	6.8	3.2
Public consumption	216.0	2.4	3.3	5.8	2.0	4.0	6.1	3.5
Gross fixed asset formation	214.5	5.0	3.3	8.5	3.5	3.8	7.5	4.3
— Enterprises	115.0	7.3	3.5	11.0	4.8	4.0	9.0	3.2
— Dwellings	59.2	6.7	3.3	10.3	4.5	4.0	8.7	3.0
— General Government	40.3	— 3.8	2.6	— 1.2	— 2.6	3.0	0.4	9.8
Domestic final uses (excluding change in stocks)	1 005.1	3.7	3.9	7.8	2.8	3.8	6.8	3.5
Domestic final uses (including change in stocks)	1 001.7	5.4	3.9	9.5	2.8	3.8	6.7	3.5
Exports ¹	255.6	:	:	14.4	4.8	1.6	6.4	5.3
Imports ¹	227.3	:	:	17.2	4.8	2.8	7.7	5.6
Gross domestic product at market prices	1 030.0	5.6	3.3	9.0	2.8	3.5	6.4	3.5
		Contribution to percentage change in gross domestic product						
Domestic final uses (excluding change in stocks)	1 005.1	3.6	—	7.6	2.7	—	6.6	3.4
Change in stocks	— 3.4	1.6	—	1.6	— 0.0	—	— 0.0	0.1
Balance of exports and imports ¹	28.3	0.4	—	— 0.2	0.1	—	— 0.2	0.0

¹ Goods and services

² Source: Federal Statistical Office "National Accounts 1975" Series 18, revised results 1960-1976

³ Estimates of Commission's Departments

· No data available

decline in purchases by France and Italy. On the other hand, sales to non-member countries, notably the United States and the OPEC countries, were still fairly buoyant. In view of the continued tendency for the German mark to appreciate on foreign exchange markets — at the end of October, its value against the currencies of Germany's 22 major trading partners was 7.2% up on the same time last year — export prices in terms of DM were not raised further.

Following a marked decline in the first half of the year, business investment in plant and machinery has generally picked up somewhat in the last few months. Judging by the flow of new orders, building demand improved further. This was mainly due to the trend in residential construction (especially the building of owner-occupied houses) and the sharp expansion in public sector civil engineering projects, although demand for commercial and industrial building whilst showing a tendency to increase remained weak.

Private consumers' expenditure accelerated noticeably in the third quarter. Retail sales in this period were nearly

10% higher in value than a year earlier: adjusted for the rise in prices, this gave an increase of 5.5%. Sales of new cars again showed an above-average rise, being 13.9% higher in the third quarter than in the same period last year. The sharp increase in consumption was probably due mainly to the fresh funds released under premium-carrying savings contracts in the middle of the year. Public consumption, which in real terms scarcely increased in the first half of the year, has probably grown somewhat more rapidly again recently.

Overall, the growth in demand was not sufficient to prevent a further slackening of an already sluggish rate of production. In the third quarter, output in manufacturing industry was only 1.4% higher than in the corresponding period last year (in the first nine months of the year, it rose by 2.9% over the same period in 1976). With productive activity falling off, unemployment remained high. At the end of November, there were 1 004 000 people out of work, or 4.4% of all employees.

Given the sluggish economic trend, merchandise imports also lost a great deal of momentum; in the third quarter,

the increase on the same period of last year fell to 3.8% in value terms.

The **price** climate again improved appreciably. Industrial producer prices have been static for several months and, in October, were only 1.5% higher than a year earlier. In October, the cost-of-living index was up 3.8% on the same month last year.

In the period January-October, the **trade balance** showed a surplus of DM 28.2 billion, an increase of almost DM 3 billion on a year earlier. As the deficit on the services balance increased appreciably, the current account for the same period showed a surplus of DM 3.9 billion, somewhat below the figure recorded for the first ten months of 1976.

Following an acceleration in the summer months, the growth in the **central bank money** stock has recently been slackening a little. Taking the average for the first nine months of the year, this measure of the money supply was 8.8% above the level of a year earlier, overshooting the target for 1977 by about one percentage point.

3. Outlook

Thanks to the stimuli provided by the economic policy measures, the underlying growth of economic activity should be somewhat stronger next year. However, taking the average for 1978, the increase in real gross domestic product will not exceed 3-4% owing to the relatively low base at the end of 1977. Even a growth rate at the upper end of this range will produce no significant improvement on the labour market.

With the outlook for world trade not particularly buoyant, exports will probably grow only moderately. Furthermore, the low level of business profits, which will again fall this year following a marked improvement in 1976, may well have an especially detrimental effect on the investment climate. The inadequate increase in demand has indeed curbed production growth. With employment levels being adjusted with a time lag and not to the full extent, productivity gains have therefore become much smaller. As the rise in wages showed little if any slowdown, production costs climbed more rapidly again. The trend of demand, both domestic and export, did not allow this to be offset by corresponding price rises, so that business profits have again worsened perceptibly.

The aids and reliefs approved in the last few months (e.g. more generous depreciation allowances, cuts in company tax and wealth tax, subsidies for research and energy-saving investment) will probably work through only gradually. On the other hand, after declining for several years, public authority investment will grow appreciably as a result of the multiannual investment programme. The trend of private and public investment will also depend largely on the extent to which administrative and other obstacles in this area can be removed.

Private consumption should be boosted considerably by the direct tax reliefs. However, these effects will be partly offset by the increase in VAT from 1st January 1978.

With demand expected to be sluggish, prices are likely, despite the increase in VAT, to rise somewhat more slowly than in 1977. The external surplus will probably shrink further.

July 1977

— On 14 July the Central Bank Council of the Bundesbank decided to lower the rate for advances on securities by ½% to 4%, with effect from 15 July. At the same time the interest rate for open market operations on bills of exchange was reduced from 4% to 3¾%.

August:

— On 25 August the Central Bank Council of the Bundesbank decided to lower the minimum reserve ratios by 10% with effect from 1 September and to raise rediscount quotas immediately by DM 2 000 million. These measures released DM 6 500 million in liquidity.

September:

— On 14 September the Federal Government approved the 1978 draft budget and the finance plan to 1981. In 1978 expenditure is to rise by over DM 17 000 million — over 10% — to approximately DM 189 000 million.

— On 23 September the Bundesbank decided, with immediate effect, to resume granting advances against the pledge of bills of exchange. Bills were accepted as collateral for 10 days at 3.5%.

October:

— The Bundestag and the Bundesrat agreed to the Mediation Committee's compromise solution concerning the Federal Government's programme to promote growth and employment. The following reliefs totalling DM 10 800 million can now enter into force:

— The Christmas tax-free allowance for wages and income tax purposes is to be increased from DM 100 to DM 400 from 1977. This measure will cost DM 2 100 million in lost tax.

— With effect from 1 January 1978 the wages and income tax basic personal allowance is to be increased by DM 300 for single persons and by DM 600 for married couples. This measure will cost a total of DM 2 100 million

— All taxpayers are to have the amount chargeable to wages and income tax reduced by DM 510 (single persons) or DM 1 020 (married couples). This measure will cost DM 5 100 million in lost tax.

— Diminishing balance depreciation for capital expenditure was raised with retroactive effect from 1 September 1977 from twice to two and a half times the straight-line value. At the same time diminishing balance depreciation was reintroduced for commercial and industrial buildings and for the privately financed construction of housing for rent. These measures will cost DM 1 500 million per annum in lost tax.

— Investment grants for research and development projects carried out particularly by small and medium-sized firms are to be raised from 7.5% to 15% (total cost: DM 100 million).

— To encourage energy-saving investment in residential construction, interest subsidies totalling DM 4 350 million (divided equally between the Federal Government and the Länder) are to be made available in the period 1978 to 1981.

— The programme to encourage publicly assisted housing will be continued from 1978 the Federal Government will grant further financial assistance amounting to DM 510 million under the social programme and DM 1 030 million under the regional programme.

November:

— On 3 November the Bundesbank decided to stop granting ten-day advances to credit institutions against the pledge of bills of exchange.

TABLE 3
Main economic indicators

FR of Germany	Year	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec
Industrial production* (1970 = 100)	1974	113.1	115.1	114.9	113.9	112.7	119.1	112.1	110.8	111.9	109.9	111.3	106.5
	1975	104.8	104.9	108.2	100.6	104.9	101.5	100.1	104.9	103.1	105.0	108.6	107.4
	1976	109.9	111.5	108.8	112.2	112.7	113.2	111.5	113.2	114.9	117.3	115.2	112.5
	1977	118.4	116.7	116.7	119.2	116.0	116.2	115.3	114.3	114.2			
New orders received* (1970 = 100)	1974	138	140	143	142	144	144	139	145	137	140	134	127
	1975	134	131	129	132	128	160	135	128	137	140	141	142
	1976	145	144	148	147	148	151	175	158	158	157	155	162
	1977	149	149	157	154	152	150	146	154	154			
Of which New domestic orders in capital goods industry*	1974	114	122	119	113	121	114	111	112	110	113	111	112
	1975	124	122	121	124	117	214	137	112	124	121	127	130
	1976	128	129	133	133	128	128	134	142	145	147	147	157
	1977	144	141	144	139	137	138	140	142				
Unemployed* (1000)	1974	358.6	378.5	439.5	516.4	515.1	542.7	585.0	632.2	671.2	745.9	832.4	816.2
	1975	859.1	920.9	1 028.3	1 100.2	1 094.3	1 109.7	1 139.5	1 143.0	1 131.7	1 147.6	1 154.9	1 179.7
	1976	1 193.7	1 202.5	1 142.2	1 107.6	1 042.0	1 031.6	1 036.5	1 032.0	1 007.5	1 000.2	984.7	980.7
	1977	1 002.4	982.2	967.6	995.7	997.6	1 010.2	1 034.2	1 032.8	1 012.5	1 012.7		
Unfilled vacancies* (1000)	1974	425.4	393.0	364.3	349.4	323.2	298.4	276.0	262.8	241.9	245.5	239.2	248.5
	1975	258.9	258.6	250.6	238.1	225.8	215.8	213.0	213.9	209.1	213.1	213.8	221.0
	1976	226.6	223.5	235.7	237.1	245.0	242.7	241.0	232.4	216.5	232.9	244.0	254.2
	1977	247.9	247.0	244.0	235.8	220.9	227.5	225.5	225.8	226.2	233.2		
Construction permits for residential construction* (1000)	1974	42.6	37.2	36.6	34.1	37.0	28.8	30.9	29.5	29.8	32.1	27.7	34.8
	1975	30.8	31.9	29.1	29.2	26.3	29.3	26.9	27.1	30.5	31.2	35.6	34.1
	1976	37.9	39.4	35.4	35.5	34.1	33.8	31.1	28.5	29.0	26.5	28.9	30.9
	1977	28.3	28.5	28.9	28.6	28.9	27.4	28.3	29.1				
Private consumers* expenditure turnover of retail trade* (1970 = 100)	1974	134	133	134	136	137	134	139	139	138	142	139	139
	1975	143	146	146	147	145	150	149	150	152	154	156	153
	1976	156	159	157	156	158	158	157	160	162	157	164	164
	1977	166	168	171	160	171	170	171	175				
Consumer prices* (1970 = 100)	1974	123.5	124.4	124.8	125.4	126.2	126.7	127.4	128.1	128.6	129.4	130.2	130.6
	1975	131.1	131.6	132.2	133.1	133.9	134.8	135.3	135.7	136.4	137.0	137.3	137.7
	1976	138.1	138.7	139.3	140.1	140.5	140.9	140.8	141.9	142.0	142.2	142.4	143.1
	1977	143.7	144.2	144.8	145.3	145.9	146.5	146.9	147.3				
Visible imports* (million EUA)	1974	4 532	4 064	4 594	4 767	5 148	4 663	5 132	5 117	4 931	5 202	5 114	5 047
	1975	4 769	4 948	4 535	5 385	4 537	5 016	4 969	4 742	5 243	5 396	5 113	5 676
	1976	5 379	5 805	6 245	6 275	6 141	6 423	6 540	6 782	6 860	6 814	7 147	7 868
	1977	7 019	7 147	7 874	7 012	7 186	7 667	7 424	7 370	7 601			
Visible exports* (million EUA)	1974	5 827	5 666	6 042	6 312	6 778	5 780	6 567	6 263	6 215	6 590	6 565	6 678
	1975	6 167	6 114	5 660	6 361	5 578	6 277	6 121	5 476	6 092	6 168	6 154	6 526
	1976	6 250	6 488	7 369	7 079	7 179	7 412	7 344	7 497	8 345	7 869	8 226	8 853
	1977	7 879	8 104	9 139	8 127	8 363	9 015	8 175	8 671	8 826			
Balance of trade* (million EUA)	1974	+1 295	+1 602	+1 448	+1 545	+1 630	+1 117	+1 435	+1 146	+1 284	+1 388	+1 451	+1 631
	1975	+1 398	+1 166	+1 125	+ 976	+1 041	+1 261	+1 152	+ 734	+ 849	+ 772	+1 041	+ 850
	1976	+ 871	+ 683	+1 124	+ 804	+1 038	+ 989	+ 804	+ 715	+1 485	+1 055	+1 079	+ 985
	1977	+ 860	+ 957	+1 265	+1 115	+1 177	+1 348	+ 751	+1 301	+1 225			
Official gold and foreign exchange reserves (DM '000 million)	1974	89.6	89.2	91.5	93.8	95.6	94.9	94.1	92.5	90.8	89.3	90.6	83.4
	1975	84.8	86.8	87.8	85.8	85.0	83.8	82.4	81.8	81.3	82.4	81.6	86.4
	1976	86.4	88.4	96.4	95.5	93.6	92.8	91.9	95.1	96.8	98.8	95.9	88.5
	1977	87.8	88.0	88.2	87.8	88.5	87.1	88.9	88.7	87.7	90.1		
Money supply* (DM '000 million)	1974	406.2	409.8	412.3	417.3	418.0	419.8	422.6	421.9	424.2	425.3	431.0	438.2
	1975	438.4	440.4	443.3	442.6	442.4	444.8	448.6	455.0	458.7	465.1	470.0	475.9
	1976	475.9	480.0	481.9	485.0	488.0	495.8	498.1	505.4	508.1	515.6	518.1	515.3
	1977	520.6	524.7	526.2	527.7	532.6	534.1	547.4	551.0	555.7			

Not available

* Seasonally adjusted

Source: EUROSTAT (except as otherwise indicated)

- Industrial production, excluding construction
- New orders received - manufacturing industry (excluding food, beverages and tobacco) - value index - Source: Deutsche Bundesbank
- Unfilled vacancies - position at end of month
- Construction - number of dwellings authorized
- Private consumer's expenditure - total retail trade, value index - Source: Deutsche Bundesbank
- Consumer prices - cost-of-living index (all households) - Source: Deutsche Bundesbank
- Imports cif, exports tob, values
- Balance of trade - difference between the seasonally adjusted values of imports and exports
- Official gold and foreign exchange reserves - including IMF Special Drawing Rights and reserve position at the IMF - Figures are given gross, liabilities to abroad not having been deducted - Position at end of month - Source: Deutsche Bundesbank
- Money supply - M3 (including interest-bearing deposits), position at end of month - Source: Deutsche Bundesbank

C. France

Since the second quarter there has been a pause in the growth of output in France, and the available indices point only a very gradual recovery. There has been a marked improvement in the external balance, but progress made in reducing the rate of inflation has been small, largely because of rises in food prices. Although the specific measures taken during the year have already led to a reduction in the number of job seekers, unemployment remains disturbingly high.

The strength of the autonomous factors underlying the growth of demand and output over the coming months is questionable, although consumer demand will gain from a somewhat faster growth of real disposable income, and exports from firmer markets abroad. The rate of inflation should begin to fall, and the improvement in the external balance should be consolidated. However, in the present circumstances achieving a lasting reduction in unemployment will be difficult and will require a sustained effort.

1. Overall Assessment and Main Policy Issues

Although it appeared from the business surveys and other leading indicators that industrial production was beginning to turn up after the summer holiday period while consumer demand was stronger in the third quarter, only as regards investment goods has there been confirmation of an improvement in the situation. While spectacular progress in restoring external equilibrium has been achieved, the rate of price inflation has diminished very slowly.

The stance of monetary and fiscal policy has, since the autumn of last year, been moderately restrictive and essentially dedicated to holding down inflation and

improving the balance of payments position, while specific measures have been taken to deal with unemployment, notably in August. A money supply (M2) growth target of 12½% was set for 1977. Because of the credit requirements of the public authorities in the third quarter, the increase in the money supply is a little above what would correspond to this target, even though private demand for credit has been weak. For 1978 a norm of 12% for growth in M2 has been established in line with an official forecast of 12.6% growth in nominal GDP. As regards fiscal policy a general government borrowing requirement of FF 15 000 million is expected this year, or about 0.8% of GDP, the same percentage as for 1976. This deficit — modest by international standards — has

TABLE I
Key Indicators

France	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁵	1977 ⁶
Gross domestic products, volume	% change	4.8	0.1	5.2	2.7
of which: Industry ¹		5.7	- 9.3	7.7	4.0
Gross domestic product in volume per person in employment	% change	5.6	1.2	5.1	2.9
Total employment (number of persons) ²		0.8	- 1.1	0.1	- 0.2
— Independent entrepreneurs	% change	- 2.7	- 2.3	- 2.3	- 2.0
— Wage and salary earners in company sector		1.7	- 1.4	0.6	0.2
— General Government		1.9	1.5	0.8	1.5
Unemployment	as % of labour force	2.7	4.2	4.4	5.1
Compensation of employees per wage and salary earner	% change	12.8	17.7	14.7	11.8
Price index of private consumption ³	% change	8.3	11.6	9.9	9.1
Current account balance ³	FF '000 million	- 5.4	- 0.3	- 27.5	- 16.1

¹ Excluding construction

² Domestic concept.

³ National accounts concept, on annual basis.

⁴ Geometric mean of the change from 1970 to 1974, unemployment and current account balance arithmetic mean over the five years

⁵ Source: Rapport sur les comptes de la nation de l'année 1976

⁶ Estimate of Commission's Departments

been achieved by a series of increases in public investment and social security transfers in March, July and August. While the proposed central government budget for 1978 shows a fall in the deficit from about FF 16 000 to 9 000 million, this is compensated by a rise in the deficit of local authorities and the social security funds, so that a general government borrowing requirement of about FF 18 000 million or 0.9% of the GDP is envisaged.

Following the growth of consumer demand during the summer, and despite the growth in real disposable household income, there seems little prospect of any further increases in the volume of this aggregate over the coming months. While exports have continued to show considerable strength, whether the recent performance can be extrapolated is doubtful. As regards investment, estimates on the level of orders are more favourable to a recovery in the first half of 1978, though it will not be possible to consolidate this until the present uncertainties have been resolved.

The underlying trend in unemployment has been difficult to monitor, since the fall observed over the last few

months appears to be linked to the specific measures implemented since early summer. Consequently, in spite of some pick-up due to the gradual phasing-out of destocking, it is unlikely that the recovery in production will be sufficiently strong of itself to lead to a significant drop in the number of job applicants. The extra output likely to be generated by spontaneous growth over the next half-year can be largely covered by exploiting productivity reserves or further reductions in part-time working. The outlook for the balance of payments and the franc is healthy. Also the rate of inflation which has been adversely affected by food price increases in recent months should now show clear signs of abating.

2. Recent developments

The second half of 1977 has been characterised by a period of sluggishness in industrial output, by a strong but stable level of demand by households, by a marked improvement in the balance of trade and by a disappointing rate of price inflation.

TABLE 2
Demand for supply of goods and services

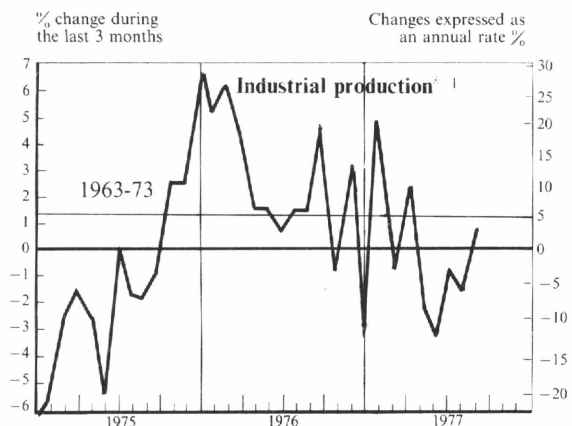
France	1975 ²	1976 ²			1977 ³			1978 ⁴
	At current prices FF '000 million	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	894.4	4.9	9.9	15.3	2.6	9.1	11.9	3.7
Public consumption	209.9	4.8	11.0	16.3	3.7	9.7	13.8	3.4
Gross fixed asset formation	335.4	4.5	9.1	14.0	0.5	10.1	10.7	2.0
— Enterprises	177.8	5.6	6.9	12.9	0.9	11.2	12.2	2.6
— Dwellings	113.8	— 0.1	13.1	13.0	— 1.0	9.0	8.0	0
— General Government	52.0	5.4	10.7	16.7	3.5	9.0	12.9	4.5
Domestic final uses (excluding change in stocks)	1 439.7	4.8	9.8	15.1	2.3	11.9	14.5	3.4
Domestic final uses (including change in stocks)	1 426.5	7.0	9.8	17.5	1.7	9.3	11.2	3.5
Exports ¹	269.8	9.4	8.6	18.8	6.6	10.7	18.0	7.1
Imports ¹	259.2	19.5	9.5	30.9	1.4	13.1	14.7	6.6
Gross domestic product at market prices	1 437.1	5.2	9.6	15.3	2.7	9.0	12.0	3.6
		Contribution to percentage change in gross domestic product						
Domestic final uses (excluding change in stocks)	1 439.7	4.9	—	15.2	2.3	—	12.1	3.4
Change in stocks	— 13.8	2.1	—	2.2	— 0.6	—	— 0.6	0.2
Balance of exports and imports ¹	10.6	— 1.8	—	— 2.0	1.0	—	0.6	0.1

¹ Goods and services

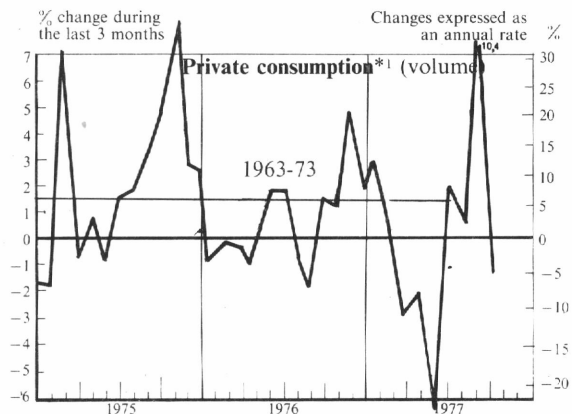
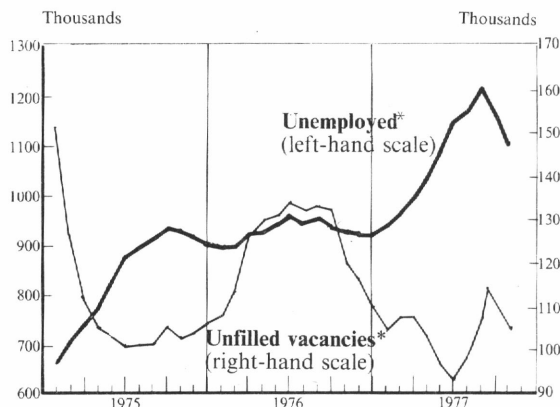
² Source: Rapport sur les Comptes de la Nation de l'année 1976

³ Estimates of Commission's Departments

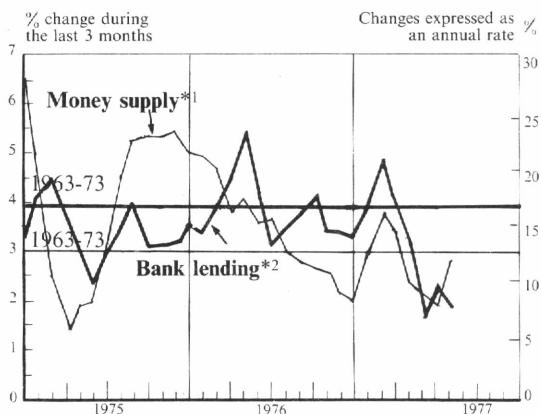
⁴ Forecast of Commission's Departments.



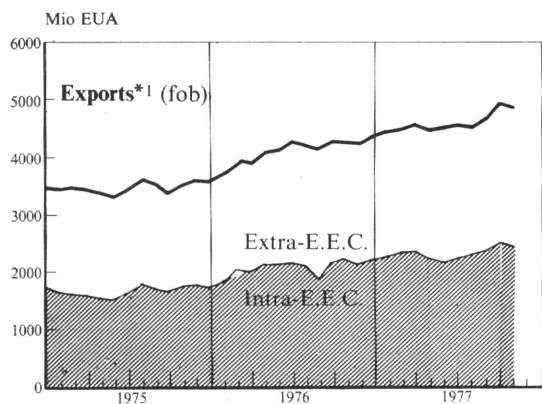
1 Except construction.



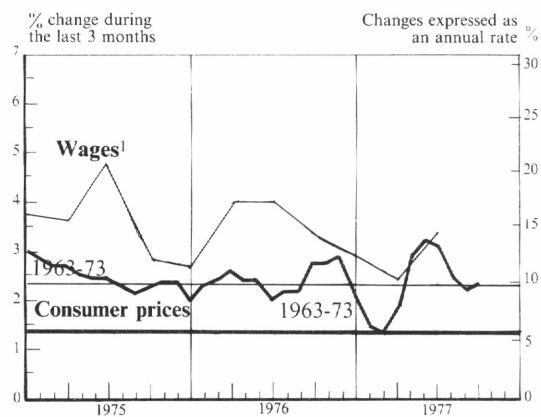
1 Consumption of manufactured goods.



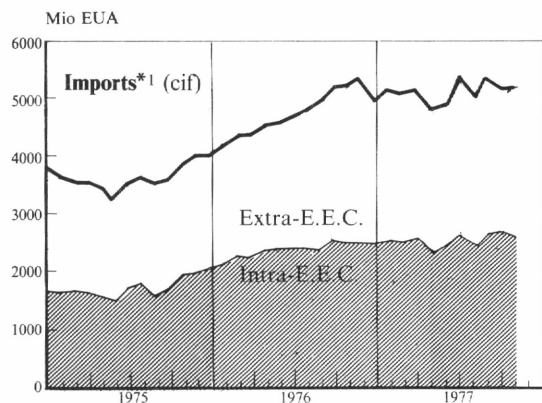
1 Money and near-money.
2 Total bank lending.
Source: Banque de France.



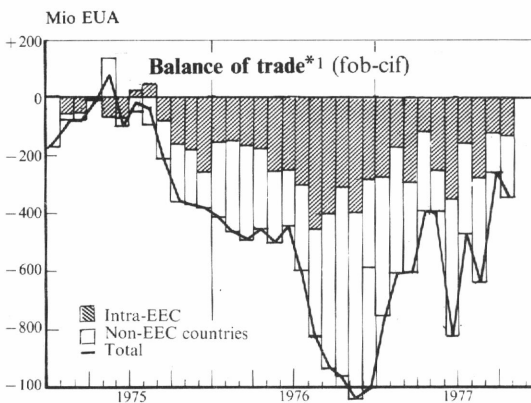
1 Excluding military supplies.



1 Quarterly index of hourly wage rates, all sectors, nationwide.



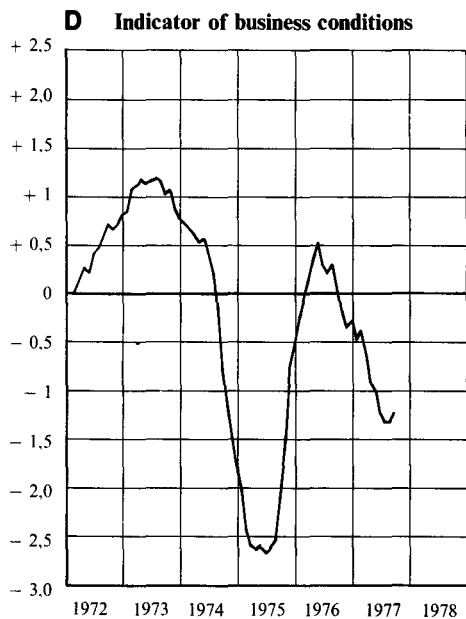
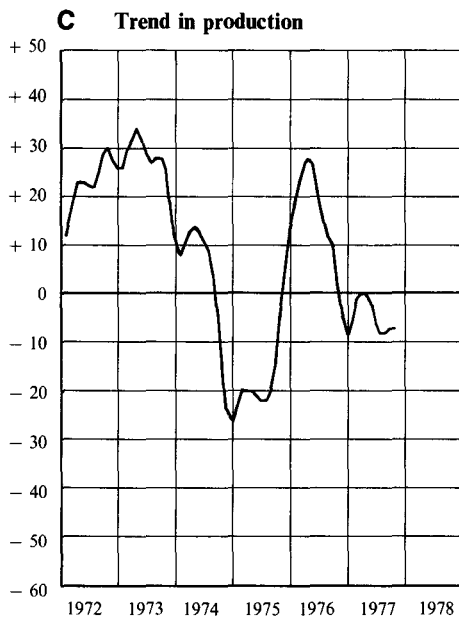
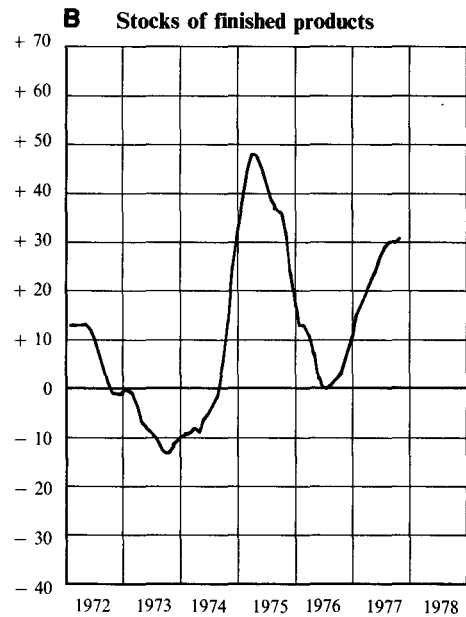
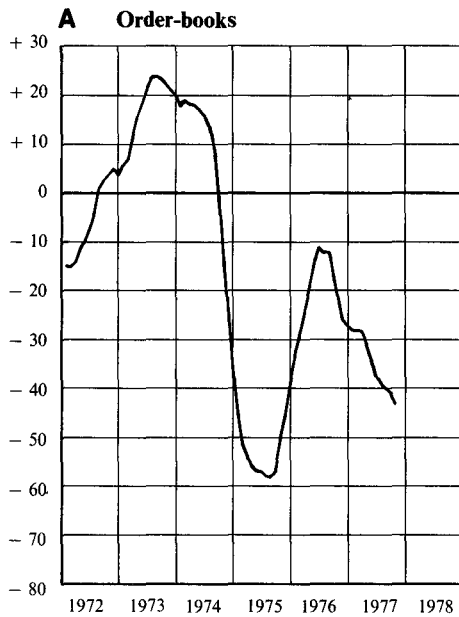
1 Excluding military supplies.



1 Excluding military supplies.

*: Seasonally adjusted.
Source: INSEE, except where otherwise stated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



NOTE:

These charts are based on answers to questions in the EEC business survey, carried out in France by INSEE.

Graphs A, B and C show a three months moving average of the difference between "above normal" and "below normal" answers to the following questions:

- a) Do you consider that your present total order-book is, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- b) Do you consider that your present stocks of finished products are, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- c) Do you think that over the next three or four months your firm's seasonally adjusted production trend will be:
 - (1) up
 - (2) unchanged or
 - (3) down?

Graph D presents an indicator of industrial business conditions, based on a principal component analysis of the answers to four questions in the monthly business survey. These are the above three questions together with a question on the recent trend on production.

Among the components of demand, **consumer expenditure** in the third quarter was some 2% in volume above that recorded in the first half-year. It would seem that this figure closely parallels the rise in real household disposable income, while the savings rate has continued to remain low by historical levels. While the real wage will have risen little in the last half-year, social security payments (which will account for 26% of gross household income in 1977 compared with some 41% for earnings) in real terms will have risen by between 12 and 13%, during the same period mainly due to the upgrading of rates on July 1. The other buoyant component was **exports**. The seasonally-adjusted volume of exports for the third quarter was 3.4% above that of the average for the first half of the year. This growth, which was evenly distributed between the Community countries and the rest of the world, represents a considerable gain in France's shares of export markets, since the total imports in volume of France's major partner countries have been stagnant or declining. As was indicated by the May survey made among exporting firms, exports continue to remain competitive, particularly those of finished goods, and export profit margins are becoming increasingly attractive.

Meanwhile **investment** and, in particular, stock building by firms have been weak. Overall there has probably been some modest destocking of finished goods recently, but a majority of businessmen still consider their stock levels too high. The demand for **loans** by the private sector has generally been weak, and the norms on bank lending have been easily respected, while long-term interest rates have remained high.

With internal demand rising only moderately since the second quarter **imports** in volume terms have remained essentially stable. Together with some easing in the prices of raw materials and overall stable import prices, as well as the export performance described above, this has meant a rapid improvement in the **balance of trade**. Indeed surpluses (fob-fob, seasonally adjusted) were recorded in September and October for the first time in two years. Also aided by vigorous growth in the surplus on services, the deficit on current account has again fallen in the third quarter (FF 2 050 as against 3 200 million in the second quarter).

The seasonally-adjusted index of industrial **production**, excluding construction, was actually marginally lower in the third quarter than in the second quarter. In these circumstances **unemployment** rose to nearly $\frac{1}{4}$ million in August. In September and October the numbers of seasonally-adjusted unemployed fell, partly due to the measures encouraging the employment of young people and partly due to an increased effort by enterprises to fill existing vacancies.

Price inflation has continued to be worryingly high, but it has been largely fuelled by the rises in food prices. The overall index rose at an annual rate of $9\frac{1}{2}\%$ in the third quarter, while food prices rose at an annual rate of 14%, service prices at 9% and manufactured goods prices at $7\frac{1}{2}\%$ (over the first nine months the price index for

manufactured goods has risen at an annual rate of 7.2% as compared to the norm of 6.5% established in September of last year). The factors which have contributed to a reduction in the rate of inflation include the contemporaneous and lagged effects of the marked deceleration in the rate of growth of wage rates, the downward trend in the price of raw materials and the stability of the franc.

3. Outlook

Over the next half-year a clear reduction in the rate of inflation and a consolidation of the progress achieved with respect to the external balance can be expected but no substantial acceleration in the rate of growth of output or employment is probable given the present prospects for world trade and the policy of equilibrating the external balance.

There is likely to be a substantial reduction in the rate of growth of prices in the coming months, as they reflect the reduced rate of increase of earnings, the falls in the prices of imported raw materials, and the new measures to control certain food prices and to eliminate distortions in market structures. The reduced rate of inflation associated with a prolongation of the current rate of growth of wage rates together with the increases in social security transfers due on January 1, should mean a faster rate of growth of real disposable income in the first quarter of 1978. This will permit some increase in the level of consumer demand.

The volume of exports will be helped by the return of agricultural exports to more normal levels and sales of industrial goods will benefit from firmer demand but further large gains in market share are improbable. Private investment will on the whole grow slowly due to various factors. Public expenditure will continue to provide a contribution to the growth of GDP.

Overall there should be some small improvement in the rate of growth of output in the next half-year. The outlook for unemployment is however worrying on the whole, though the specific measures to provide jobs taken by the authorities in 1977 will have a further impact.

The modest rate of growth of demand, particularly of stock-building, and output will mean that imports will grow slowly, and thanks to the increase in food exports, over the next six months, the balance of trade in goods will stay in rough equilibrium. The current account deficit will continue to fall, aided by the spectacular growth in the service surplus.

Major economic policy measures

July 1977

- The minimum hourly wage (SMIC) was raised from FF 9 34 to FF 9 58, an increase of 2.6% since 1 June
- The Government decided to release FF 1 250 million, or half the Economic Action Fund, to finance new public works.
- Entry into force of the law introducing various measures to encourage employment of young people. The main provisions of this law focus on two areas:

TABLE 3

Main economic indicators

France	Year	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct.	Nov.	Dec
Industrial production* (1970 = 100)	1975	115	114	112	112	108	112	110	110	111	114	113	118
	1976	120	120	122	122	122	123	124	124	129	123	128	125
	1977	129	127	129	126	123	128	124	124	126			
Production outlook	1975	- 22	- 10	- 16	- 13	- 9	- 14	- 16		- 8	4	15	18
	1976	22	27	31		31	26	14		12	5	5	11
	1977	- 3	- 1	+ 7	+ 2	- 5	- 6	- 9					
Unemployment* (1 000)	1975	676.2	707.9	739.9	784.4	826.8	877.0	900.0	910.7	933.1	928.1	913.3	905.6
	1976	899.6	901.4	920.7	929.4	953.1	966.7	950.1	961.7	941.3	935.4	931.4	929.9
	1977	944.7	972.4	1 002.5	1 039.4	1 096.7	1 150.6	1 180.1	1 215.9	1 157.7	1 100.2		
Vacancies* (1 000)	1975	150.7	125.4	112.7	106.0	102.8	100.1	100.3	100.6	105.9	102.7	104.8	106.4
	1976	107.5	113.9	124.4	129.6	130.3	134.1	131.1	132.3	131.7	118.6	114.4	110.2
	1977	104.8	108.5	108.7	103.8	96.6	93.1	98.1	108.4	113.0	106.8		
Private consumption manufactured goods consumption* (1963 FF'000 million)	1975	13.46	13.75	13.29	13.56	13.63	13.50	13.80	14.06	14.29	15.00	14.46	14.66
	1976	14.88	14.43	14.61	14.72	14.67	14.86	14.60	14.39	15.11	14.79	15.09	15.40
	1977	15.26	15.19	14.96	14.94	14.21	15.26	15.03	15.69	15.06			
Consumer prices (1970 = 100)	1975	145.9	147.0	148.2	149.5	150.6	151.7	152.8	153.8	155.1	156.3	157.3	158.2
	1976	159.9	161.0	162.4	163.8	164.9	165.6	167.2	168.4	170.2	171.8	173.2	173.8
	1977	174.3	175.5	177.1	179.4	181.1	182.5	184.1	185.1	186.7			
Wages and salaries (1962 = 100)	1975	344.6			357.4			374.7			385.3		
	1976	395.7			411.6			428.2			442.7		
	1977	455.6			466.0			481.3					
Visible imports* (million FF)	1975	20 175	19 686	19 511	18 523	16 917	18 563	19 392	18 777	19 222	20 421	20 793	20 804
	1976	21 739	22 698	22 931	23 696	24 146	24 530	25 412	27 011	28 451	28 966	29 488	27 590
	1977	28 982	28 351	29 072	26 977	27 296	29 929	27 948	30 131	29 148	29 189		
Visible exports* (million FF)	1975	19 188	19 342	19 163	18 512	17 380	18 146	19 324	18 642	18 102	18 550	18 883	18 825
	1976	19 611	20 378	20 425	21 404	21 586	22 285	22 268	22 529	23 318	23 580	23 572	24 329
	1977	24 792	24 997	25 717	24 812	25 126	25 379	25 324	26 611	27 698	27 218		
Balance of trade* (million EUA)	1975	- 177	- 62	- 63	- 2	+ 88	- 79	- 13	- 25	- 214	- 359	- 368	- 380
	1976	- 408	- 448	- 480	- 440	- 491	- 431	- 591	- 820	- 936	- 975	- 1 067	- 583
	1977	- 752	- 603	- 601	- 387	- 388	- 816	- 471	- 638	- 259	- 352		
Intra EEC trade balance (million EUA)	1975	+ 4	- 44	- 41	- 6	+ 61	- 59	+ 25	+ 67	- 83	- 154	- 184	- 227
	1976	- 169	- 163	- 175	- 184	- 245	- 241	- 288	- 451	- 397	- 306	- 390	- 271
	1977	- 276	- 167	- 278	- 96	- 249	- 349	- 148	- 269	- 108			
Gross official reserves (FF '000 million)	1975	95.92	96.49	97.37	98.52	100.52	100.21	93.19	94.59	95.57	99.66	101.79	100.98
	1976	99.71	95.62	94.75	88.39	88.21	89.65	85.51	85.21	85.33	86.49	86.52	91.53
	1977	92.20	92.37	92.31	92.94	93.23	103.11	101.59	101.90	101.98	102.06		
Bank lending* (FF million)	1975	647.5	656.0	660.5	667.1	670.8	681.0	689.5	697.4	703.1	711.3	720.3	728.7
	1976	736.1	749.9	761.2	775.5	779.1	784.5	802.3	808.8	817.6	829.3	836.1	844.2
	1977	861.8	877.4	880.5	889.6	891.1	900.5	906.3					
Money and near money (M2)* (FF '000 million)	1975	651.9	657.5	661.1	664.3	670.9	682.7	693.9	705.6	719.1	730.9	743.8	754.7
	1976	766.4	779.0	783.9	798.2	807.0	812.8	822.5	829.1	835.0	843.7	847.2	851.4
	1977	869.4	879.2	880.6	890.3	898.3	898.3	897.4	915.2				
L.T. interest rates	1975	10.90	10.69	10.34	10.36	10.31	10.21	10.20	10.11	10.10	10.15	10.19	10.18
	1976	10.16	10.16	10.29	10.24	10.19	10.37	10.51	10.61	10.66	10.95	10.94	11.04
	1977	10.66	10.72	10.88	11.12	11.19	11.11	11.07	11.00				
S.T. interest rates	1975	11.42	9.95	9.18	8.26	7.83	7.32	7.29	7.18	6.92	6.68	6.74	6.48
	1976	6.36	7.20	7.64	7.53	7.51	7.60	8.27	9.45	9.25	10.74	10.67	10.44
	1977	9.95	9.83	9.74	9.22	9.09	8.82	8.67	8.52				

Not available

Seasonally adjusted

Source INSEE (except as otherwise indicated)

— Industrial production: excluding construction and public works: about 50% of the comprehensive annual index.

— Production outlook: Balance of replies to monthly business surveys

— Unemployment: unsatisfied job requests at month-end

— Vacancies: unfilled vacancies at month-end

— Private consumption: volume of consumption of manufactured goods, coverage: about 40% of the quarterly index which covers all goods and services

— Consumer prices: index covering 295 items

— Wages and salaries: index of hourly wage rates, all sectors, nationwide, as at first day of quarter

— Imports of, exports of, excluding military supplies

— Balance of trade: difference between the seasonally adjusted values of imports and exports

— Gross official reserves: gold and foreign exchange reserves, SDR's and position at IMI Source EUROSTAT

— Bank lending: total bank lending, position at end of month Source Banque de France

— Money and near money: position at end of month Source Banque de France

— L.T. interest rates: yield on bonds issued by the public and semi-public sectors

— Short-term interest rate: overnight rate private loans

- Aids to recruitment until 30 June 1978 no social security contributions will be payable in respect of young people under the age of twenty-five and assistance will be provided if they are employed abroad
- Vocational training, which is the subject of two measures: practical traineeships in firms consisting of 200 hours' training, and six to eight months training courses organized.
- All employees in industry and commerce between the ages of 60 and 65 may, subject to certain conditions, retire on an early retirement pension equal to 70 % of their last gross wage.
- Family allowances were increased by 10.6%.

August:

- The Government adopted additional measures to sustain economic activity:
- The allowance paid to low-income families at the beginning of the school year was increased by FF 300 to FF 454 for each child under 16 years of age.
- The cost of bank credit was slightly lowered (from 9.60% to 9.30%).
- The discount rate was lowered from 10.5% to 9.5%.
- FF 1 000 million in supplementary credits was to be made available to firms on preferential terms by the Crédit National.
- FF 900 million in appropriations set aside in the 1977 budget will be released to assist public works (in particular roadbuilding) and housing

September:

- The Government adopted the draft 1978 budget, under which central government expenditure in 1978 is to increase by 12.5%, or at the same rate as that forecast for gross domestic product in value terms (4.5% in volume, with a rise in prices of 7.8%). The budget deficit is planned to total FF 8 900 million or 0.4% of gross domestic product

October:

- The minimum hourly wage (SMIC) was raised from FF 9.58 to FF 9.79, an increase of 2.2% since 1 July.
- The Government adopted measures intended to increase occupational mobility (transport vouchers, removal allowances and dual residence allowances)
- FF 400 million in supplementary credits were released for the benefit of the small craft industries. For this purpose, the "banques populaires" were authorized to issue a FF 200 million loan, and ceilings on equipment loans (by the Société de caution mutuelle artisanale) were partially removed

November:

- For 1978, the official growth targets for bank lending and money supply were fixed at 13.2% and 12% respectively.

D. Ireland

Economic growth has accelerated over the past few months as a result of the persistent development of exports and private consumption. Thus for 1977 as a whole, gross domestic product could grow by more than 5% in real terms, the highest rate in the Community. Employment has improved somewhat and the inflation rate has moderated. The trade balance has, however, worsened.

Economic policy has been aimed, as a priority, at employment, in particular by the creation of jobs in the public sector. The outlook remains favourable for a continued growth of demand and production. The external constraint could, however, strengthen and reduce the room for manoeuvre of the authorities' employment stimulation policy.

1. Overall assessment and main policy issues

The overall performance of the Irish economy over the past few months has, on the growth front, been considerably more favourable than that in other Community countries. Firstly, despite the relative weakness of world demand Irish exports have continued to grow rapidly. Secondly, domestic demand has become more and more sustained, the greater than expected acceleration of consumer expenditure being complemented by the persistent progress of private investment. For 1977 as a whole, the growth rate of gross domestic product in volume should exceed 5% on a year to year basis. On account of the open nature of the economy, this has led to a greater dependence on external supplies and a pronounced deterioration in the trade deficit. Progress has been made on the anti-inflationary front, the inflation rate now being below 12% on the previous year. The acceleration of growth has, in the past few months, resulted in improved employment figures but the unemployment rate still remains above 9% of the labour force.

Faced with these developments, government strategy has been aimed as a priority at the employment problem. Numerous measures¹ have been taken over the past months in order to reduce unemployment; the majority by creating jobs in the public sector. In addition, in conformity with the electoral programme of the new government, motor vehicle tax on private cars has been abolished² and the government has been endeavouring — within the framework of the preparation of the coming budget — to lay down the basis of a new pay agreement which would respect the limits envisaged last June.

In general, this growth permitting policy which has enabled appreciable short term results to be achieved, holds a certain amount of risks for the future. In the first place, although the current balance of payments deficit looks as if it will be maintained this year within acceptable limits, it is to be feared that adverse developments could occur as a result of the stimulation of consumer demand

¹ See list in annex.

² All private cars, except those over 16 H.P.

TABLE 1
Key indicators

Ireland	Unit	1970-1974 average ^{3 4}	1975 ⁴	1976 ⁴	1977 ⁵
Gross domestic product, volume	% change	3.7	0.4	3.2	5.5
of which: industry ¹	%	4.9	- 6.2	9.0	10.0
Gross domestic product in volume per person in employment	% change	3.7	1.9	4.6	4.8
Total employment (number of persons) ²	% change	0	- 1.5	- 1.4	0.7
Unemployment	as % of labour force	5.9	7.9	9.4	9.4
Compensation of employees per wage and salary earner	% change	12.2	24.6	21.0	17.0
Price index of private consumption ¹	% change	10.8	21.3	17.0	13.7
Current account balance ¹	Mio £	- 109.4	- 18.0	- 150	- 220

¹ National accounts concept, on annual basis

² Domestic concept

³ Geometric mean of the change from 1969 to 1974, unemployment and current account balance arithmetic mean over the five years

⁴ Source Economic Review and Outlook, June 1977

⁵ Estimates of Commission's Departments

which may be accompanied by a possible moderation in exports, linked to the appreciation of the pound. Such a scenario would not add to the productive potential of the economy and would, if it arose, indicate the need for countervailing action. In addition, the comments made by the Commission on the occasion of the recent communication to the Council on the subject of the operation of budgetary policy in 1978 remain valid. These imply, in particular, a prudent regulation of non-priority expenditure and an expansion of the tax base in order to avoid too large an increase in the net borrowing requirement.

2. Recent developments

In the past few months the Irish economy has seen rapid growth, stability in unemployment, a moderation in price rises and a deterioration in the trade balance.

The acceleration in growth stems from the persistent dynamism of **exports** and business investment: thus industrial and agricultural sales have grown by 5% and 10½% respectively in the period August-October on the preceding period.¹ But it has also been as a result of the sustained development of private **consumption**, as is shown by the continued buoyancy in retail sales in the third quarter: in particular, sales of new cars have grown very rapidly as a result of the abolition of motor tax applied in August. Private **investment**, judging from the latest surveys, is still growing rapidly. The construction sector has equally benefited from the stimulatory measures taken during the summer. Cement sales rose by 16% in the period August-October on the preceding period.

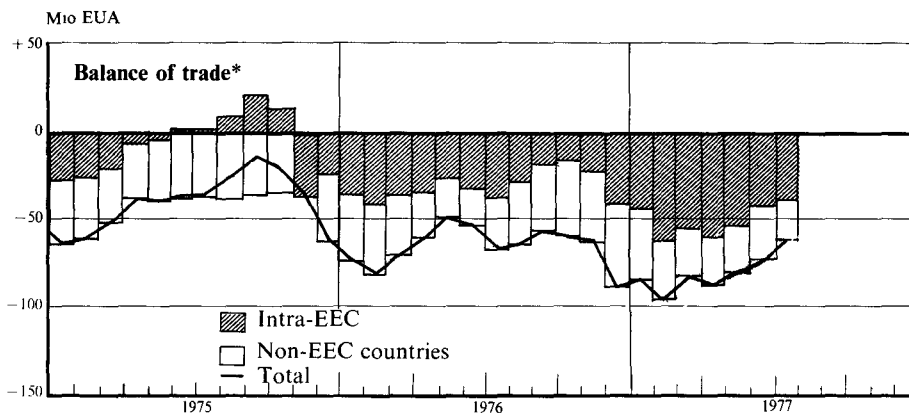
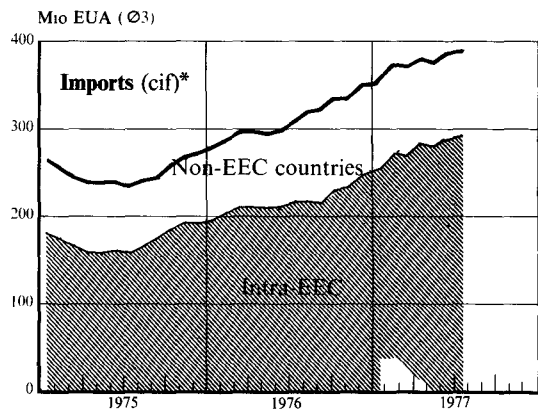
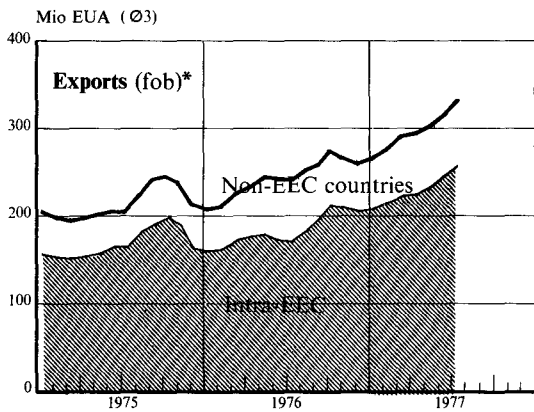
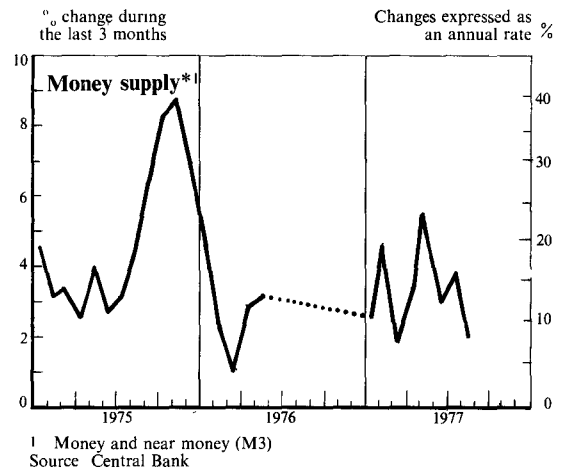
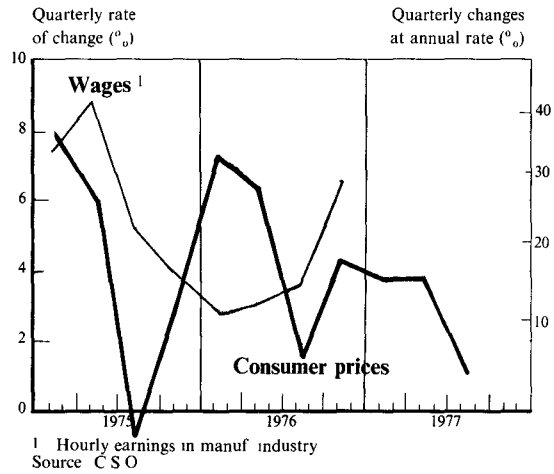
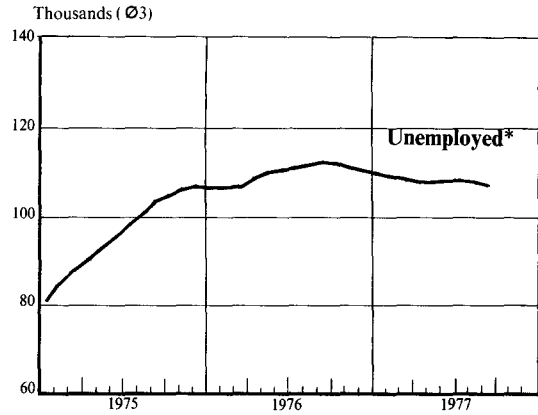
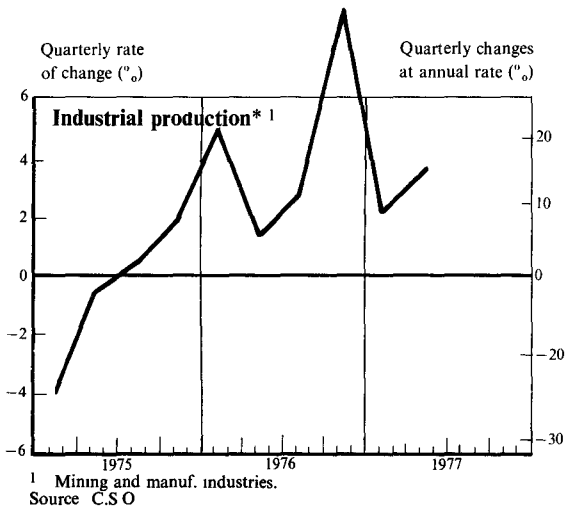
As a counterpart to this expansion in demand, **production** has continued to react favourably. Industrial output grew more rapidly in the second quarter. Agricultural production has grown as well as a result of a favourable harvest and higher cattle output. **Employment** improved quite rapidly and lately the rate of unemployment has tended to stabilise. At the end of October it was 9.4% of the labour force as against 9.9% in August 1976 (the month in which the highest level was recorded).

The rise in **prices** has continued to moderate as a result of a slower development in non-food prices. At mid-August the consumer price index was only 1% higher than in the previous quarter.

Import growth in value has accelerated (+5.2% in August-October on the preceding three months) despite a moderation in import prices. As a result, the **trade balance** has deteriorated substantially, reaching a monthly average of £ 54 m. during the period in question. Due to back payments of EEC transfers and exports of services, the current account deficit has however been less substantial than initially expected. Despite a low level of external borrowing, the **foreign exchange reserves** have continued to grow, reflecting private capital inflows. Since mid-October the **exchange rate** of the pound has appreciated (+1½% on a trade weighted basis).

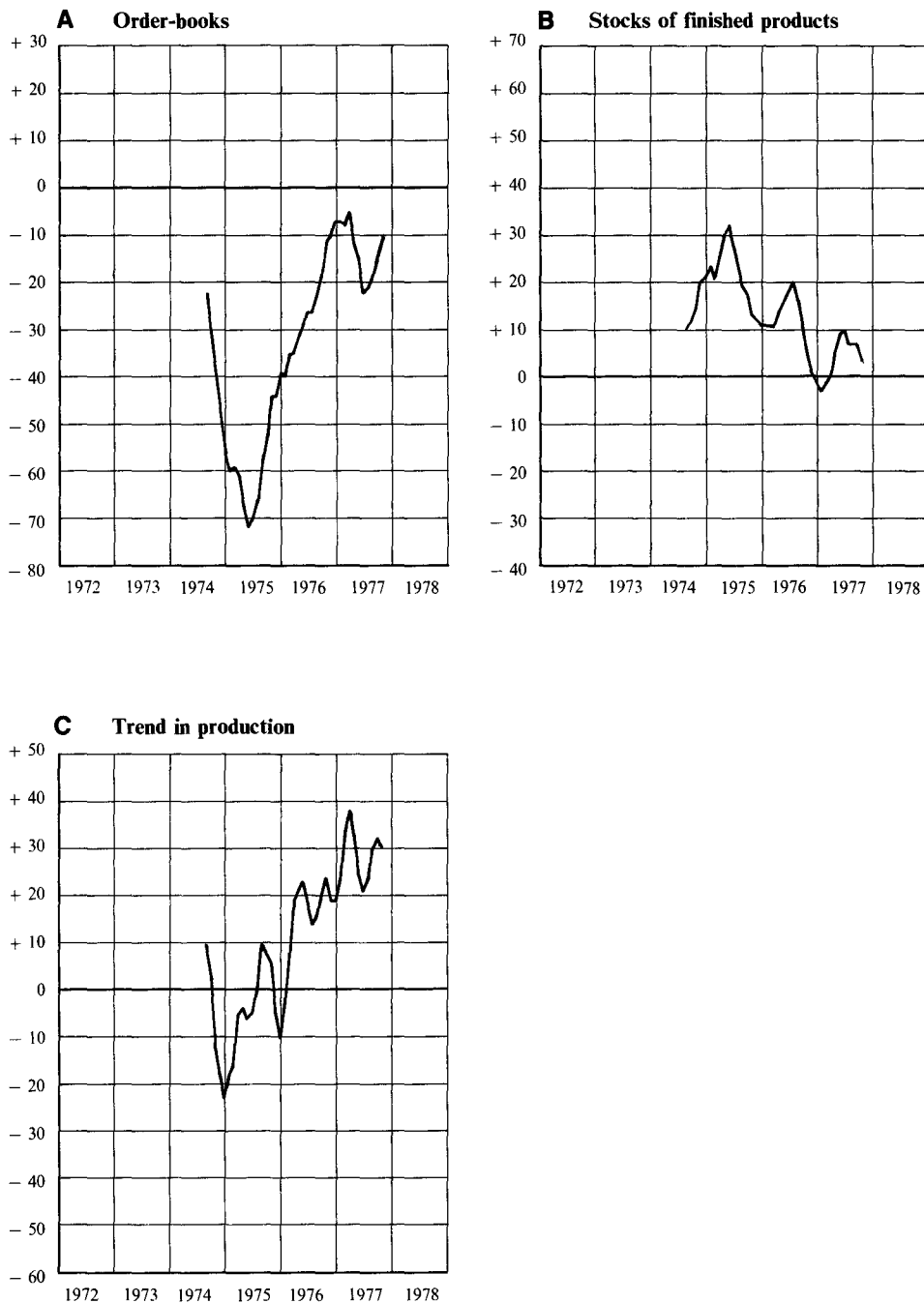
Despite additional expenditure and shortfalls in certain receipts due to recent measures, the **public sector borrowing requirement** for 1977 will be below the budgetary forecasts of January, in part due to the reduction in the cost of debt servicing.

¹ Seasonally corrected.



* Seasonally adjusted figures.
Ø3: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



NOTE:

These charts are based on answers to questions in the EEC business survey, carried out in Ireland by the CII-ESRI. Graphs A, B and C show a three months moving average of the difference between "above normal" and "below normal" answers to the following questions:

- a) Do you consider that your present total order-book is, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- b) Do you consider that your present stocks of finished products are, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- c) Do you think that over the next three or four months your firm's seasonally adjusted production trend will be:
 - (1) up
 - (2) unchanged or
 - (3) down?

TABLE 2

Demand for and supply of goods and services

Ireland	1975 ²	1976 ²			1977 ³			1978 ³
	At current prices Mio £	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	2 366	2.8	17.0	20.2	5.0	13.7	19.4	6
Public consumption	700	2.0	19.7	22.1	3.5	16.0	20.1	5½
Gross fixed asset formation	873	4.4	17.9	23.1	9.0	16.0	26.5	9½
Domestic final uses (excluding change in stocks)	3 939	3.0	17.7	21.2	5.6	14.7	21.1	6½
Domestic final uses (including change in stocks)	3 870	6.7	16.4	24.3	6.3	14.6	21.9	7
Exports ¹	1 631	8.4	21.8	32.1	12.5	18.0	32.7	11
Imports ¹	1 835	15.4	17.6	35.7	13.0	20.0	35.6	13½
Gross domestic product at market prices	3 666	3.2	18.3	22.0	5.5	13.1	19.5	5
		Contribution to percentage change in gross domestic product						
Domestic final uses (excluding change in stocks)	3 939	3.2	—	22.8	6.0	—	22.7	7½
Change in stocks	— 69	3.9	—	2.8	0.8	—	0.9	½
Balance of exports and imports ¹	— 204	— 4.0	—	— 3.6	— 1.2	—	— 4.1	— 2½

¹ Goods and services.

² Source: Economic Review and Outlook, June 1977

³ Estimates of Commission's Departments

3. Outlook

In the coming months growth should continue at a rapid pace and the increase in Gross Domestic Product should be over 5% for 1978 as a whole. Export expansion will remain strong, more especially since accelerating sales to the United Kingdom should compensate for some erosion of sales elsewhere because of the strength of sterling. Domestic demand could register even more substantial progress. Indeed, even given the hypothesis of marked moderation in the growth of incomes, private consumption should be stimulated by wage drift already observed in 1977 and the tax cuts at the beginning of 1978. In addition, public consumption will grow appreciably as a result of already adopted or proposed measures. On account of the delay in implementing certain public investment projects, it is to be expected that their development will accelerate in the coming months and should largely compensate for an eventual moderation of investment growth in the private sector. Construction sector investment is likely to remain dynamic.

As a counterpart of this behaviour in demand, production will continue to register further progress, although this could be a little slower than in 1977 as greater degrees of capacity utilisation are achieved.

The labour market picture is unlikely to change markedly. However, unemployment could still moderate further in spite of the growth in the labour force.

The rise in prices should slow down further; the degree however will depend to a large extent on the outcome of pay negotiations for 1978. Import volume growth will remain very high, even though the proposed buy-Irish campaign should have some effects. Thus, despite an expected improvement in the terms of trade, the current balance of payments deficit should still grow in 1978 to reach at least £ 400 million.

In these circumstances, the principal problem facing the authorities is to avoid the risk that a too pronounced expansion of consumer demand could pose for external equilibrium, and in the longer run for employment. This implies an appropriate demand management policy and the successful conclusion of a pay agreement within the limits envisaged. In order that this can be accepted within the intended framework and in conjunction with the already proposed tax changes, further progress in the process of including agricultural incomes in the tax net will undoubtedly be an important factor in economic strategy.

TABLE 3
Main economic indicators

Ireland	Year	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec
Industrial production* (1970 = 100)	1975		110.4			109.8			110.3			112.5	
	1976		118.2			120.0			123.5			125.8	
	1977		128.7			133.5							
Unemployed* (1 000)	1975	83.4	85.4	88.6	92.9	96.9	99.6	101.9	104.3	105.8	107.2	107.4	109.2
	1976	107.4	108.9	110.4	111.7	112.0	112.2	114.3	114.1	112.9	112.0	111.5	110.9
	1977	109.6	109.0	109.5	109.0	108.6	109.0	109.2	109.2	107.7	107.1		
Private consumers' expenditure* (1970 = 100)	1975	177.8	177.5	178.2	184.5	189.5	187.5	198.0	194.0	202.4	201.7	208.9	223.2
	1976	219.7	225.6	212.8	227.8	228.5	230.3	223.7	227.4	243.8	241.9	253.1	267.3
	1977	250.6	259.2	262.5	267.6	277.5	272.7	282.3					
Consumer prices (1970 = 100)	1975		177.8			188.6			187.1			192.2	
	1976		206.2			219.1			222.4			231.8	
	1977		240.6			249.7			252.4				
Visible imports* (million EUA)	1975	275.0	272.0	220.2	252.1	240.2	228.5	252.1	228.3	253.5	261.8	274.3	281.5
	1976	266.5	287.2	315.0	291.6	286.6	309.1	303.2	309.7	330.4	309.7	359.0	328.7
	1977	369.5	363.2	402.7	365.0	389.3	395.7	388.9	395.8				
Visible exports* (million EUA)	1975	212.6	201.0	172.1	210.9	211.4	179.8	225.5	203.8	231.6	268.6	230.3	205.6
	1976	199.9	211.9	218.5	250.8	241.0	248.5	246.1	229.1	280.2	272.8	271.9	260.7
	1977	252.9	283.1	302.4	291.9	295.8	317.3	341.4	333.4				
Balance of trade* (million EUA)	1975	- 62.4	- 71.0	- 48.1	- 41.3	- 28.7	- 48.7	- 26.7	- 24.5	- 21.9	+ 6.8	- 44.0	- 76.0
	1976	- 66.6	- 75.3	- 96.5	- 40.8	- 45.6	- 60.6	- 57.1	- 80.5	- 50.2	- 36.9	- 87.2	- 68.0
	1977	- 116.6	- 80.1	- 100.3	- 73.0	- 93.5	- 78.3	- 47.5	- 62.4				
Official foreign exchange reserves (million EUA)	1975	952	929	929	932	974	1 025	1 106	1 095	1 140	1 097	1 139	1 298
	1976	1 422	1 403	1 495	1 491	1 463	1 382	1 313	1 362	1 490	1 476	1 560	1 609
	1977	1 669	1 604	1 665	1 584	1 588	1 552	1 619	1 728	1 842	1 869		
Money supply (million EUA)	1975	1 016	982	1 044	1 020	998	1 015	1 042	1 064	1 128	1 101	1 112	1 175
	1976	1 158	1 153	1 129	1 107	1 060	1 144	1 132	1 148		1 071	1 099	1 191
	1977	1 152	1 121	1 172	1 165	1 197							

Not available

* Seasonally adjusted

Source: EUROSTAT (except as otherwise indicated)

Industrial production: CSO Mining and manufacturing industry

Unemployment: Number of registered unemployed

Private consumers' expenditure: Retail Sales Index in value

Visible trade: Imports cfr. exports tob

Balance of trade: difference between values of imports and exports

Official Foreign Exchange Reserves: Official External Reserves, Monetary Authorities' reserves of convertible currency, holdings of special drawing rights and reserve position in the IMF

Money Supply: Currency and current accounts

Major economic policy measures

July 1977:

— A new government department of economic planning and development whose functions include medium and long term economic and social policy and planning is established.

— A grant scheme is introduced for persons purchasing or building their first house or flat. The grant amounts to £1 000.

— The Minister for Local Government provides extra grants to local authorities of £5.5 million to enable them to create 950 new jobs by the end of the year.

— The system of marriage differentiation in public service pay is eliminated with effect from 1 July 1977, at a cost of £3.5 million in a full year.

— The Minister for Local Government raises the limit of local authority house purchase loans from £4 500 to £7 000. The annual income eligibility limit for applicants is also increased. The new measures will cost £25 million and provide an extra 1 000 jobs.

— Additional educational expenditure of £3.75 million is announced to provide employment for an additional 1 200 school teachers.

August:

— Annual road tax on all cars up to and including 16 horse power is abolished from August 1977.

— The Minister for Health and Social Welfare announces plans to create 570 new jobs in the health services.

September:

— Measures are taken by the Central Bank to provide a suitable climate

for the further development of the Irish foreign exchange market by withdrawing from its dominant position in the market. These included a minimum amount in which the Bank will deal with authorized dealers, a reduction in the number of currencies quoted, a discontinuation of dealing by the Bank in forward options, measures to encourage dealing between local banks and the establishment of a Foreign Exchange Committee to monitor market activity and encourage further improvement in foreign exchange practices.

—The Employment Incentive scheme is widened to cover employers in hotels, restaurants and the catering trade from 1 September.

— The Minister for Industry and Commerce announces a series of measures aimed at increasing the number of jobs provided by small industry. Additional expenditure will amount to £2 million for the creation of 800 new jobs.

— Plans are announced for the establishment of an industrial development consortium under the chairmanship of the Minister for Industry and Commerce in an effort to increase employment by setting targets and monitoring progress in job expansion. The consortium will bring together representatives of various State agencies

October:

— Social Welfare rates are increased by approximately 5% from the beginning of October.

— Estimates by the National Economic and Social Council show that if full employment is to be attained by 1986, between 23 000 and 28 000 new jobs will have to be created each year

E. Italy

In the summer months the current account again closed with large surpluses. The slowdown in the rate of price increases, by contrast, was only partially maintained and in August and September there was, if anything, some fresh acceleration. Economic activity in the third quarter was still tending to slacken, though much less sharply than in the second quarter. The degree of plant utilization fell further, and the number of unemployed maintained the upward tendency in evidence since the beginning of the year.

Economic activity can be expected to recover towards the end of the year and particularly in 1978. The Government considers it desirable for the growth of real gross domestic product to reach 3% next year and believes that this rate can be achieved under a special programme.

The current account is likely to remain in surplus, but the upward movement of prices will probably not be checked to the extent agreed with the IMF and the Community.

1. Overall assessment and main policy issues

The stabilization efforts made by the Government especially since the autumn of 1976 produced very tangible results in 1977. The ultimate economic policy objectives laid down in connection with the last Community loan to Italy, at the Council meeting held on 17 May 1977, namely slowing down the upsurge in prices and improving the balance of payments on current account, have been achieved in full. Indeed, the consumer price increase between December 1976 and December 1977 will probably be under 16%, and the current account, which was still in heavy deficit in the early months of 1977, showed substantial surpluses in the spring and the second half of 1977. At the same time the public sector deficit (Treasury, local government, social security institutions and ENEL) fell as a proportion of gross domestic product in money terms (from 13.2% in 1976 to probably 10½% in 1977).

However, although the monetary authorities relaxed interest rate policy to a certain extent, these results have been accompanied by a recessionary trend in the second and third quarters. Even so, real gross domestic product is likely to rise by approximately 2% between 1976 and 1977 while at the end of 1976 growth in 1977 was still expected to be virtually nil. Average unit wage costs continued on a very strong upward trend in 1977.

For 1978 the Italian Government, according to its recent report on forecasts and norms, is aiming at a 3% increase

in real gross domestic product, in order to sustain employment. In view of the balance of payments situation, however, this growth rate is not to be achieved through a general boost to demand, but through selective stimulation of investment ("qualified economic recovery" by "programmed actions") and would inter alia depend on responsible behaviour by the public authorities, employers and unions. In the Government's opinion, therefore, real wages should not rise in 1978 but be kept steady. According to the above report, if real gross domestic product grows by only 2% — the rate on which the central government budget for 1978 is based — prices will rise by 12% on average for the year;¹ the balance of payments on current account would close with a surplus of Lit 2 000 000 million. This would be compatible with a ceiling of Lit 19 000 000 million on the public sector deficit (instead of the Lit 14 450 000 million agreed with the Community and the IMF) and a ceiling of Lit 34 000 000 million on domestic credit expansion (instead of Lit 30 000 000 million, as agreed with the IMF).

¹ The Commission's departments consider that this rate implies a price increase between December 1977 and December 1978 that considerably exceeds the 8% agreed with the Community.

TABLE 1
Key indicators

Italy	Unit	1970-1974 average ^{5 6}	1975 ⁶	1976 ⁶	1977 ⁷
Gross domestic product, volume	% change	4.1	- 3.5	5.6	1.9
of which: Industry ¹		4.3	- 9.2	12.0	1.2
Gross domestic product, volume, per person in employment	% change	3.8	- 3.6	4.8	1.7
Total employment (number of persons) ²	% change	0.3	0.1	0.8	0.2
of which: — Independent entrepreneurs		- 2.6	- 0.9	- 0.1	- 0.5
— Wage and salary earners		1.6	0.6	1.2	0.5
Unemployment	as % of labour force	3.3	3.3	3.7	7.0 ³
Compensation of employees per wage and salary earner	% change	16.0	20.9	21.2	25.0
Price index of private consumption ⁴	% change	9.6	17.6	17.5	18.5
Current account balance ⁴	Lit. '000 million	- 745	- 377	- 2 340	1 160

¹ Excluding building and construction.

² Domestic concept

³ Because of important modifications made by ISTAT in the quarterly surveys of the labour market, this figure is not comparable with those of the previous years

⁴ National accounts concept

⁵ Geometric mean of the change from 1969 to 1974, unemployment and current account balance: arithmetic mean over the five years.

⁶ Source: ISTAT or "Relazione generale sulla situazione economica del Paese, 1976"

⁷ Estimates of Commission's Departments

2. Recent developments

After growing very rapidly in the spring, the value of merchandise **exports** in the summer and in early autumn ceased to tend upwards. But this was probably only a passing phase of consolidation. Exports in the third quarter were 21.5% up on a year earlier. Foreign exchange receipts from services were still rising sharply, with receipts from tourism in July no less than 95% up on a year earlier.

Following a decline in absolute terms in the second quarter, domestic demand in the third quarter may well have grown again slightly in terms of value. In terms of volume, however, it probably ran level or fell a little. According to the indicators (mostly qualitative) available so far, the value of **private consumption** probably rose, after declining in the spring. This is at any rate what is suggested by the results of the EEC business surveys on order books and stock levels in the consumer goods industry. Households' purchasing power indeed tended to rise owing to the cost-of-living supplements paid under the sliding wage scale agreements.

Investment in plant and machinery no doubt fell in the period under review, though perhaps more slowly than in the spring. This was probably due mainly to the continuing decline in capacity utilization¹ and the unsatisfactory trend of business profits. Although less pronounced than before, the downward tendency of stockbuilding also seems to have persisted.

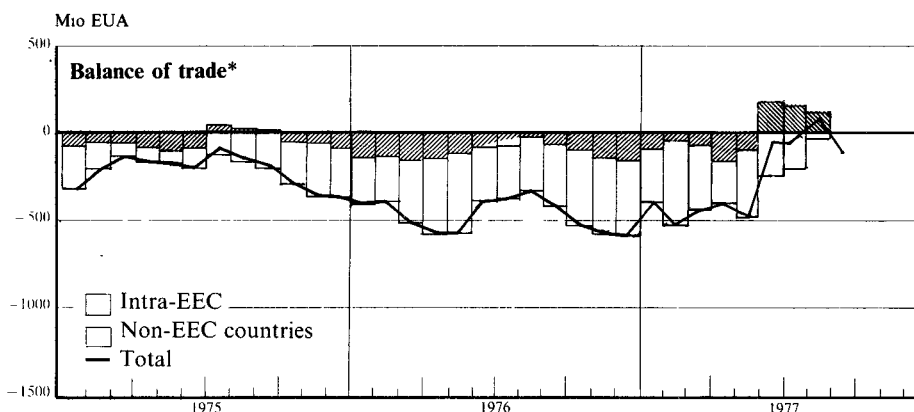
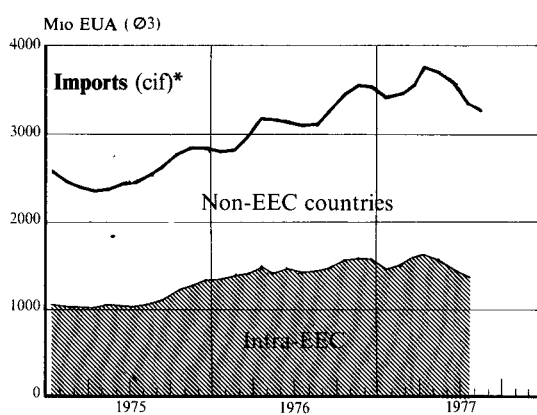
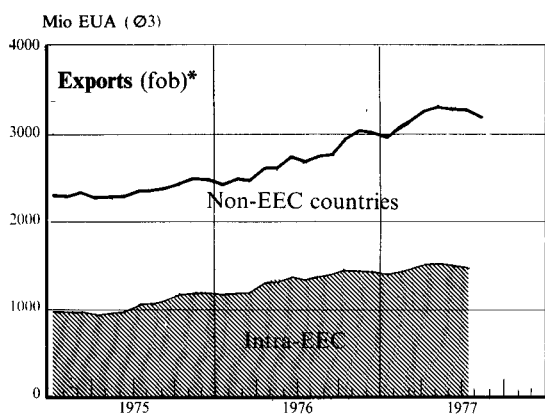
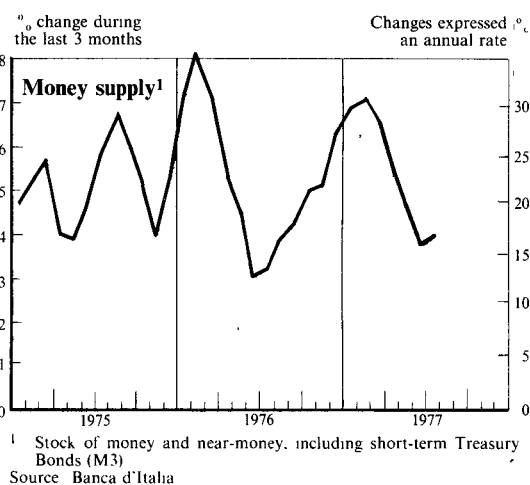
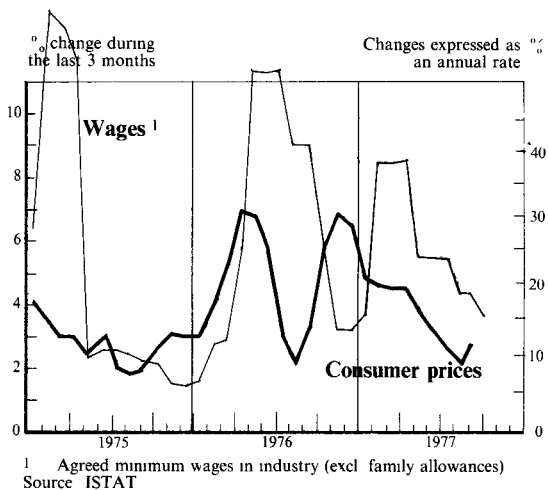
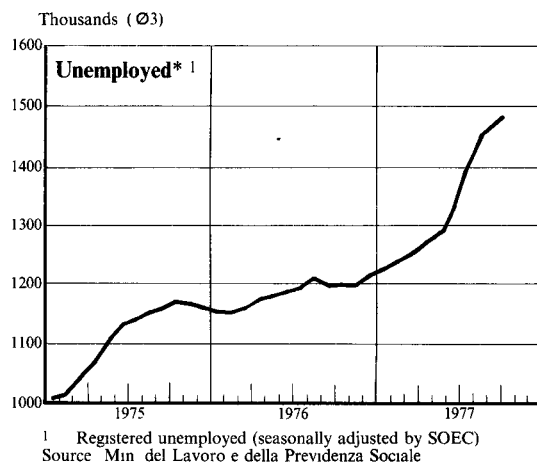
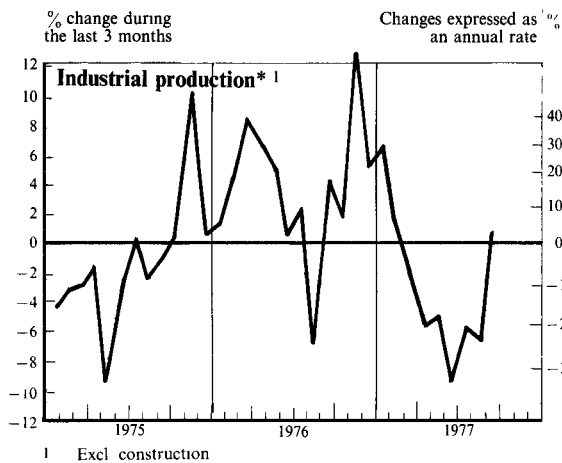
On the supply side, **industrial production** showed a further underlying fall between the second and the third quarter, especially where plant and machinery and consumer goods are concerned. According to the ISTAT indices — seasonally adjusted by ISCO — it declined by 1.4%, appreciably less than in the second quarter when it was down by 7.5%. Moreover, industrial production in July, August and September tended upwards again, on a month-to-month comparison. The unadjusted level in the third quarter was approximately 5% down on a year earlier (up 4.4% in the second quarter, up 3.6% in the first nine months).

Given the weak trend of overall demand, imports also showed a particularly marked fall-off in the third quarter. The value of merchandise **imports** in this period was only 7½% up on the level of a year earlier (first quarter: up 33.4%, second quarter: up 18.6%).

The third quarter saw a continued downward tendency not only in the degree of utilization of plant capacity but also in the **level of employment**.² In July-August, in industrial firms with 500 or more employees it was at any rate some 5% below the corresponding level of the

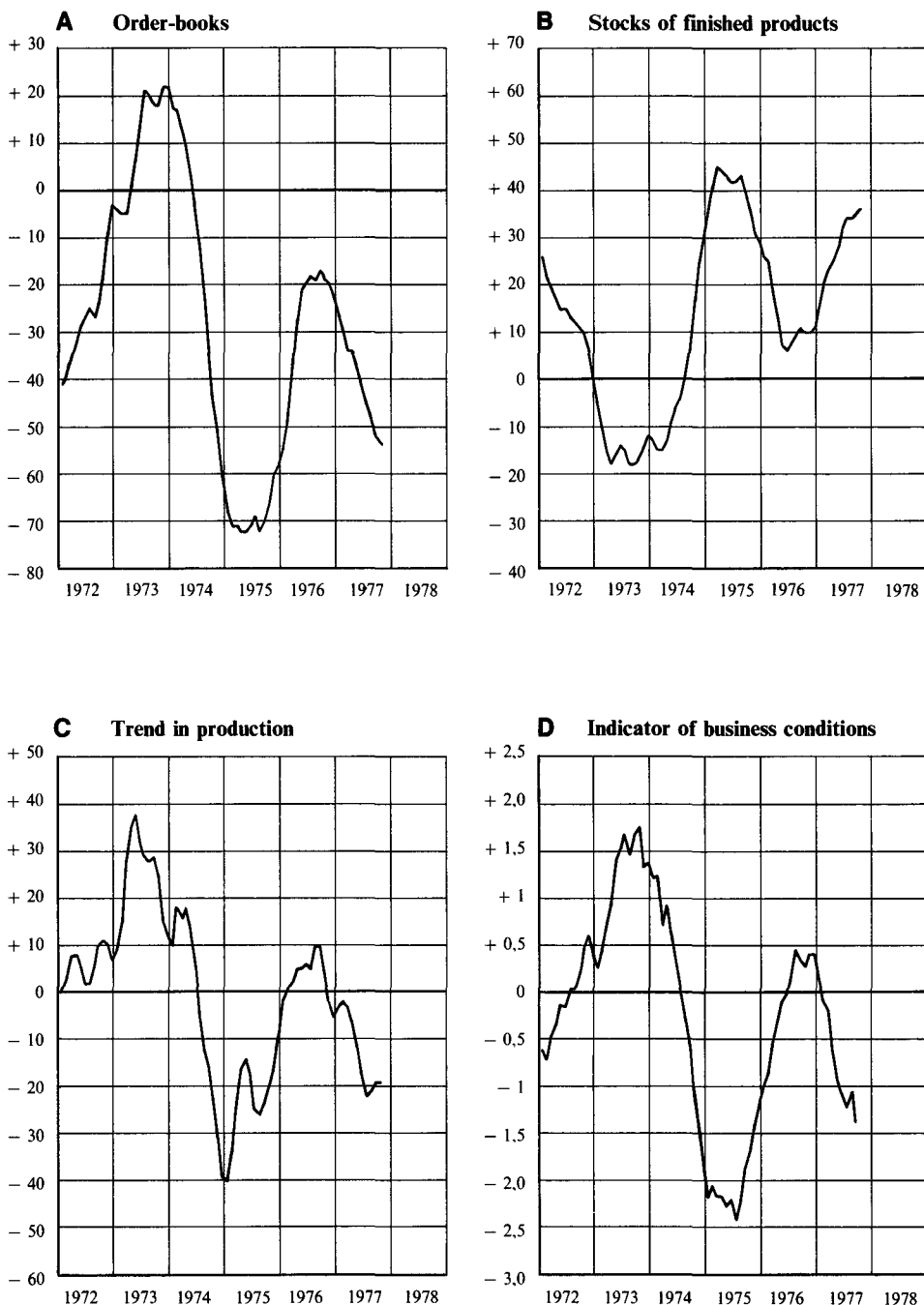
¹ According to the ISCO-Mondo economic business surveys, capacity utilization in industry in September was 71.6% (compared with 75.6% in December 1976).

² Number of persons employed multiplied by the average number of hours worked per employee.



* Seasonally adjusted figures.
Ø3: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



NOTE:

These charts are based on answers to questions in the EEC business survey, carried out in Italy by ISCO-Mondo Economico.

Graphs A, B and C show a three months moving average of the difference between "above normal" and "below normal" answers to the following questions:

- Do you consider that your present total order-book is, for the season :
 - above normal
 - normal or
 - below normal?
- Do you consider that your present stocks of finished products are, for the season :
 - above normal
 - normal or
 - below normal?
- Do you think that over the next three or four months your firm's seasonally adjusted production trend will be
 - up
 - unchanged or
 - down?

Graph D presents an indicator of industrial business conditions, based on a principal component analysis of the answers to four questions in the monthly business survey. These are the above three questions together with a question on the recent trend on production.

TABLE 2
Demand for supply of goods and services

Italy	1975 2	1976 2			1977 3			1978 3
	At current prices Lit '000 million	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	76 744	3.2	17.5	21.3	1.9	18.5	20.8	2.9
Public consumption	16 153	1.9	20.5	22.8	2.0	21.1	23.5	2.3
Gross fixed asset formation	23 753	2.3	18.6	21.3	4.0	18.9	23.6	3.2
— Building and construction	14 003	- 1.2	19.9	18.5	1.0	20.0	21.2	2.5
— Plant and machinery	9 750	7.2	17.0	25.3	8.0	17.5	26.9	4.0
Domestic final uses (excluding change in stocks)	116 650	2.9	18.1	21.5	2.3	18.9	21.7	2.9
Domestic final uses (including change in stocks)	115 739	5.5	19.7	26.3	0.4	18.5	19.0	3.6
Exports ¹	26 311	12.6	18.9	33.9	7.0	21.0	29.5	7.0
Imports ¹	27 835	13.1	24.7	41.0	0.8	18.1	19.0	7.9
Gross domestic product at market prices	114 215	5.6	17.8	24.4	1.9	19.3	21.6	3.3
		Contribution to percentage change in gross domestic product						
Domestic final uses (excluding change in stocks)	116 650	2.8	—	22.0	2.3	—	21.6	2.9
Change in stocks	- 911	2.6	—	4.6	- 1.9	—	- 2.1	0.7
Balance of exports and imports ¹	- 1 524	0.2	—	- 2.2	1.5	—	2.1	- 0.3

¹ Goods and services.

² Source: Relazione generale sulla situazione economica del Paese, 1976

³ Estimates of Commission's Departments

previous year (first quarter: up 8%, second quarter: up 3%). The average number of hours worked per employee and probably also the number of employees tended to fall. The number of **unemployed** (Ministry of Labour statistics), which had been on a rising trend since the beginning of the year, showed a particularly sharp increase in the period under review, although this was at least partly attributable to special factors. ¹ According to ISTAT's most recent sample survey, the number of unemployed in July totalled 1 692 000 or 7.7% of the labour force, redefined since the beginning of the year (6% in North and Central Italy, 11.5% in Southern Italy and the islands). 74% of the unemployed were between 14 and 29 years of age.

The slackening in the rate of **price** increases was only partially maintained in the third quarter. Indeed, between June and September consumer prices rose somewhat less sharply but wholesale prices more sharply than between March and June. Calculated on an annual basis, consumer prices rose by 11.8% (compared with 13.2% between March and June) and wholesale prices by 8.6% (7.1%). In both August and September, consumer and wholesale prices accelerated again compared with the

month before. In September consumer prices were 18.2% and wholesale prices 14.3% up on the corresponding level of the previous year.

The trend of merchandise exports and imports described above produced a further improvement in the **trade balance** which was much larger than the normal seasonal movement. On a cif/fob basis, the third-quarter balance closed with a surplus of Lit 329 000 million, compared with a deficit of Lit 742 000 million a year earlier. Since service transactions also produced another large surplus, the **current account balance** (on a transactions basis) closed with a surplus of some Lit 1 500 000 million (some Lit 700 000 million a year earlier). ² As a result of several foreign loans and owing to the substantial difference between interest levels in Italy and abroad, the capital account was also in surplus. The **overall balance of payments** closed with a surplus of no less than Lit

¹ As a result of the law to promote the employment of young people, passed last June, a great many persons who previously were not included in the labour force registered on the lists of job-seekers displayed in the Ministry of Labour offices. Quarterly Survey 2/1977, p. 64.

² First nine months: a surplus of some Lit 830 000 million, compared with a deficit of Lit 1 624 000 million a year earlier.

2 474 000 million.¹ The simultaneous increase in the net official gold and foreign exchange reserves — by Lit 618 000 million to Lit 14 884 000 million — fell far short of this surplus because the Italian monetary authorities repaid a substantial amount of their own debt to the IMF and the Bundesbank and because the banks reduced their short-term external indebtedness, which had risen sharply in the first seven months, to Lit 5 774 000 million in August-September (December 1976: Lit 2 635 000 million). The weighted **exchange rate** of the lira against all other currencies remained virtually steady in the third quarter; in October it deteriorated by 0.8%. From the end of June to the beginning of December a slightly rising trend was discernible against the dollar. On the forward market too the dollar rate of the lira hardened.

Cash disbursement under the **central government budget** again grew more slowly than predicted in the third quarter. But cash receipts also fell appreciably short of forecasts, mainly because the growth of indirect tax revenue slackened as a result of the economic situation. Overall, for the period January to September, the net borrowing requirement amounted to Lit 8 622 000 million (compared with Lit 7 893 000 million a year earlier). As a result of the additional demands made on the Cassa Depositi e Prestiti since January 1977 in connection with the financing of the local government current deficits, the other Treasury transactions produced a deficit which was appreciably higher than a year earlier. This was matched by a distinct improvement in the remaining Treasury transactions.

The acceleration in the growth of the **monetary base**² induced by the balance of payments trend described above led in the third quarter to a sharper increase in **bank liquidity**, especially since spontaneous demand for bank loans was sluggish. The banks therefore invested their available funds in the new type of Treasury credit certificates³ and in short-term Treasury certificates ("BOT"). Despite the rapid rise in the public sector borrowing requirement, the growth of total **domestic lending** stayed within the limits agreed with the IMF and the Community. The downward trend of **interest rates**, particularly short-term interest rates, continued, especially since the discount rate and the rate for advances against securities, following the cut in June, were again lowered in August (to 11.5%). Interest rates on interbank deposits thus fell from 14.3% in June to 12.1% in October. The yield on bonds issued by the institutions lending against goods and securities was 14.4% in October (compared with 14.6% in June).

3. Outlook

Provided that short-term economic policy stays out the course on which it was set until mid-September, economic activity, boosted by rising export demand and a recovery in domestic demand, is likely to tend upwards again until the middle of next year.

With non-member countries and especially member countries expected to import more, **exports** are indeed

likely to expand. On the domestic demand side, **stock-building** will probably be past its lower turning point around the beginning of the autumn 1977. Investment in plant and machinery too might then enter a phase of slow recovery. A little later, **private consumption** should likewise begin to sustain economic activity.

Assuming that economic activity will increase in the second half of 1978 as well, **real gross domestic product** might well grow by some 3% between 1977 and 1978. The accompanying rise in employment will probably be quite slow and is unlikely to match the increase in the labour force, so that the number of **unemployed** should climb further.

The upward movement of **prices** is likely to gather some momentum in the fourth quarter of 1977 and to continue at the rate reached towards the end of 1977 until the middle of next year. The **current account** will show a surplus for 1978 as whole.

This would mean the achievement in 1978 of the ultimate **economic policy** objective for the current account, which was laid down for the Italian Government at the Council meeting of 17 May 1977 in connection with the last Community loan. The other objective, an increase in consumer prices of no more than 8% between December 1977 and December 1978, is not, however, likely to be met, although the increase will probably be much less steep than between December 1976 and December 1977. In addition, it must be feared that the ceilings on the public sector deficit and the growth in total domestic lending agreed with the Community and the IMF last spring, in order to achieve the ultimate economic policy objectives mentioned above, will be greatly exceeded in 1978 unless corrective action is taken. At the macroeconomic level, major domestic equilibrium conditions will thus remain precarious next year. Enterprises are also confronted with difficult financial problems. The ratio of debt to equity capital has become increasingly unfavourable as a result of the galloping cost increases of the seventies and the insufficient supply of risk capital.

Major economic policy measures

July 1977:

— On 8 July, the obligation on banks to invest at least 30% of the growth of their deposits in fixed-interest securities was extended to the end of 1977. The percentage thus remaining unchanged and taking seasonal factors into account, this extension marks some relaxation of policy and is intended to encourage a fall in the lending rates of banks.

— At the end of July, Italy repaid to the IMF SDR 700 million, equivalent to Lit 720 000 million. This amount represented part of the stand-by credit received in 1974.

¹ According to provisional figures it showed another large surplus in October (Lit 868 000 million).

² Mainly notes and coins in circulation and assets readily convertible into central bank money.

³ Two-year maturity.

TABLE 3
Main economic indicators

Italy	Year	Jan.	Feb.	Mar	Apr	May	June	July	Aug.	Sept	Oct	Nov.	Dec
Industrial production (1970 = 100)	1975	109.6	112.7	108.3	107.5	102.2	105.5	107.0	99.4	107.1	108.0	110.6	107.9
	1976	109.5	115.9	117.7	116.9	122.8	119.9	121.2	114.8	125.2	123.6	129.0	132.0
	1977	132.0	131.4	129.7	124.7	125.1	118.4	117.8	117.5	119.6			
Unemployed (1 000)	1975	996.7	1 010.4	1 023.4	1 079.1	1 112.8	1 131.0	1 141.2	1 140.7	1 175.3	1 171.7	1 169.0	1 163.5
	1976	1 147.4	1 149.7	1 166.4	1 170.4	1 186.5	1 182.2	1 203.6	1 200.2	1 215.9	1 179.3	1 203.2	1 215.2
	1977	1 227.6	1 235.9	1 245.1	1 273.1	1 298.4	1 307.0	1 403.7	1 481.4	1 471.4	1 503.3		
Construction: Housing starts (1000)	1975	14 542	13 659	16 005	16 728	20 881	19 537	17 923	14 873	14 856	16 788	17 206	13 437
	1976	13 601	35 485	21 377	19 692	18 291	14 877	14 591	15 939	15 412	14 584	16 263	17 898
	1977	13 056	14 385	16 411	17 119	16 985	17 480	16 360	15 196				
Private consumers' expenditure: retail sales (1970 = 100)	1975	190.4	195.1	204.6	193.2	204.3	203.6	208.5	200.9	204.5	209.9	208.3	218.5
	1976	224.6	225.8	223.1	245.2	237.5	248.9	238.8	251.7	256.5	261.5	265.9	276.3
	1977	280.2	277.8	281.2	295.1	295.4	311.7	303.6	309.6	321.3			
Consumer prices (1970 = 100)	1975	163.2	165.6	165.8	168.0	169.4	170.7	171.4	172.5	173.9	175.8	177.8	179.2
	1976	181.1	185.1	188.8	193.8	197.7	198.6	199.6	201.8	205.2	211.1	215.7	218.6
	1977	221.4	225.7	228.6	231.4	234.2	235.8	237.2	239.4	242.5			
Visible imports (million EUA)	1975	2 540	2 274	2 542	2 326	2 251	2 539	2 463	2 267	2 839	2 736	2 819	3 210
	1976	2 696	2 629	3 123	3 020	3 317	3 146	3 031	3 139	3 304	3 402	3 843	3 697
	1977	3 351	3 460	3 763	3 628	3 846	3 568	3 200	3 238	3 305			
Visible exports (million EUA)	1975	2 183	2 227	2 335	2 230	2 090	2 335	2 306	2 334	2 469	2 505	2 537	2 652
	1976	2 408	2 212	2 608	2 414	2 775	2 612	2 847	2 676	2 877	2 989	3 127	3 103
	1977	2 950	2 953	3 326	3 212	3 366	3 538	3 085	3 314	3 195			
Balance of trade (million EUA)	1975	- 356	- 47	- 207	- 96	- 161	- 204	- 157	67	- 370	- 231	- 282	- 558
	1976	- 288	- 417	- 515	- 606	- 542	- 533	- 185	- 464	- 427	- 413	- 716	- 595
	1977	- 401	- 507	- 437	- 416	- 480	- 30	- 114	76	- 109			
Official foreign exchange reserves (million EUA)	1975	2 383	2 302	2 451	2 589	2 436	2 439	1 686	1 421	2 121	1 945	1 565	1 119
	1976	847	895	1 257	1 378	1 313	1 607	2 466	2 595	1 451	1 729	2 730	2 852
	1977	2 971	2 707	2 650	2 913	3 896	5 567	6 153	6 272	5 859	6 562		
Monetary base (Lit. '000 million)	1975	34 765	34 730	35 128	35 252	35 818	36 436	37 500	37 914	39 132	39 592	39 258	42 439
	1976	41 774	42 455	43 413	43 630	43 958	44 861	45 393	45 677	45 045	46 930	47 188	49 819
	1977	49 871	50 571	51 506	51 891	52 432	52 247	54 262	54 422				

Not available.

Source: EUROSTAT (except as otherwise indicated).

- Industrial production, excluding construction: adjusted for seasonal variations.
- Unemployed: series provided by the Ministero del Lavoro e della Previdenza Sociale, adjusted for seasonal variations by EUROSTAT.
- Construction: private and public housing starts in Italy. Source: ISTAT
- Private consumers' expenditure: value index of the turnover of major retail outlets, adjusted for seasonal variations.
- Consumer prices: unadjusted index.
- Imports cif, exports fob, adjusted for seasonal variations
- Balance of trade: difference between values of exports and imports, seasonally adjusted.
- Official gold and foreign exchange reserves: position at end of month.
- Gold assets assimilated to gold continue to be calculated on the preceding parity.
- Monetary base: Includes, in particular, the fiduciary issue; sight deposits with the Banca d'Italia, the Treasury and the savings and loans bank; deposits with the Post Office. unused facilities for ordinary advances with the Banca d'Italia; unused liquid assets abroad, in convertible currencies, that banks can freely use

August:

— On 8 August, the scheme decided on at the beginning of February under which the central government would take over part of the burden of firms' social security contributions, was extended to export trading firms and hotel and catering trade.

— On 12 August, Parliament passed, with a substantial number of amendments, the draft law on industrial reorganization and conversion, which had been laid before it at the end of September 1976. The main

purpose of the law is to modernize and transform enterprises in manufacturing industry and in the mining and quarrying sector with a view to making them more competitive on an international level. To this end, a special fund of Lit 2 630 000 million has been set up to assist enterprises that are carrying out reorganization and conversion projects in line with the sectoral intervention programmes drawn up by the CIPI (Interministerial Committee for Industrial Policy). The appropriations for this purpose, including substantial increases in the endowment funds of enterprises in which the government has a holding, will total Lit 8 066 000

million for the period 1977-82. The law came into force on 22 September 1977 but, according to the Italian authorities, it will not begin to produce effects before the middle of 1978.

— On 23 August, the Banca d'Italia decided that the ceiling on bank lending introduced in October 1976 and subsequently extended to the end of March 1978 should, as from September, be extended to apply to bank loans granted to hospitals and mutual insurance companies.

— On 26 August, the discount rate and the rate for advances against securities were cut from 13% to 11.5%. The supplement which can be added in the event of certain limits being exceeded remained unchanged at 3%. As was the case with the reduction of two percentage points announced on 11 June, the Minister for the Treasury stated that the lowering of rates was justified by an easing of inflation and by the favourable balance of payments trend.

— On the same date, the Government announced plans to eliminate the double taxation of distributed dividends and reduce the flat-rate tax on dividends ("cedolare secca") from 50% to 30%. It also made clear its intentions to introduce a number of tax concessions in respect of the purchase of new shares.

— Under a Decree published on 29 August, a number of administrative responsibilities will be transferred from central to local government, in particular to the regional authorities. This transfer covers a substantial number of responsibilities in the social and economic field, in which the central government broadly retains only such powers as come under the headings of national interest and external relations. The cost of implementing the Decree is put at Lit 15 000 million in 1978. A corresponding decree published on the same date listed the central government departments that will have to be abolished.

September

— At the beginning of September, the Banca d'Italia repaid to the Bundesbank \$ 500 million of the loan made by the Federal Republic of Germany in September 1974, and then renewed in September 1976 for a period of two years. The balance still outstanding is \$ 1 500 million.

— A \$ 200 million loan was granted to ENI (Ente nazionale idrocarburi) by a syndicate of European, US and Japanese banks.

— On 20 September, the Government agreed to a draft law introducing prescription charges for pharmaceutical products, payable by persons other than those in receipt of social security pensions and social assistance. The prescription charges will range from Lit 200 to Lit 600, depending among other things on the price of the product prescribed. The scheme is expected to curb the consumption of pharmaceutical products and to reduce the social security deficit.

— On 30 September, the Government published its report on the forecasts and norms for 1978 ("Relazione previsionale e programmatica"). For the first time, the report contained a summary of the draft central government budget, which was presented to Parliament on the same date and which had until 1976 been presented towards the end of July. The draft central government budget was accompanied by a government draft law which anticipated the finance act ("legge finanziaria") and was designed primarily to lay down rules for containing the growth in current expenditure and forestalling any further carrying-forward of unexpended appropriations ("residui passivi"). The forecasts for the trend in the main economic aggregates given in the report and serving as a basis for the draft budget, take account of the need to press ahead with the fight against inflation and to achieve a substantial current account surplus. According to these forecasts for 1978, GDP in real terms is to grow by only 2%, consumer prices are to rise by 12%, and the current account to reach a surplus of Lit 2 000 000 million. However, with a view to helping employment and stepping up productivity, the Government intends to achieve a 3% increase in real GDP in 1978, largely because of measures aimed at stimulating investment.

— The main features of the central government budget for 1978 (budget on an appropriations basis) presented on 30 September are as follows: revenue, excluding borrowings, will be 31.7% up on the initial estimates in the draft budget for 1977 (against a rise of 37.2% in 1977); expenditure, excluding redemption of debts, will grow by 25.8% (against 26.0%); when borrowings and redemption of debts are included, the central government deficit will come to Lit 10 784 million (against Lit 9 849 000 million in 1977). Taking into account the further increase in the State undertakings' operating deficits, the overall deficit will be Lit 12 574 000 million, as against Lit 11 466 000 million for the previous year. The relative share of current expenditure (part of which, however, is ultimately intended for investment purposes) in total budgetary expenditure will again show a slight increase: at 23.1%, the growth in capital expenditure will be smaller than that in current expenditure (25.7%).

October

— Towards the middle of the month, the monetary authorities eased some of the measures (which had been tightened up several times since February 1976) governing the amount of foreign currency which Italian residents travelling abroad could take out of the country.

— On 28 October, the Government extended the rent freeze until the end of January 1978 for tenants whose annual income was less than Lit 8 million.

F. Netherlands

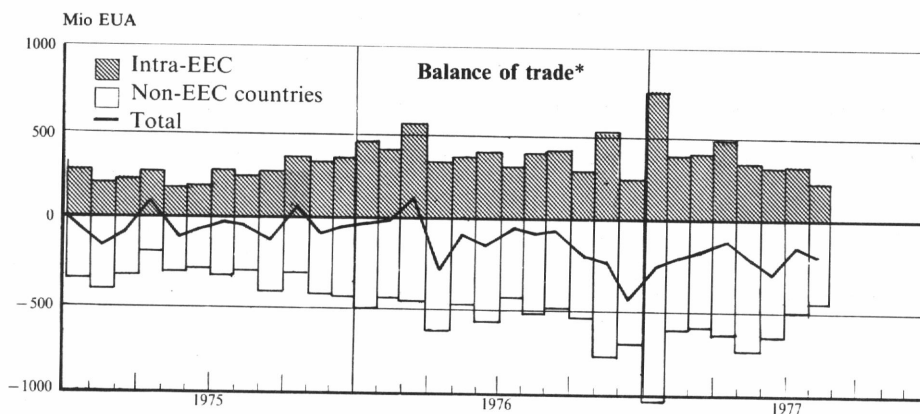
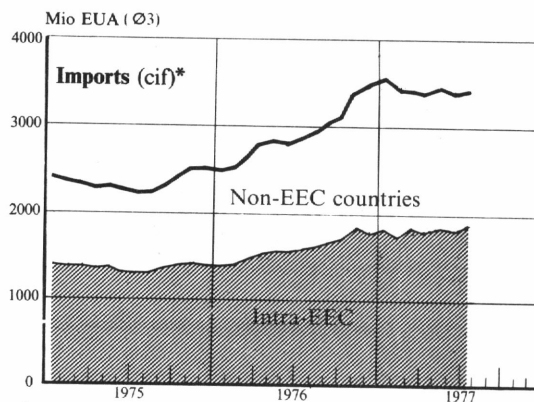
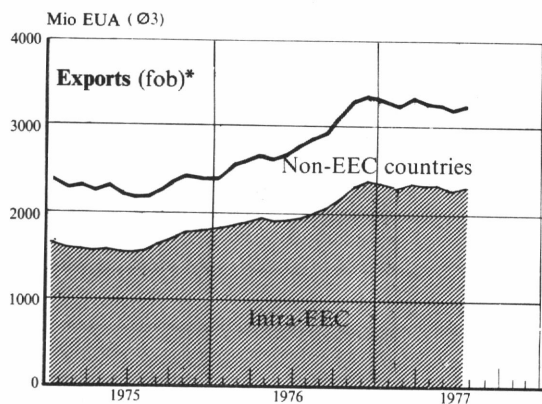
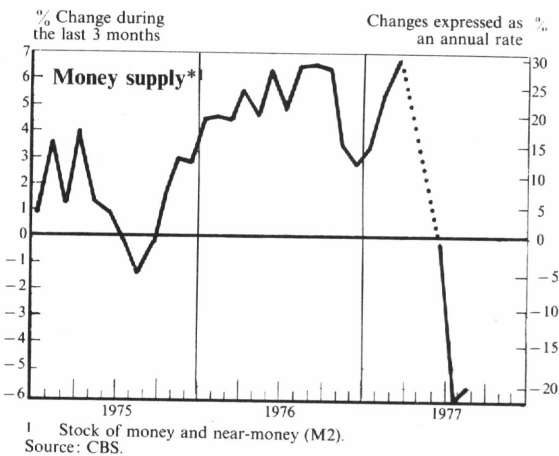
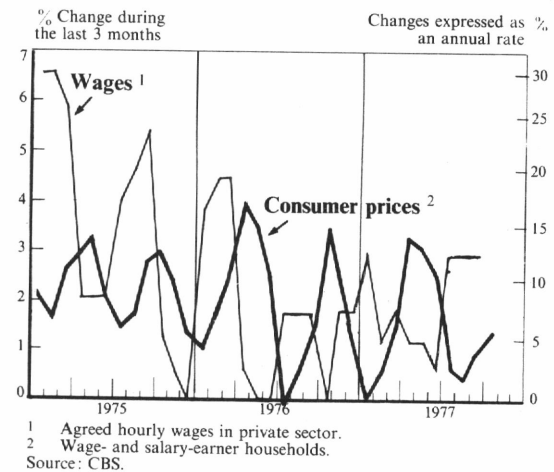
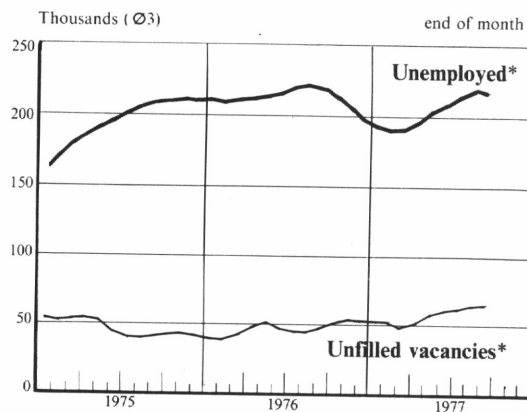
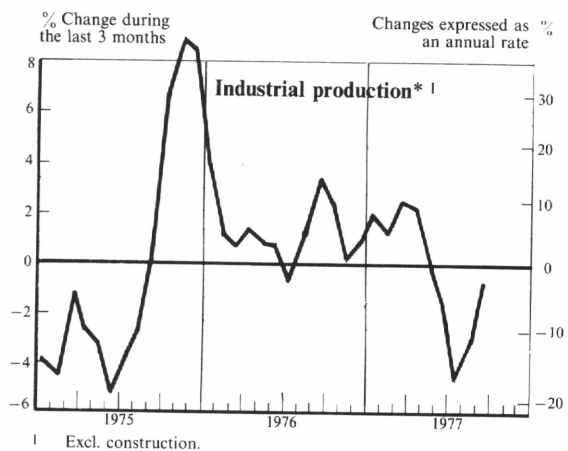
After a weakening trend in the first half of 1977 exports may show some recovery. Domestic demand on the other hand may lose momentum and output is likely to expand rather slowly over the coming months. The recent reduction of unemployment may prove only temporary and may be followed by a resumed increase. The price performance may continue to improve as a result of a continued rather modest rise in import prices as well as in domestic costs. The current external surplus may in 1978 turn out to be somewhat higher than in 1977, remaining, however, substantially below the record level of 1976.

With prospects for growth of output and activity in 1978 rather bleak in the Netherlands as well as elsewhere in the Community the general measures to stimulate activity decided this Autumn by the Dutch authorities seem appropriate. Given that the external surplus has already been considerably reduced and that the budget deficit in 1978 should remain compatible with medium term budgetary policy considerations there is now little scope for further action to boost demand on the part of the Dutch authorities. Indeed, a more pronounced strengthening of demand and activity would seem to be closely dependent upon developments in the Community as a whole.

1. Overall assessment and main policy issues

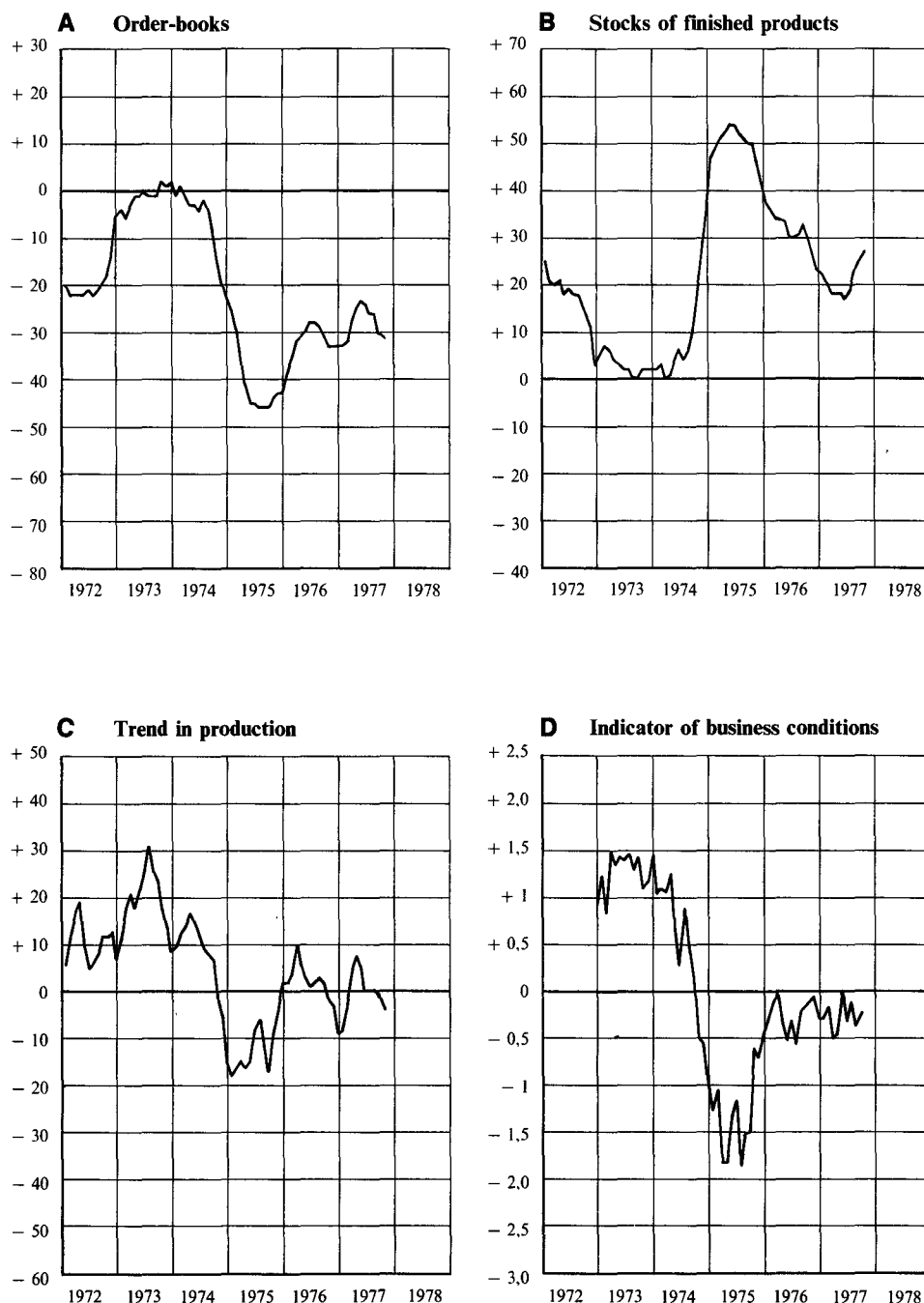
The Dutch economic scene in the summer and early autumn of 1977 presented rather contradictory features,

with some sectors of the economy — such as construction — remaining fairly buoyant — while others, notably certain parts of manufacturing industries catering for exports, were experiencing stagnating or falling trends.



* Seasonally adjusted figures.
Ø3: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



NOTE:

These charts are based on answers to questions on the EEC business survey, carried out in the Netherlands by the Centraal Bureau voor de Statistiek.

Graphs A, B and C show a three months moving average of the difference between "above normal" and "below normal" answers to the following questions:

- a) Do you consider that your present total order-book is, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- b) Do you consider that your present stocks of finished products are, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- c) Do you think that over the next three or four months your firm's seasonally adjusted production trend will be:
 - (1) up
 - (2) unchanged or
 - (3) down?

Graph D presents an indicator of industrial business conditions, based on a principal component analysis of the answers to four questions in the monthly business survey. These are the above three questions together with a question on the recent trend on production.

TABLE 1
Key indicators

Netherlands	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁵	1977 ⁶
Gross domestic product, volume	% change	5.0	- 1.2	4.6	2.4
of which: industry ¹		6.5	- 4	6	1
Gross domestic product in volume per person in employment	% change	4.8	- 0.5	4.9	2.3
Total employment (man/year) ²	% change	0.2	- 0.7	- 0.3	0.1
— Independent entrepreneurs		- 1.6	- 2.1	- 2.1	- 1.9
— Wage and salary earners in company sector		0.3	- 0.8	- 0.5	0.4
— General Government		2.0	1.9	2.9	0.6
Unemployment	as % of labour force	2.1	4.0	4.3	4.2
Compensation of employees per wage and salary earner	% change	14.0	13.4	10.8	8
Price index of private consumption ³	% change	7.9	10.3	9.2	7
Current account balance ³	Fl '000 million	2.8	4.4	6.6	2.7

¹ Excluding construction.

² Domestic concept.

³ National accounts concept.

⁴ Geometric mean of the change from 1969 to 1974; unemployment and current account balance: arithmetic mean over the five years.

⁵ Source: Nationale Rekeningen 1976, CBS.

⁶ Estimates of Commission's Departments.

Generally speaking, unemployment has remained on the same level as a year ago although with some fluctuations. The steady improvement of the trend in prices has continued in recent months. Given a fairly well sustained growth in domestic demand, a considerable weakening of exports of ships, levelling off of the growth of exports of energy products, a temporary decline in agricultural exports and perhaps some delayed effects on exports of other manufactured products of a loss of competitive strength, the Dutch external balance on goods and services deteriorated strongly in the first half-year. It may now be in the process of improving as some of the temporary factors cease to operate but a return to the 1976 level of the current external surplus is by no means expected.

Given the duration of negotiations concerning the formation of a government following general elections in May, the 1978 budget proposal was fully elaborated by the outgoing government assuming the continuation of present policies without new proposals or changes in priorities. However, as the macroeconomic projections underlying the budget estimates suggested a need for additional measures to sustain activity the government first accepted a budget deficit somewhat above the level suggested by medium-term budgetary policy considerations and, secondly, hinted that measures aimed at sustaining activity and containing the rise in unemployment might indeed be warranted. In recent months measures have in fact been implemented: public works,

subsidies for part-time work, and for energy saving, subsidies for legal minimum wages, delay to 1st April of the increase of VAT on natural gas, lowering of employees' contributions to social security. Thus, a total of some 2 000 million guilders (0.8 % of GDP) is estimated to be added to the budget deficit initially foreseen. An additional measure, foreseen by the government, consisting of a lowering of direct taxes by mid-1978 had not been actually proposed at the time of writing.

Following the agreement of May 1977 between the Nederlandsche Bank and the banking system to limit the expansion of credit (short-term credit to the private sector plus all longer term credits) in 1977 to 12.5 %, but also due to a fall in the monetary financing of the budget deficit as well as to a switch in the structure of deposits in favour of savings deposits, there has been a sharp reversal of trends in the monetary aggregates, with a fall in the wider definition money supply (M2). Moreover, in November, the minor snake currencies came under pressure again, due essentially to divergent movements of the exchange rates between the major currencies. Conversion of guilder nominated assets into other currencies seems to have taken place to a certain extent leading to further decline in domestic liquidity and a rise in short term interest rates. As of 10th November the Nederlandsche Bank increased the official discount rate 1 percentage point to 4.5 %. This measure led to a return to a calmer exchange market situation without intervention from the Nederlandsche Bank.

2. Recent developments

After a period of relative buoyancy in late 1976 and early 1977 the expansion of activity showed signs of slowing down in the second and third quarter.

Merchandise **exports** rose somewhat in volume terms in the third quarter. Moreover, with domestic demand losing pace imports rose only slowly in volume terms. Since, furthermore, terms of trade may have improved, the trade balance — and hence the current external account — improved somewhat in the third quarter compared with the first half of the year.

However, following a fairly brisk rise in the first part of 1977, **domestic demand** seems to have stagnated in recent months. Only dwelling construction seems to have expanded somewhat. Business investment in machinery and equipment probably remained on the level registered in the first half-year. Other categories of fixed investment including public investment, which had already fallen in the second quarter, may have declined further and the rate of inventory formation may also have contracted. Private consumption stagnated in the second quarter and may have been constant also in the summer months as the

rise in real disposable income has been very modest and the restrictions on bank lending may have exerted a moderating influence on consumer spending.

With only weak impacts from external and domestic demand the growth of output was probably brought to a halt. **Production** in manufacturing (seasonally adjusted) actually declined by 1% between the second and third quarter and in September stood some 2.5% below the level of a year ago. Unemployment, which had reached a peak in August, has fallen somewhat in recent months judging from the seasonally adjusted series which however due to possible changes in the pattern of seasonal fluctuations, may not at present fully reflect the underlying trend.

The upward movement of costs and prices lost further momentum in the third quarter, as the rise, in import prices slowed down and as certain food prices (potatoes, vegetables and fruit) showed a rather marked decline from their level of a year earlier. Between June and October the general index of consumer prices rose by 1.3% only, attaining a level 5.4% higher than a year earlier.

TABLE 2
Demand for and supply of goods and services

Netherlands	1975 ²	1976 ²			1977 ³			1978 ³
	At current prices Fl '000 million	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	120.80	2.7	9.2	12.1	3.5	7	11	2
Public consumption	38.37	4.3	8.5	13.1	0.5	7	7.5	2.5
Gross fixed asset formation	43.96	—	1.9	8.2	7.5	7	15	1.5
— Enterprises	24.49	—	3.1	7.6	4.2	10	5	16
— Dwellings	10.66	—	1.9	9.1	11.1	12.5	10	24
— General Government	8.81	—	2.9	8.8	5.6	—	6	8.5
Domestic final uses (excluding change in stocks)	203.13	—	2.0	8.8	11.0	3.8	7.0	11.0
Domestic final uses (including change in stocks)	201.63	—	4.4	8.7	13.5	4.2	6.9	11.4
Exports ¹	109.47	—	10.5	6.3	17.4	—	0.5	3.5
Imports ¹	102.17	—	10.9	6.5	18.1	—	2.5	4
Gross domestic product at market prices	208.93	—	4.4	8.6	13.3	—	2.4	6.6
		Contribution to percentage change in gross domestic product						
Domestic final uses (excluding change in stocks)	203.13	—	1.9	—	10.7	—	3.6	—
Change in stocks	— 1.50	—	2.3	—	2.4	—	0.5	—
Balance of exports and imports ¹	7.30	—	0.1	—	0.3	—	—	1.9

¹ Goods and services

² Source: Nationale Rekeningen 1976, CBS.

³ Estimates of Commission's Departments.

3. Outlook

On the basis of present trends and policies the growth of economic activity seems unlikely to accelerate in the near future.

The recovery of exports may continue, but with stagnation of natural gas exports, declining exports of transport equipment as well as a difficult competitive position for many other industries the overall increase in

merchandise exports in 1978 may hardly exceed the expected growth of some 5% in export markets (in volume terms). However, given present prospects for the expansion and composition of domestic demand, merchandise imports may rise less fast than exports entailing a decline in the trade deficit as well as an increase in the surplus on current external account.

The recent slowdown in the growth of domestic demand may indeed continue: building permits and housing starts

TABLE 3
Main economic indicators

Netherlands	Year	Jan.	Feb	Mar	Apr	May	June	July	Aug.	Sept	Oct.	Nov	Dec.
Industrial production* (1970 = 100)	1975	117	117	120	116	115	115	111	113	116	119	122	123
	1976	122	122	122	124	123	124	124	125	129	126	125	129
	1977	127	124	125	131	125	124	124	123	128	.	.	.
Unemployed* (1 000)	1975	164.5	171.8	181.4	191.0	193.9	197.8	203.4	205.9	207.6	207.9	209.0	209.4
	1976	203.3	209.8	207.5	208.1	210.4	215.8	219.2	224.7	218.4	210.7	203.9	198.6
	1977	192.3	191.1	193.4	196.5	201.5	208.4	213.4	219.8	216.3	208.5	.	.
Permits for residential construction* (1 000)	1975	10.7	8.5	9.3	10.0	9.4	10.7	8.2	12.7	7.4	10.0	8.9	8.1
	1976	9.8	10.1	8.3	10.0	9.4	10.1	9.0	12.6	10.5	10.5	8.8	12.3
	1977	9.7	10.7	7.6	12.4	10.8	5.3	8.8	8.4	7.7	.	.	.
Retail turnover* (1970 = 100)	1975	160.5	159.7	161.9	164.4	172.3	163.0	166.6	166.2	174.3	181.4	173.0	183.2
	1976	179.6	176.8	176.4	187.5	180.9	186.1	188.3	183.8	201.6	185.1	188.5	201.6
	1977	191.5	192.6	202.0	203.2	197.4	208.0	.	.	.	.	.	.
Consumer prices (1969 = 100)	1975	150.1	150.5	152.7	154.6	155.5	155.8	156.7	158.2	160.2	161.6	162.0	162.3
	1976	163.2	164.7	166.3	169.8	170.4	170.4	169.6	171.4	173.2	175.6	175.8	175.8
	1977	175.6	176.9	178.4	181.4	182.3	182.7	182.4	183.1	184.2	185.0	.	.
Visible imports* (million Ff)	1975	7 497	7 147	6 570	7 016	7 021	7 295	6 903	6 663	7 770	7 091	7 949	8 068
	1976	7 500	7 847	8 168	8 699	8 033	8 702	8 379	9 133	8 641	9 131	8 828	10 378
	1977	9 386	9 435	9 421	9 313	9 041	9 942	8 678	9 656	9 290	.	.	.
Visible exports* (million Ff)	1975	7 547	7 031	6 400	7 836	6 606	7 482	7 223	6 622	7 454	7 954	7 990	8 429
	1976	7 689	8 047	8 897	8 633	8 072	8 672	8 743	8 622	9 109	8 975	10 029	9 659
	1977	8 694	8 774	9 381	9 115	8 391	9 032	8 157	8 820	9 008	.	.	.
Balance of trade (million Ff)	1975	+ 50	- 116	- 170	+ 820	- 415	+ 187	+ 320	- 41	- 316	+ 863	+ 41	+ 361
	1976	+ 189	+ 200	+ 729	- 66	+ 39	- 30	+ 364	- 511	+ 468	- 156	+ 1 201	- 719
	1977	- 692	- 661	- 40	- 198	- 650	- 910	- 521	- 836	- 282	.	.	.
Official gold and foreign exchange reserves (million Ff)	1975	18 873	18 682	18 432	18 415	17 992	17 634	18 452	19 222	19 463	19 829	19 861	19 997
	1976	19 825	21 366	20 522	19 981	19 599	17 586	17 465	17 691	17 832	18 506	19 484	19 607
	1977	19 180	18 886	19 151	18 966	20 769	20 428	20 508	20 877	20 981	20 746	.	.
Money supply* (million Ff)	1975	69 244	71 590	71 423	72 037	72 443	72 074	71 366	71 412	71 954	72 585	73 558	74 061
	1976	75 746	77 005	77 290	80 026	80 634	82 124	83 841	85 994	87 633	89 179	89 110	90 074
	1977	92 100	94 013	96 155	98 898	96 539	94 685	92 924	91 230	.	.	.	.

Not available

* Seasonally adjusted

Source: EUROSTAT (except as otherwise indicated).

— Industrial production, excluding construction Source: CBS

— Unemployed end-of-month figures Source: CBS

— Number of dwellings authorized

— Value index of retail turnover

— Consumer prices wage-and salary-earner households Source: CBS

— Imports cif, exports fob value Source: CBS

— Balance of trade difference between figures for imports and exports

— Official gold and foreign exchange reserves gross reserves of gold and foreign exchange in the Nederlandsche Bank at end of month. Source: CBS

— Money supply Stock of money and near money at end of month. Since April 1977, new series Source: CBS

point to stagnant or perhaps declining housing construction over the coming months and business investment may remain flat following the rise in late 1976 and first half of 1977. Public investment on the other hand may rise a little if the new reflationary measures announced at the end of October are implemented as foreseen and other categories of public expenditure on goods and services may show a rather strong increase. Private consumption can be expected to expand somewhat probably less fast than in 1977 as the rise in real disposable income may remain modest even including the impact of additional budgetary measures taken in the Autumn.

Pending a marked upturn in demand and output in the Community as a whole, prospects are thus for a modest increase in the Dutch GDP and for a continued decline in employment. Given the outlook for a further increase in the active population the rise in the number of unemployed may thus resume in the course of 1978.

The price performance may on the other hand improve. Although some uncertainty still surrounds the outlook for energy prices import prices, or the assumption of a stable effective exchange rate for the guilder, would seem unlikely to rise more than 4-5%. Hourly wage cost being also likely to increase rather modestly, the rise in consumer prices for 1978 as a whole may be distinctly lower than the 7% estimated for 1977.

Pending a reversal of trends in the Community as a whole, be it through early action to boost activity or through a subsequent — and possibly delayed — strengthening of autonomous demand components, the Dutch economy is likely to go through a period with sustained employment problems and slow growth in the enterprise sector. In the short run, there is little further the Dutch authorities can do on their own behalf without running into external or internal constraints of a financial nature. However, a part at least of these constraints may be removed if a higher degree of coordination of policy measures is obtained within the Community and if the slowdown of the rise in prices and costs in the Netherlands is maintained and further pursued.

Major economic policy measures

May 1977:

- The scheme for assisting the recruitment of handicapped persons was extended and its scope widened to include employers taking on handicapped persons on a part-time basis.
- The scheme for encouraging the creation of temporary jobs was extended.
- The various measures to promote employment of young people were extended.

June:

- The wage and salary limits up to which scholarships and education allowances are available were raised.
- Under the Price Regulation, industry was authorized to pass on in higher prices a maximum of 0.7% of its wage and salary bill. The permitted increase in trading margins was raised from 3.5% to 5% by the distributive trades and from 3.5% to 5.2% for the services sector.
- In order to acquire the same pension rights as civil servants, political office-holders will henceforth have to complete forty years of service instead of twenty. Their pension fund contributions will be reduced.
- The scheme under which employers recruiting young persons who had been unemployed for a long time received a wage-cost subsidy of 30% was extended.
- A removal allowance was made available to unemployed persons taken on at some distance from their homes and to workers moving with their firms.

July:

- The minimum wage was raised by 3.5%.
- The insurance companies were authorized to increase car insurance premiums by 3%.
- Family allowances were increased by 3.5%.
- The ceiling applicable to the first annual allowance paid under the scheme for assisting the purchase or construction of dwellings was reduced from Fl 4 700 to Fl 4 000.

August:

- The wages and salaries of government employees were increased by 3.3% (subject to a minimum of Fl 55 per month). An across-the-board increase of 0.5% was also granted.

September:

- The central government draft budget for 1978 was presented. Taking into account the counter-cyclical items, the increase in expenditure compared with the draft budget for 1977 is 11.1% and compared with the probable outturn for 1977 12.8%; the increase in revenue, on the same comparison, is 16.2% and 10.6% respectively. Excluding the repayment of central government debt, the deficit, which was put at Fl 12 800 million in the draft budget for 1977 and which should in fact total Fl 7 700 million in 1977, is likely to rise to Fl 10 000 million in 1978. The tax ratio is likely to increase to 32.9%, compared with 32% in 1977.

October:

- The Government decided on a set of additional measures (total cost: Fl 2 000 million). These include:
 - measures to promote employment (between Fl 1 200 million and Fl 1 550 million, Fl 400 to 550 million of which will go to firms in difficulty and to energy saving, Fl 400 to 600 million for public works, Fl 300 million for temporary jobs, Fl 100 million additional subsidies for minimum wages);
 - the postponement, from 1 January to 1 April, of the increase in VAT on energy products (Fl 200 million);
 - the postponement of rent increases from 1 April to 1 July;
 - an additional Government contribution to retirement and survivors insurance (Fl 45 million);
 - a further reduction in employees' invalidity insurance contributions (Fl 270 million).

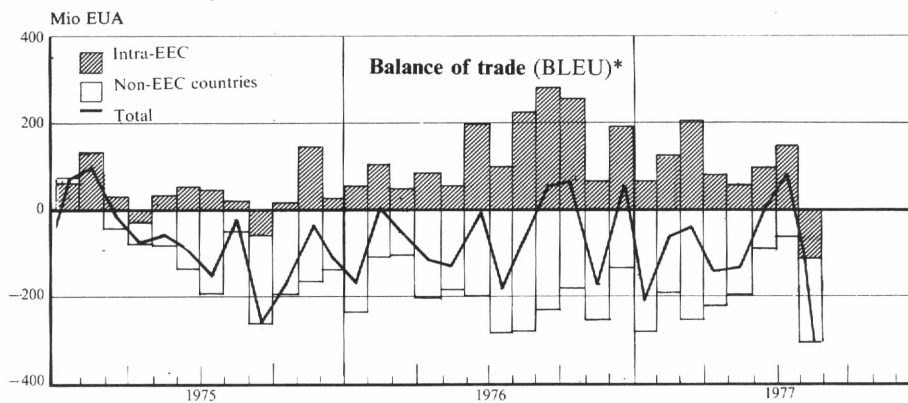
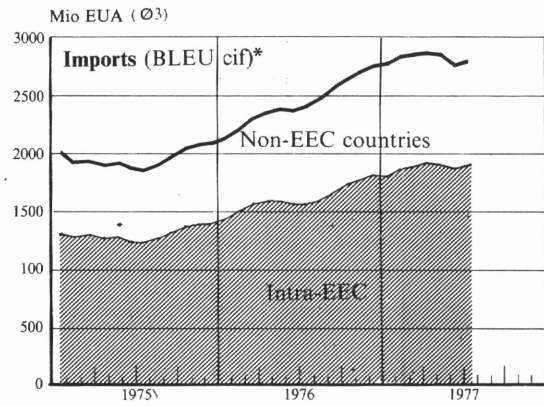
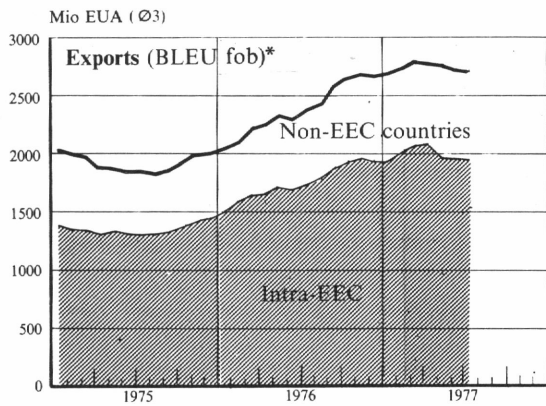
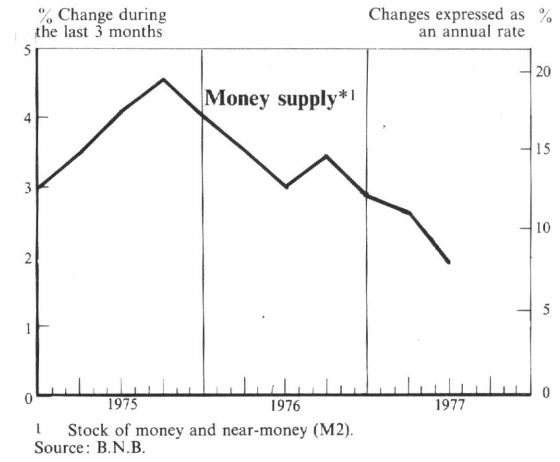
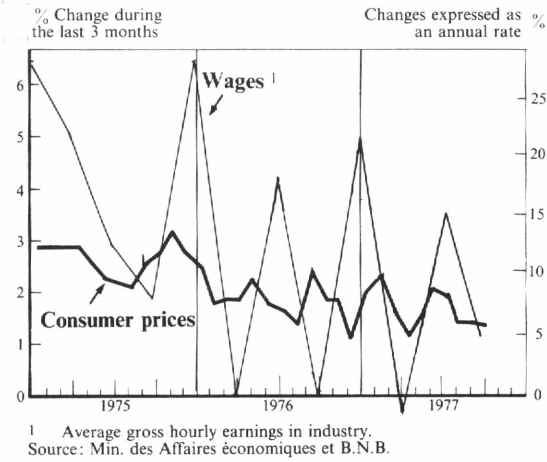
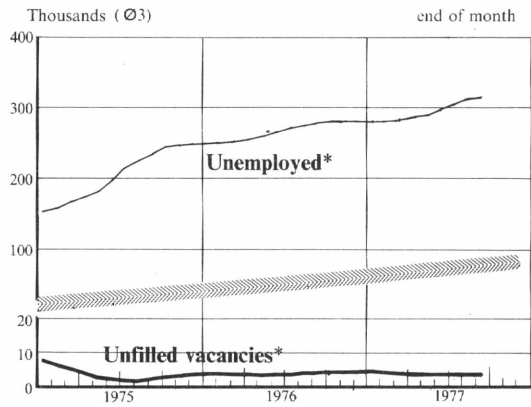
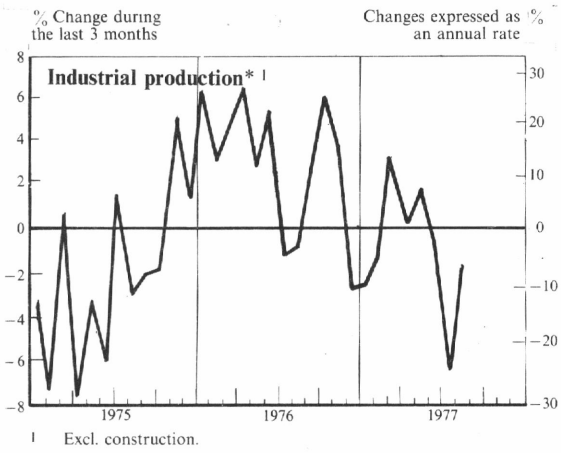
November:

- The Nederlandsche Bank increased the discount rate from 3½ to 4½%.

G. Belgo-Luxembourg Economic Union

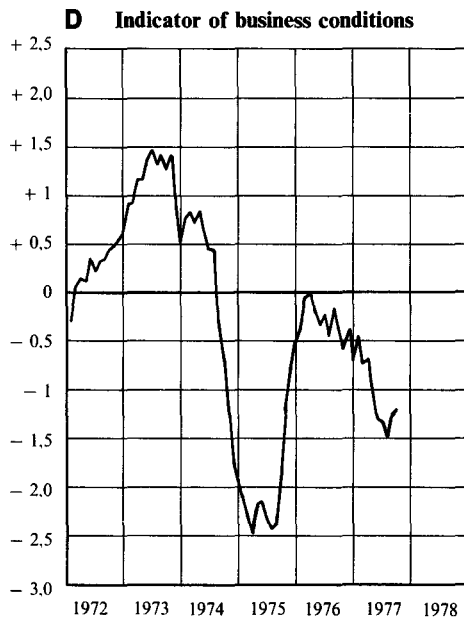
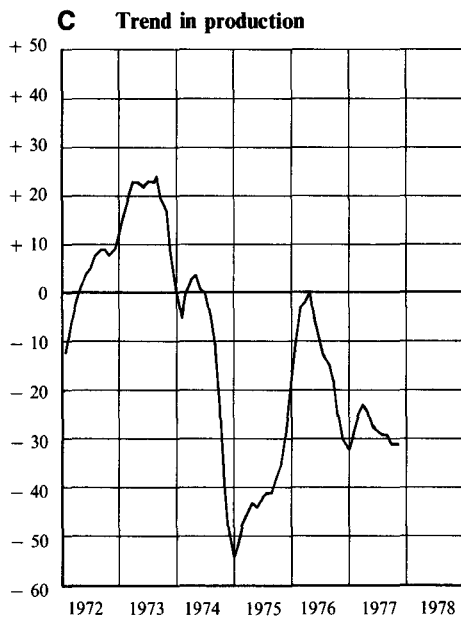
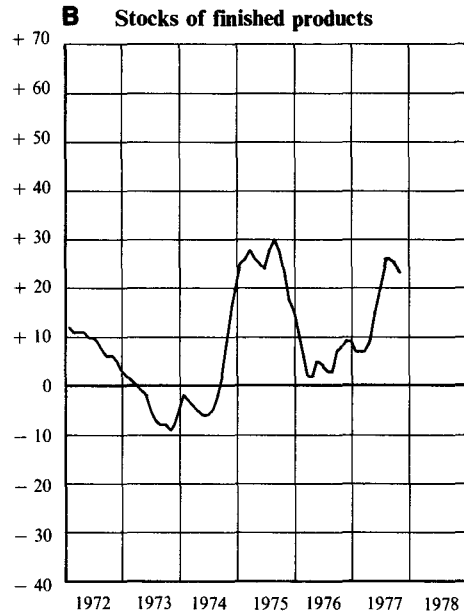
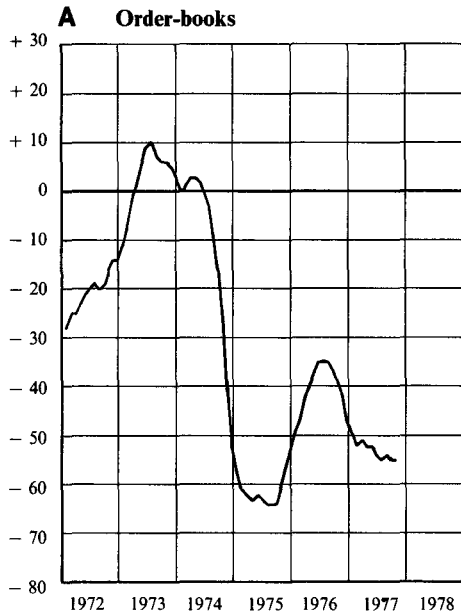
Belgium

Both internal and external demand in Belgium have been sluggish in 1977 and as a result growth has come to a halt and there may even have been a slight decline in output from the summer onwards. Unemployment has continued to



* Seasonally adjusted figures.
Ø3: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



NOTE:

These charts are based on answers to questions in the EEC business survey, carried out in Belgium by the National Bank. Graphs A, B and C show a three months moving average of the difference between "above normal" and "below normal" answers to the following questions:

- a) Do you consider that your present total order-book is, for the season :
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- b) Do you consider that your present stocks of finished products are, for the season :
 - (1) above normal
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- c) Do you think that over the next three or four months your firm's seasonally adjusted production trend will be :
 - (1) up
 - (2) unchanged or
 - (3) down?

Graph D presents an indicator of industrial business conditions, based on a principal component analysis of the answers to four questions in the monthly business survey. These are the above three questions together with a question on the recent trend on production.

increase, whilst the upward movement in prices and costs has slowed down further. The balance of payments has remained in deficit on current account.

No improvement in the business climate is to be expected in coming months. The further development of economic activity and employment will depend essentially on the scale and nature of efforts to restimulate growth being made in the Community as a whole. Since the central government budget deficit is already relatively high, the power of the Belgian authorities to stimulate demand and production is relatively limited. The implementation of an ambitious programme to reduce unemployment could well lead to some decline in the number of job-seekers in the coming year.

1. The overall situation and main policy issues

Growth has slowed down in the Community in 1977 and as a result Belgian exports (in volume) first stopped growing, and then actually fell back, a movement that has been reflected in a parallel development of industrial production. After the deterioration in 1976 the current account has shown a recovery although it still remains in deficit. The upward movement of prices and costs has continued to lose momentum. Both the number of persons wholly unemployed (seasonally adjusted) and on short-time working have risen sharply. The weakness of production and demand has curtailed the expansion of tax revenue while at the same time necessitating additional official expenditure, so that the budget deficit has widened, but general government requirements have been covered without recourse to inflationary borrowing. As a result, the situation on the money and capital markets has been relatively untroubled, at any rate until November.

Although what is already a very large central government borrowing requirement (6.5% of GDP in 1977) limits the authorities' room for manoeuvre to take additional action to stimulate production, the draft central government budget for 1978 includes a considerable expansion of public investment and a scheme for scaling down unemployment. The objective of the latter, described in more detail in the chronological list of economic policy measures given at the end of this section, is to reduce by about 75 000 (2 % of the labour force) the numbers of workers unemployed by assigning them either to training courses, temporary employment, or early retirement. As this plan can only be implemented by stages, its impact will probably be spread over the entire year, and it will, in any case, have only a limited effect on the number of unemployed women, who in fact account for two-thirds of the total number of unemployed persons of normal work ability.

TABLE I
Key indicators

Belgium	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁶	1977 ⁶
Gross domestic product, volume	% change	5.2	- 2.0	3.0	2.8
of which: industry ¹		6.7	- 6.4	6.0	3.0
Gross domestic product in volume per person in employment	% change	4.1	- 0.6	4.4	3.4
Total employment (number of persons) ²	% change	1.0	- 1.5	- 1.3	- 0.7
— Independent entrepreneurs		- 3.1	- 1.8	- 1.7	- 1.9
— Wage and salary earners in company sector		2.0	- 2.3	- 1.9	- 1.2
— General Government		2.4	3.0	2.2	2.6
Unemployment	as % of labour force	2.3	4.5	5.9	6.7
Compensation of employees per wage and salary earner	% change	11.1	15.6	11.9	9.7
Price index of private consumption ³	% change	6.3	12.1	8.9	7.1
Current account balance ³	FB '000 million	38.9	12.2	- 11.2	- 3.0

¹ Excluding construction

² Domestic concept

³ National accounts concept.

⁴ Geometric mean of the change from 1969 to 1974; unemployment and current account balance arithmetic mean over the five years

⁵ Source: Institut national de Statistique, National accounts

⁶ Estimates of Commission's Departments

The bank rate which had been held at 6% since the lowering in June was raised to 7% on 2nd December. The aim of this increase was exclusively to alleviate the pressure of which the Belgian franc has been the object during the last week of November; the measure does not indicate a change in priorities. However, it may at least temporarily put an end to the decline in short term rates during the Autumn. This decline has favoured a switch of deposits towards longer investment, facilitated the borrowing of the Treasury as well as the abolition, in October, of the last restrictions on mortgage loans. As a monetary and financial policy aimed at assisting investment remains a key objective of the authorities, the decline in interest rates should resume as soon as calmer conditions are restored in the foreign exchange market.

2. Recent developments

After marking time in the early months of 1977, BLEU exports (seasonally adjusted) have, in real terms, been declining since the spring. However, as imports have lost just as much momentum, the trade balance has staged a modest recovery, which was marked in the summer

months, when the terms of trade swung in favour of the Union.

The expansion of domestic demand has also lost vigour. The average volume of retail sales in June, July and August was lower than in the preceding three months and the same was true for purchases of motor cars for the period August to October (all comparisons using seasonally adjusted data). The number of industrial and commercial building licences issued fell short of the figure for the corresponding months of 1976. Residential construction held up until the summer, but then also slowed down. Only public investment has been maintained. Stocks of finished products have continued to build up in industry, usually to levels higher than those judged appropriate by managements.

With demand weakening in virtually all sectors, industrial production has declined and the financial position of companies has deteriorated. Employment has again contracted and unemployment has increased. At the end of October, the number of registered wholly unemployed (seasonally adjusted) was 321 700, 7.9% of the labour force, the number of unemployed of normal working

TABLE 2
Demand for and supply of goods and services

Belgium	1975 ²	1976			1977 ³			1978 ³
	At current prices FB '000 million	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	1 406.0	3.3	8.9	12.5	3.0	7.1	10.3	2.8
Public consumption	387.2	3.3	10.0	13.6	2.5	8.0	10.7	4.3
Gross fixed asset formation	504.7	- 0.1	8.8	8.7	0.8	7.5	8.4	0.9
— Enterprises	288.0	- 3.5	7.2	3.4	- 1.4	6.0	4.5	0
— Dwellings	140.0	5.0	11.0	16.6	2.0	9.5	11.7	- 1.0
— General Government	76.7	3.3	10.5	14.2	6.3	8.5	15.3	7.2
Domestic final uses (excluding change in stocks)	2 297.9	2.5	9.1	11.9	2.5	7.3	10.0	2.7
Domestic final uses (including change in stocks)	2 285.7	4.2	9.1	13.7	2.4	7.3	9.9	2.4
Exports ¹	1 061.8	8.0	6.4	14.9	4.6	4.2	9.0	5.0
Imports ¹	1 060.9	10.7	7.1	18.6	3.8	3.7	7.6	4.7
Gross domestic product at market prices	2 286.6	3.0	8.7	12.0	2.8	7.6	10.6	2.5
		Contribution to percentage change in gross domestic product						
Domestic final uses (excluding change in stocks)	2 297.9	2.8	—	12.0	2.5	—	10.1	2.6
Change in stocks	- 12.2	1.4	—	1.5	0	—	0	- 0.2
Balance of exports and imports ¹	12.2	- 1.2	—	- 1.6	0.3	—	0.5	0.1

¹ Goods and services.

² Source: Institut national de Statistique, National accounts.

³ Estimates of Commission's Departments

ability (not seasonally adjusted) reached 215 850 of which 64% are women. The number of workers on short-time has increased markedly over the level of a year previously.

Inflation had already been slowing down in the first half of the year, and has continued to do so, mainly because the prices of imports and those of food products in general have not been rising so fast. By the end of October, the consumer price index showed an increase of 6.5% on the October 1976 figure but was only 1.2% up on the July 1977 figure. For the first eight months of the year, the BLEU current account registered a deficit of 12 billion FB compared with 23 billion for the corresponding period of the previous year. The overall balance was more or less in equilibrium, whereas it was in deficit by 33 billion for the period January to August 1976 largely because of important speculative movements.

Nonetheless, because the public authorities have been borrowing less on the money markets and because the growth of lending to firms and households has slowed down, the rate of expansion of the money supply (M2) has again been lower. The exchange rate (trade-weighted) for the franc has stabilised since August.

3. Outlook

Given the present pattern of economic indicators, particularly the forward indicators, it is probable that the lack of vigour in the economy will persist for a few months, until measures to revive activity adopted or being prepared in Belgium and in certain other Community countries begin to take effect. **Export** orders on hand are still low and the relatively high level of stocks of finished products will probably force many firms to slow down output. All in all, **gross fixed capital formation** will tend to mark time, the only real stimulus to demand in this sector being that provided by public investment. None the less, the rate of expansion of private **consumers' expenditure** should remain fairly strong, this being partly a matter of increases in welfare payments. The measures announced in the autumn could well help to curb the spread of **unemployment** or even reduce it if exports recover in 1978.

Because of the impact of the recent change in VAT rates 1st January, and the outlook for the growth in costs, the increase in the **retail price** index is unlikely to be less than that registered in 1977. To the extent that the terms of trade remain unchanged there is likely to be little change in the current account of the **balance of payments** from the 1977 figures.

In 1978, those responsible for economic policy will face at one and the same time two main problems — the effects of slackening economic activity and the sharper impact of grave difficulties specific to particular sectors, especially the basic manufacturing industries and textiles. Here, the main need will probably be to establish a strategy to scale down unemployment and to reinforce the basis for the expansion of the economy without increasing the burdens on the budget.

A change of direction in industrial policy could be a key element in this strategy. Nonetheless, safeguarding the short-term position of Belgian industry will be necessary for its success.

Major economic policy measures

June 1977:

- The autonomous public credit institutions reduced their interest rates on investment credit from 11.15% to 10.90%.
- The financial intermediaries reduced their interest rates on deposits with terms of one year or more by 0.25%.
- The Government approved a draft law on tax concessions designed to encourage business investment, notably by leaving it to enterprises to choose the depreciation method for new investment, permitting a 110% depreciation for additional investment undertaken between 1 March and 31 December 1977, and granting a five-year tax exemption on income (up to a maximum of 5%) on new capital injected during this same period.

July:

- As from 5 July, the financial intermediaries reduced their interest rates on short-term deposits by 0.25%.
- The private savings banks reduced the interest rate on mortgage loans by between 0.25% and 0.50%, bringing the base rate down to 11%.
- The banks reduced their rates for discount credit (average rate: 7.25%); the rate for overdrafts remained unchanged at 9%.
- Under the agreement concluded between the Government and the Banque Nationale on 15 July, the ceiling on direct advances from the Banque Nationale to the Government was raised from FB 21 300 million to FB 38 300 million (FB 37 000 million instead of FB 20 600 million under the heading of Belgian public securities and the remainder under the heading of Luxembourg public securities).

August:

- As from 12 August, the financial institutions reduced the interest rates on medium-term certificates of two years or more by 0.25%, bringing the yield on five year certificates to 9%.
- The Government adopted the basic features of its budget for 1978. Total current expenditure was fixed at FB 956 100 million, 11.0% up on the 1977 adjusted budget and 14.3% on the original budget. Current revenue was estimated at FB 932 200 million, leaving a current deficit of FB 23 900 million. On capital account, expenditure was estimated at FB 134 400 million and revenue at FB 10 900 million. The overall deficit would amount to FB 147 400 million. The budget estimates were based on a GNP growth rate of 3% in volume terms and 11.2% in value terms. Following the July adjustment, the budget for current transactions in 1977, which had shown a slight surplus when originally tabled, will close with an estimated deficit of FB 60 000 million.
- When drawing up the 1978 budget, the Government adopted the following tax measures: reinforcement of the fight against tax evasion at frontiers and of penal sanctions for blatant cases of tax evasion, no deduction of excessive professional charges; an increase in succession duties, moderated by an increase in the initial allowances (expected to yield FB 1 100 million in 1978); replacement of the 14% and 18% VAT rates by a single 16% rate as from 1 January (estimated additional yield of FB 8 200 million); higher taxes on tobacco products (the proceeds to go to sickness insurance funds); application of increased VAT rates (decided in February but postponed); collection of the additional communal tax at the same time as personal income tax (additional revenue of FB 20 000 million, but only in 1978); indexation of certain tax scales (FB 3 500 million); adjustment of scales for taxable incomes above FB 500 000 (+ FB 1 700 million); full deductibility of VAT on job-creating investment (revenue loss of FB 3 000 million in 1978); temporary tax reliefs to encourage investment (revenue loss of FB 5 400 million). Taken together, the new taxes would bring in an additional FB 31 600 million.
- The Minister for Employment and Labour prepared a programme for reducing unemployment, consisting of the reinforcement of decisions taken earlier and of new measures: increase in the number of trainees in firms (from 12 000 to 27 000 in 1978) through the obligation to take on one trainee for every 50 persons employed and to pay them 90% of the normal

TABLE 3
Main economic indicators

Belgium	Year	Jan.	Feb.	Mar	Apr.	May	June	July	Aug.	Sept	Oct	Nov.	Dec.
Industrial production* (1970 = 100)	1975	113.7	112.4	113.5	105.0	108.9	106.7	106.6	105.9	104.7	104.8	111.3	106.1
	1976	111.6	114.7	111.7	119.0	117.7	117.4	118.1	116.8	119.5	124.0	120.2	116.3
	1977	121.7	119.8	119.9	122.6	122.1	120.2	114.1	119.1	115.7	:	:	
Unemployed* (1 000)	1975	155.6	163.9	171.3	179.2	184.2	191.0	220.5	231.6	240.9	244.7	249.1	251.0
	1976	251.6	252.1	254.5	257.7	263.0	264.8	276.2	279.4	277.9	281.8	284.6	278.8
	1977	283.5	281.6	286.0	289.3	295.9	293.5	306.8	311.4	315.0	321.7	.	
Construction. Permits for residential construction*	1975	5 975	6 083	5 690	6 104	4 852	6 297	5 361	6 080	6 925	6 299	7 183	8 067
	1976	7 909	8 201	8 116	7 159	7 895	8 169	6 598	8 426	7 985	8 205	7 523	9 636
	1977	5 923	5 882	6 657	7 392	5 928	7 226				:		
Private consumption: Retail turnover* (1970 = 100)	1975	130.4	126.5	126.2	132.7	128.5	125.1	126.9	128.5	129.3	133.7	127.6	132.3
	1976	133.6	132.3	131.1	136.8	129.0	132.4	135.3	132.7	135.2	131.2	132.7	136.1
	1977	137.3	136.9	137.6	141.0	132.7	135.3	130.7	135.5	:	:	:	
Consumer prices (1970 = 100)	1975	142.5	144.1	145.1	146.7	147.9	148.5	149.9	151.0	152.3	154.1	155.7	156.5
	1976	158.0	158.5	159.5	161.0	162.2	162.4	163.7	164.4	166.5	166.9	167.5	168.4
	1977	170.1	171.4	171.3	172.2	173.9	175.0	175.5	176.1	177.3	177.7	178.4	
Visible imports* (FB '000 million)	1975	89.73	90.33	89.82	89.89	84.31	91.43	94.59	88.10	99.33	99.98	102.80	100.24
	1976	104.19	103.04	107.25	112.40	107.01	115.42	113.32	115.24	121.53	113.66	119.80	114.01
	1977	120.82	120.10	124.27	117.60	114.30	118.17	107.32	118.57	.	.	.	
Visible exports* (FB '000 million)	1975	91.46	90.96	85.35	83.40	80.86	85.12	85.19	84.86	83.39	88.00	98.14	91.00
	1976	91.31	99.59	98.53	98.74	97.88	108.67	97.18	112.01	113.48	113.37	102.78	111.24
	1977	106.46	110.18	118.44	106.68	105.34	115.07	103.35	111.35	:	:	.	
Balance of trade (FB '000 million)	1975	+ 1.73	+ 0.63	- 4.47	- 6.49	- 3.45	- 6.31	- 9.40	- 3.24	- 15.93	- 11.97	- 4.65	- 9.24
	1976	- 12.89	- 3.45	- 8.72	- 13.66	- 9.13	- 6.75	- 16.14	- 3.22	- 8.05	- 0.30	- 17.02	- 2.77
	1977	- 14.36	- 9.93	- 5.83	- 10.93	- 8.97	- 3.10	- 3.97	- 7.22	:	:	.	
Official gold and foreign exchange reserves (FB '000 million)	1975	217.4	223.1	224.9	226.6	230.9	234.1	236.2	238.2	234.6	235.9	234.3	235.3
	1976	223.0	218.4	216.0	208.2	207.8	207.2	200.5	199.4	185.7	185.5	192.3	205.1
	1977	208.3	211.9	215.1	217.7	220.9	221.9	224.5	224.7	225.1	(227.5)		
Money supply* (FB '000 million)	1975			1 456.7			1 515.7			1 584.9			1 650.0
	1976			1 708.5			1 759.9			1 819.9			1 871.5
	1977			1 920.9			1 957.4						

Not available

* Seasonally adjusted

Source: EUROSTAT (except as otherwise indicated)

- Industrial production, excluding construction
- Unemployed end-of-month figures
- Construction number of residential buildings authorized
- Private consumption volume index of retail turnover
- Consumer prices all households
- BLEU Imports cif, exports fob value Source: INS
- BLEU Balance of trade difference between figures for imports and exports
- Official gold and foreign exchange reserves gross reserves of gold and foreign exchange held by the monetary authorities, position at end of month Source: BNB
- Money supply Stock of money and near-money at end of quarter Source: BNB

wage; increase in the number of jobless given work by the public authorities (from 20 000 to 25 000 in 1978); increased recourse to the statutory early retirement scheme and extension of the statutory scheme to small and medium-sized enterprises (34 000 workers); voluntary transfer of 18 000 older unemployed persons to the early retirement scheme; creation, in the public service, of a temporary work force with a special status, enabling 24 000 jobless to be employed on publicly or socially useful work, upgrading of manual work (1 500 persons). These measures are designed to reduce the average number of wholly unemployed and those on short time from 295 000 in 1977 to 220 000 in 1978. The extra

expenditure required for this programme is FB 23 700 million, FB 9 200 million of which is accounted for by the temporary special work force.

— The autonomous public credit institutions decided to reduce interest rates on investment credit by 0.20% to 10.70%.

September:

— Public transport charges were increased by between 10% and 20%.

— The financial intermediaries reduced their interest rates for ordinary savings-book deposits from 4.25% to 4.0%, but this was offset by a 0.25%

increase in the loyalty bonus (from 1.25% to 1.50% at the CGER). The interest rates on medium-term certificates and time deposit accounts were reduced by between 0.25% and 0.50%, depending on the term. At the same time, the rates for mortgage and investment loans were reduced by 0.50% to 10.50%.

— A nine-year loan, carrying a coupon of 9.50% and issued at 100.25%, yielded the Treasury FB 61 500 million. The subscription list was opened and closed on the same day

— The Government and representatives of government employees concluded an agreement under which civil servants are to receive an end-of-year bonus of FB 6 000 (increased from FB 4 250) plus 2.5% of their annual salary. The total cost was estimated at FB 1 700 million. The Government also undertook to recruit immediately 2 400 new civil servants (over and above the measures under the anti-unemployment programme).

— The Caisse Générale d'Épargne et de Retraite reduced its base rates for mortgage loans from 10.50 to 10%.

October:

— As from 1 October, the autonomous public credit institutions reduced their interest rates for loans to industry, the professions and farming from 10.70% to 10.25%.

— The restrictions on mortgage lending ratios were abolished.

— As from 15 October, the price of cigarettes was increased by FB 5 through the introduction of a "special health tax" the revenue from which will be paid to the sickness and invalidity insurance funds.

— The Minister for Agriculture and Small Business presented a plan for the development of and employment in small and medium-sized enterprises; the aim is to simplify administrative formalities, to encourage the employment of additional staff by allowing exemption from employers' social security contributions for one year, to reduce the contributions of particularly labour-intensive firms, to improve access to credit and to help young people set up on their own by granting special assistance.

— On 8 October, the banks decided to reduce the interest rate on overdrafts by 0.25%, from 8.75% to 8.50% per annum.

— The Minister responsible decided to change the way in which the consumer price index was calculated: henceforth, the sub-indices for fruit, potatoes and other vegetables included in the overall index would be three month moving averages.

— The Minister for Economic Affairs presented a plan for safeguarding the textile industry. The plan would cost the Government FB 700 million and would make it possible to grant the industry non-interest bearing credit lines worth some FB 3 000 million.

December:

— The bank rate is raised from 6 to 7%.

Luxembourg

In Luxembourg, export demand has remained weak and domestic demand has expanded more slowly than was expected. No substantial change in the economic climate is foreseen for coming months, so that the employment situation is likely to deteriorate further.

Because the steel industry has such an important place in the Luxembourg economy, the task of industrial diversification and manpower retraining is a very heavy one. Efforts to adapt to changing circumstances must be pressed forward within the consultation framework established by the Luxembourg Tripartite Conference.

1. The overall situation and main policy issues

Economic activity in Luxembourg showed signs of recovery — sporadic and varying in intensity — between the third quarter of 1976 and the second quarter of 1977, a period of a little more than a year and a half. However, in the third quarter of 1977, the movement seems to have subsided in most industries.

This means that more serious employment problems and further difficulties with regard to company profitability could well occur in the coming months.

Because the employment cycle always tends to lag behind the production cycle, unemployment is only now increasing and the avoidance of large-scale redundancies by passive measures such as not replacing retiring workers does not dispose of the problem facing young people, whose qualifications and expectations all too seldom match available vacancies.

From the beginning of the crisis the authorities have intervened to safeguard employment by introducing special work schemes and share time working and by accelerating public works. As set out in the programme resulting from the Tripartite Conference of representatives of management, unions and the government held last April, the authorities have established two distinct objectives, these being to establish the conditions

under which the economy can be got under way again (by encouraging investment, exports, and the work of the self-employed) and to soften the impact of the crisis for those hit hardest by it (by encouraging work-sharing and paying the allowances needed to maintain the purchasing power of the households whose members are out of work or on short time).

These were the two objectives underlying the draft central government budget for 1978, which is designed to leave a borrowing requirement of about the same size as the estimated figure for 1977 (nearly Flux 2 000 million).

2. Recent developments

The main features of the economic situation in Luxembourg are the persisting weakness of export demand and a rate of increase in domestic demand which will probably be lower than was expected.

For the first ten months of the year, incoming export orders for Luxembourg's main exporting industry, the steel industry, were 5.3% below the corresponding period for 1976, although the pattern varied very widely according to the origin of the orders, since orders from the other ECSC countries fell by 16.3% while orders from non-member countries rose by 39.3%. Since order-books in other industries have also been shrinking, exports

TABLE 1
Key indicators

Luxembourg	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ^{5 6}	1977 ⁶
Gross domestic product, volume	% change	4.1	- 8.4	2.7	1
of which: industry ¹	:	:	- 18	6.3	0.5
Gross domestic product in volume per person in employment	% change	1.7	- 8.6	4.3	2.1
Total employment (number of persons) ²	% change	2.4	0.2	- 1.5	- 1.1
— Independent entrepreneurs		- 3.6	- 2.6	- 1.8	- 2.3
— Wage and salary earners in company sector		3.9	0.4	- 1.4	- 0.9
— General Government		2.2	2.9	0.7	1.4
Unemployment	as % of labour force	0	0.2	0.4	0.5
Compensation of employees per wage and salary earner	% change	12.9	12.5	10	8.5
Price index of private consumption ³	% change	6	10.7	9.8	6.8

¹ Excluding construction

² Domestic concept

³ National accounts concept.

⁴ Geometric mean of the change from 1969 to 1974, unemployment and current account balance: arithmetic mean over the five years

⁵ Source: Statec

⁶ Estimates of Commission's Departments

: No data available

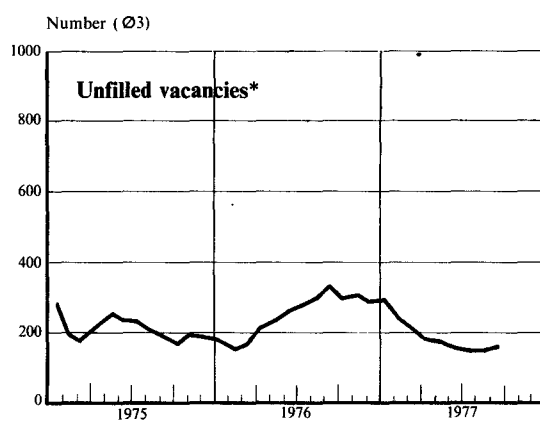
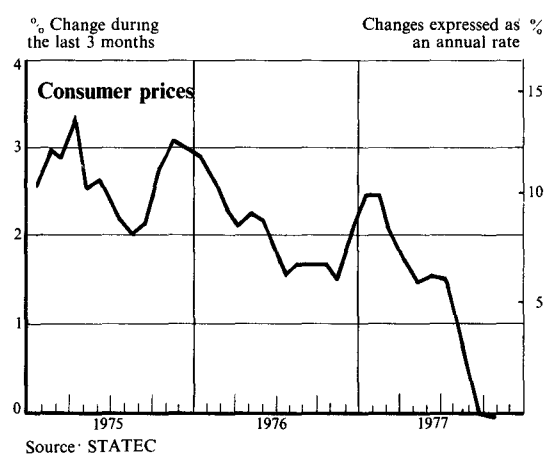
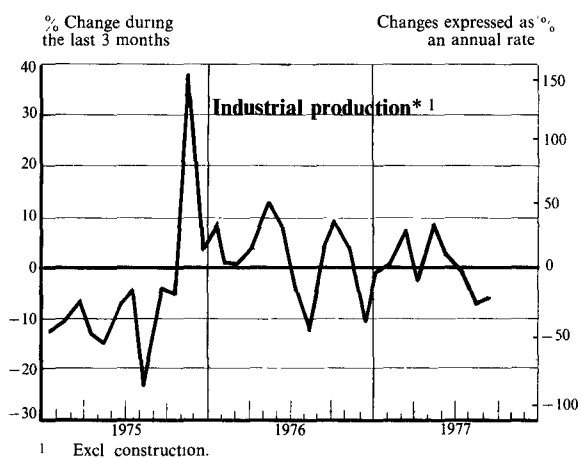
TABLE 2
Demand for and supply of goods and services

Luxembourg	1975 ²	1976 ²			1977 ³			1978 ³
	At current prices mio Flux	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	48 390	3	9.8	13.1	2.5	6.8	9.5	2
Public consumption	12 099	2	10.2	12.4	1.8	9.5	11.5	1.7
Gross fixed asset formation	23 545	- 4.6	7.4	2.4	3.1	8	11.8	0
— Enterprises	11 880	- 10.1	6.6	- 4.2	4.2	8.9	13.4	- 2
— Dwellings	6 120	- 10	8	- 2.8	0	7	7	0
— General Government	6 166	10.7	8	19.6	4	7.3	11.6	3
Domestic final uses (excluding change in stocks)	84 034	0.7	9.2	10	2.6	7.5	10.4	1.4
Domestic final uses (including change in stocks)	85 944	0.2	9.1	9.3	1.8	7.4	9.5	1.1
Exports ¹	65 130	3.1	- 0.7	2.4	1.2	0.4	1.2	2.2
Imports ¹	69 483	0	7.5	7.6	2.2	2.2	4.5	1.8
Gross domestic product at market prices	81 591	2.7	2.5	5.3	1.0	6.5	7.6	1.3
		Contribution to percentage change in gross domestic product						
Domestic final uses (excluding change in stocks)	84 034	0.7	—	10.3	2.8	—	11	1.6
Change in stocks	1 910	- 0.5	—	- 0.5	- 0.8	—	- 0.8	- 0.3
Balance of exports and imports ¹	- 4 353	2.5	—	- 4.5	- 1	—	- 2.6	0

¹ Goods and services

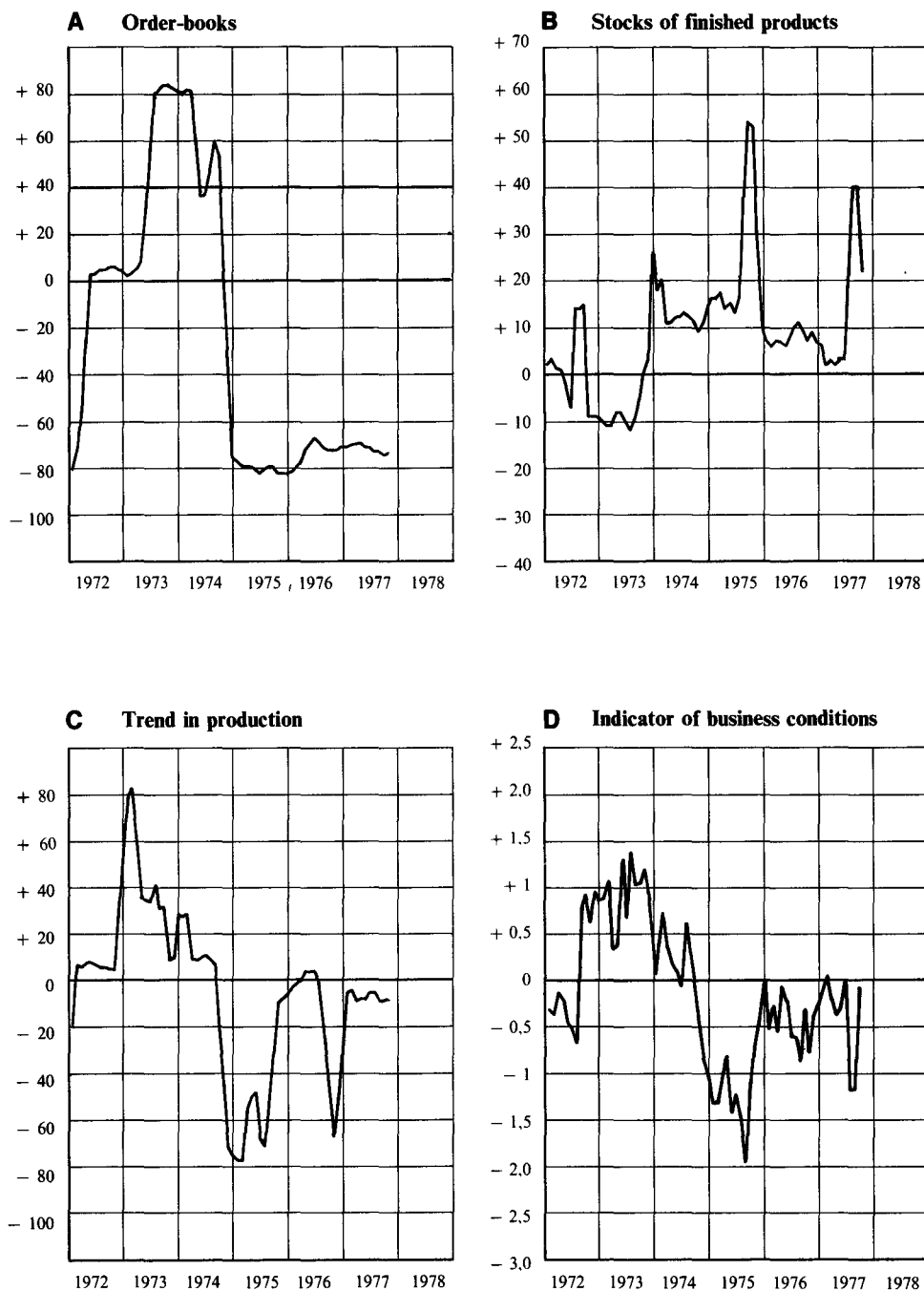
² Source: Statec.

³ Estimates of Commission's Departments



* Seasonally adjusted figures.
 Ø3: three month moving average.
 Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



NOTE:

These charts are based on answers to questions in the EEC business survey, carried out in Grand Duchy of Luxembourg by STATEC. Graphs A, B and C show a three months moving average of the difference between "above normal" and "below normal" answers to the following questions:

- a) Do you consider that your present total order-book is, for the season:
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- b) Do you consider that your present stocks of finished products are, for the season :
 - (1) above normal
 - (2) normal or
 - (3) below normal?
- c) Do you think that over the next three or four months your firm's seasonally adjusted production trend will be:
 - (1) up
 - (2) unchanged or
 - (3) down?

Graph D presents an indicator of industrial business conditions, based on a principal component analysis of the answers to four questions in the monthly business survey. These are the above three questions together with a question on the recent trend on production.

could well be marking time, in value as well as in volume. With domestic demand holding fairly firm, imports have probably continued to increase, though not as fast as in the past. As a result, the current account could well have deteriorated once again.

As for domestic demand, it now appears to have been expanding rather more slowly than was expected some months ago: while private consumption has continued to grow, mainly because of purchases of motor-cars and perhaps of other durables in general (thanks to the increase in consumer credit) gross fixed asset formation has probably not been as vigorous as could have been expected. This is partly because some of the investments announced in the steel industry have been postponed. Moreover, while the recovery of orders to civil engineering firms was confirmed in the autumn, the upward movement in residential construction orders has apparently not persisted.

For the first nine months of the year, the industrial production index prepared by the Luxembourg statistical office (Statec), shows virtually no change on the previous year (0.3%). Within this figure, an increase of 3.6% for the non-steel sector is almost completely offset by a contraction of 2.9% in steel output. Average production in the last three months shows a decline of 6.8% for steel production and 2.4% for total production. The building and construction production index for the first nine months of the year shows a decline of 2.6% when compared with the figure for the corresponding months of 1976.

In addition industrial employment has continued to decline. At the end of September, the decline in the

number of workers employed in industry was 2.1% in one year. The index for the number of paid workers shows that numbers had declined between 1976 and 1977 (8 months) by 3.5% in steel, but had remained stable in the other industries. By October, the number of job-seekers had almost doubled in comparison with October 1976.

The upward movement in consumer prices has continued to slow down. In November, the year-on-year increase rate was down to 5.3% the lowest percentage since July 1973. The lowest increase was for food and the highest for beverages and tobacco.

3. Outlook

None of the available indicators holds out hope of an improvement in the economic situation in coming months.

Sales to other EEC countries are likely to be inhibited by the heavy stocks of finished products already built up in other countries, stocks which may hold back their own production. Exports to non-member countries are unlikely to continue growing at the present pace. Although the services balance could well go on developing favourably, the possibility of current account deficit cannot be ruled out.

As for domestic demand, private and public consumption and gross fixed asset formation must be expected to expand rather more slowly than in 1977. While the steel managements are apparently determined to press forward with rationalization investment, other classes of investment, except perhaps in civil engineering, will remain depressed.

TABLE 3
Main economic indicators

Luxembourg	Year	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec.
Industrial production* (1970 = 100)	1975	106.2	101.9	101.5	93.3	87.5	94.7	89.5	67.1	91.4	85.7	92.8	94.1
	1976	94.1	93.7	94.8	97.4	105.9	102.3	94.2	93.7	107.0	103.3	96.9	95.8
	1977	102.7	97.2	103.0	100.1	105.6	105.7	99.9	98.1	98.8	.	.	.
Unfilled vacancies*	1975	246	165	181	240	244	267	185	248	201	153	163	263
	1976	152	143	174	192	271	210	258	353	309	334	247	333
	1977	255	260	180	191	178	159	138	150	160	170	.	.
Consumer prices (1970 = 100)	1975	134.6	136.6	137.5	139.2	140.1	141.1	142.3	142.9	144.0	146.2	147.4	148.3
	1976	150.5	151.3	151.6	153.8	154.7	154.9	156.1	157.3	157.5	158.7	159.7	160.8
	1977	162.4	163.5	164.2	165.2	165.8	166.7	167.4	167.0	166.6	167.3	168.1	.

Not available

* Seasonally adjusted

Source EUROSTAT (except as otherwise indicated).

Industrial production, excluding construction

-- Unfilled vacancies end-of-month figures

-- Consumer prices all households

All in all, with stock-building on a smaller scale than previously estimated, the gross domestic product in real terms may be expected to increase by about 1 ½ % in 1978.

It is likely that the tendency for consumer prices to increase less rapidly will persist. The growth rate between 1977 and 1978 should be of the order of 5 %.

Taking the overall picture, the problems facing the Luxembourg authorities, mainly the social and economic implications of the difficulties besetting the steel industry, will tend to grow more serious in the coming year, so that a proper industrial diversification and manpower retraining policy will be needed even more than before. This policy should be pursued in line with the principles established by the Luxembourg Tripartite Conference and implemented as part of the dialogue between unions and management to which the Conference has given a kind of institutional framework.

Major economic policy measures

April 1977:

— A tripartite conference (government, employers, trade unions) was held to examine the medium-term economic trend, with the emphasis on employment. The plan of action which emerged from the conference and which was published in July combines measures to stimulate economic growth (establishment of a national credit and investment company, investment aid, aid to the small business sector, development of industrial estates, increase in the funds of the Del Credere Office, public works, housing policy, measures to combat non-reported work), with action to influence the labour market, graduated according to the seriousness of unemployment (improving the transparency of the market, banning overtime, providing vocational training and guidance, introducing a special recruitment scheme for government departments, extending the system of short-time working, granting waiting allowances). Where necessary, contractual measures may be taken to reduce production costs in the interests of protecting employment; the rules on the operation of the sliding wage scale may be adjusted temporarily and arrangements made to freeze prices and profit margins.

June:

— The grant on the birth of a child was increased from Flux 6 000 to Flux 9 000.

July:

— Under a new set of rules, holding companies must have a minimum capital of Flux 1 million to qualify for exemption from corporation tax, surtax, supplementary tax and coupon tax. A special department was set

up to supervise holding companies. Companies infringing the law on holding companies will have their status revoked.

— The government was authorized to issue one or more loans amounting in total to Flux 1 000 million, provided for in the 1977 budget.

— Investment is to be encouraged through a temporary tax concession in the form of a corporation tax rebate.

— Various measures were taken concerning foreign workers, in particular:

— abolition of the arrangements enabling work permits to be withdrawn for reasons pertaining to the labour market situation;

— liberalization of the work permit system;

— establishment of a National Immigration Council responsible for studying all problems relating to immigration.

August:

— Following the work of the above-mentioned tripartite conference, a national credit and investment company was set up by law on 2 August. The purpose of this company which is a public institution ranking as a banking and savings institution, is to grant medium- and long-term loans with a view to promoting the setting-up, extension, conversion, reorganization and rationalization of enterprises, provided that the operation is of general economic benefit. It may also lodge funds with approved credit institutions to provide cover for equipment loans to small and medium-sized enterprises. In addition, it may arrange export credit. With regard to holdings, it may, with the authorization of the responsible ministers, either contribute part of the capital of companies which are to be set up, or purchase and manage transferable securities.

— By amendment of the Belgian-French-Luxembourg convention on the operation of the Luxembourg railways, the capital of the Luxembourg railways was increased from Flux 800 million to Flux 1 600 million. France did not participate in this increase, so that its share was reduced from 24.5 % to 12.25 %, while Luxembourg's share was increased by the same proportion.

— Non reported work by wage and salary earners and self-employed persons was prohibited and made subject to penal sanctions.

September:

— The draft central government budget for 1978 was presented to Parliament. Its objective is to encourage full employment, in particular by strengthening the productive potential of enterprises and increasing public investment, and to lessen the effects of the crisis on the least-favoured groups of society. The draft budget is based on a medium-term growth rate of 2.75 %. If special factors — both cyclical and fortuitous — are taken into account, expenditure is to amount to Flux 39 363 million, an increase of 7.4 % on the 1977 final budget, and revenue to Flux 39 111 million, an increase of 8.9 %. The deficit should be Flux 252 million compared with Flux 712 million in the final 1977 budget.

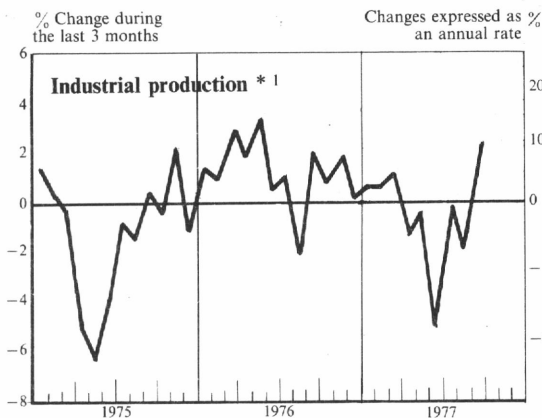
October:

— The central government issued a Flux 1 000 million twelve-year loan carrying an interest rate of 7.50 % per annum.

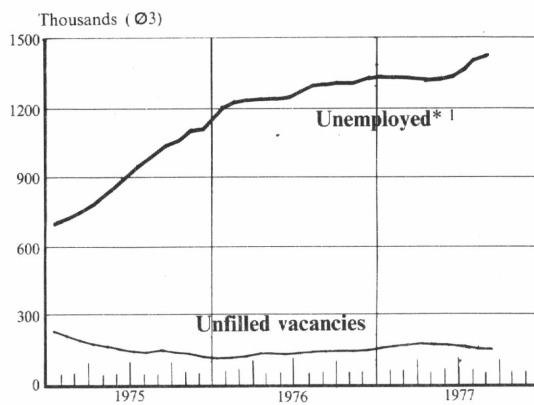
H. United Kingdom

Although confidence in the financial situation of the United Kingdom remained firm in the second half of 1977, the level of economic activity has not recovered as anticipated and unemployment has continued to rise. However, the current account of the balance of payments has moved decisively into surplus and the rate of price inflation has fallen significantly.

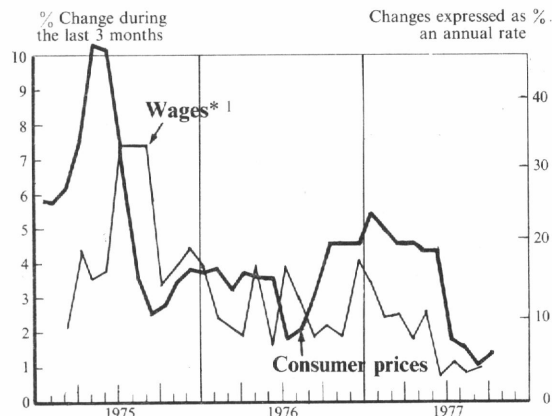
The absence of an agreement between the Government and the trade unions of the future level of pay settlements points to an acceleration in the rate of growth of earnings. This, combined with direct tax reductions, at a time of falling rates of inflation, will contribute to a strengthening of private consumption in the first half of 1978, and a more satisfactory rate of growth of output. Unemployment, however, is likely to remain at a high level. The current account of the balance of payments should remain in surplus despite some increase in imports.



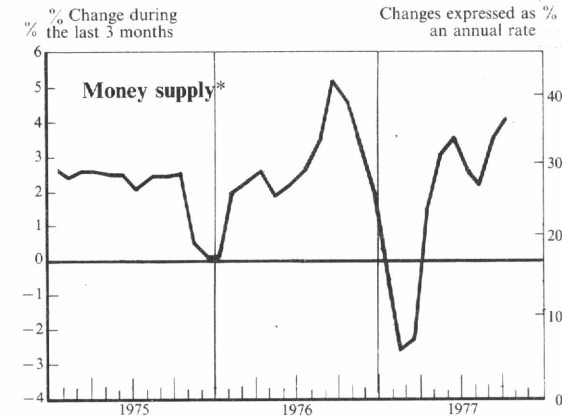
1) All industries.
Source: C.S.O.



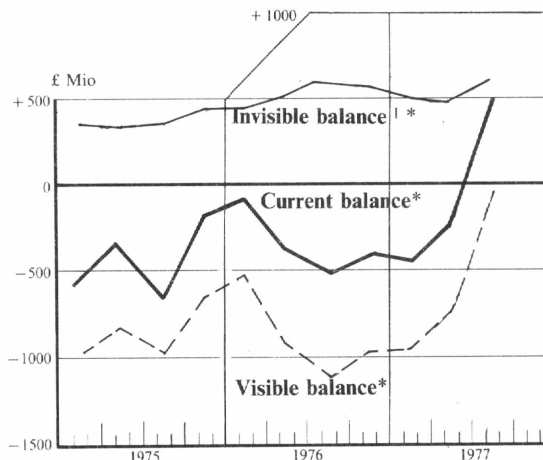
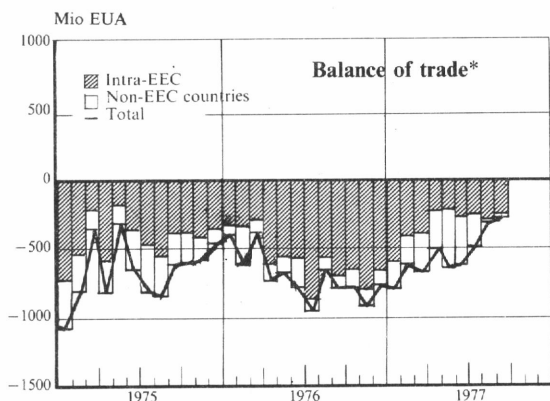
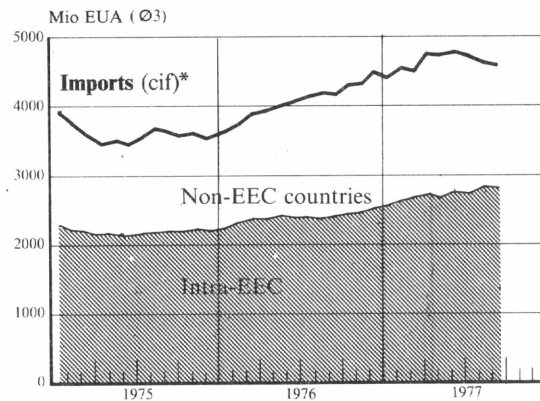
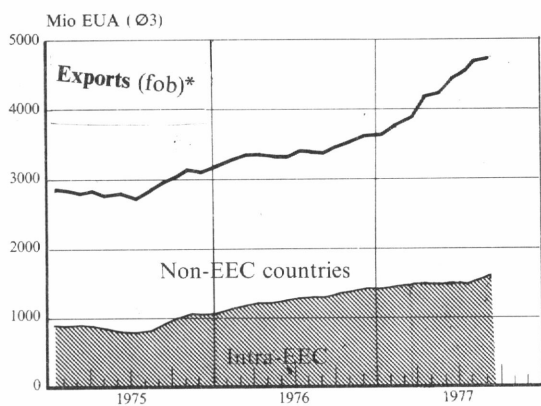
1 Excl. school-leavers and adult students.
Source: Dept. of Employment.



1 Monthly average earnings in Great Britain.
Source: Dept. of Employment.



Money supply: M3 (including interest-bearing deposits).
Source: Bank of England.



1 Includes services, factor incomes and current transfers.
Source: C.S.O. and Dept. of Trade and Industry.

* Seasonally adjusted figures.
Ø3: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

1. Overall assessment and main policy issues

In the United Kingdom, in the second half of 1977, the continued improvement in the financial indicators, the move into surplus on the current account of the balance of payments and the fall in the underlying rate of inflation contrasted sharply with the disappointing rate of growth of domestic output and the high and still rising level of unemployment. These circumstances provided both the need and the room for some adjustments to the Government's policies which, however, remained cautious and well within the guidelines communicated to the International Monetary Fund (IMF) in December 1976.

The first modification to the Government's policies occurred in July 1977, after it became clear that the Trades Union Congress (TUC) was unable to agree to a limit on the level of pay settlements for the following twelve months. On 15 July, the Government announced its new pay policy which aimed at keeping the growth of average earnings below 10% by means of the continued observance of a 12-month gap between settlements, by allowing increases in take-home pay through income tax adjustments and by a sustained effort to persuade negotiators to remain within the Government's guidelines. As part of this policy, the Chancellor presented a set of measures which, however, were little different in total cost from the proposals in the March Budget. These measures included increases in the tax-free personal allowances above those proposed in the March Budget, and a reduction in the basic rate of income tax from 35%

to 34%, which were equivalent to an increase of over 2½% in disposable income for a man on average earnings. These proposals were reinforced by other measures of particular importance to families and people with low incomes, and by the allocation of existing funds to employment support schemes and investment in industry.

By the Autumn, it had become evident that the level of total demand was markedly lower than had been anticipated at the time of the Spring Budget and that both Domestic Credit Expansion (DCE) and the Public Sector Borrowing Requirement (PSBR) for 1977/78 would be well within the figures communicated in December 1976 to the IMF. The Government, therefore, introduced a second set of measures, on 26 October, designed to provide a modest but quick-acting stimulus to activity and, in due course, to employment. For 1977/78, the budgetary measures consisted largely of further income tax reductions and a Christmas bonus for old-age pensioners at a total cost of about £1 billion. For the next financial year (1978/79) there is to be an increase in the previously-planned level of public expenditure of a little over £1 billion. It is officially estimated that the measures should raise output by 1% and increase employment by 170 000, by the first quarter of 1979, compared with what they otherwise would be. After these measures, the PSBR is forecast to be only £7½ billion in 1977/78 and £7 billion in 1978/79 (compared with the figures of £8.7 billion and £8.6 billion respectively, communicated to the IMF).

TABLE 1
Key indicators

United Kingdom	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁵	1977 ⁶
Gross domestic product, volume	% change	2.5	— 1.7	1.6	0.4
of which: industry ¹		1.8	— 6.0	1.0	0.6
Gross domestic product in volume per person in employment	% change	2.3	— 1.0	2.3	0.5
Total employment (number of persons) ²	% change	0.2	— 0.7	— 0.7	— 0.1
— Independent entrepreneurs		0.8	— 1.6	— 0.1	:
— Wage and salary earners in company sector		1.3	— 2.2	— 1.8	:
— General Government		1.7	6.2	2.1	:
Unemployment	as % of labour force	2.8	3.9	5.2	5.9
Compensation of employees per wage and salary earner	% change	14.0	30.6	14.8	10.5
Price index of private consumption ³	% change	9.8	23.5	15.3	15.3
Current account balance ³	£ '000 million	— 0.5	— 1.7	— 1.4	0.2

¹ Manufacturing industry only

² Domestic concept.

³ National accounts concept, on annual basis.

⁴ Geometric mean of the change from 1969 to 1974, unemployment and current account balance arithmetic mean over the five years

⁵ Source: Central Statistical Office

⁶ Estimates of Commission's Departments
No data available

Although the official outlook for the PSBR would have permitted a larger fiscal stimulus in October, there was a danger that the growth of the money supply would then move beyond the Government's target range of 9%-13% for the current financial year. The pressure leading to faster monetary expansion has largely come from capital inflows which, given the authorities' policy of preventing any appreciation of the exchange rate, continued at a high level. This policy consisted throughout the first half of the year of stabilising the sterling exchange rate in terms of the US dollar (at about \$ 1.72). Increasing weakness of the dollar, however, caused the authorities to modify their policy on 27 July 1977, and the rate of exchange was then maintained stable in effective terms (at an index of around 61.5 compared with Smithsonian parities). As the upward pressure on sterling continued despite a rapid fall in interest rates and some relaxation of exchange controls (announced on 26 October), the authorities finally decided, on 31 October, to allow sterling to float freely in an attempt to ensure that monetary growth remained within the target range.

2. Recent developments ¹

Signs of some strengthening of total demand appeared in the second half of 1977, and **Gross Domestic Product (GDP)** is likely to have increased by between ½% and 1% compared with the first half-year. This albeit modest improvement was due to the vigorous growth of net exports and a recovery in private consumption being largely offset by a marked reduction in stocks.

The strengthening of **private consumption**, which is likely to have been 1½% above the level of the preceding half-year, resulted from an increase in real incomes due to falling rates of inflation together with the rise in disposable income following the uprating of social

¹ Unless otherwise stated, this analysis is based on seasonally-adjusted data. In addition, volume changes are calculated on the basis of prices of the preceding year (or half-year) rather than at constant 1970 prices. As this increases the impact of North Sea oil, estimates of growth of GDP and exports will be higher, and imports lower, than using the 1970 price basis.

TABLE 2
Demand for and supply of goods and services

United Kingdom	1975 ²	1976 ²			1977 ³			1978 ³
	At current prices Mto £	% change on preceding year						
		Volume	Price	Value	Volume	Price	Value	Volume
Private consumption	63.333	0.2	15.3	15.5	- 1.0	15.3	14.2	3.8
Public consumption	22.847	2.4	13.1	15.8	- 0.4	10.8	10.4	- 0.4
Gross fixed asset formation	20.509	- 4.4	17.5	12.3	- 4.1	12.8	8.2	2.8
— Enterprises	11.427	- 4.2	18.6	13.6	:	:	:	:
— Dwellings	4.020	- 0.4	14.8	14.3	:	:	:	:
— General Government	5.062	- 7.9	14.1	5.1	:	:	:	:
Domestic final uses (excluding change in stocks)	106.689	- 0.2	15.1	14.9	- 1.5	13.9	12.2	2.7
Domestic final uses (including change in stocks)	105.389	1.0	15.2	16.4	1.1	13.9	12.6	3.4
Exports ¹	26.801	6.5	22.0	30.0	7.5	16.2	24.8	6.1
Imports ¹	28.935	4.2	21.3	26.4	2.2	16.1	18.6	5.7
Gross domestic product at market prices	103.255	1.6	15.3	17.1	0.4	13.9	14.3	3.7
Domestic final uses (excluding change in stocks)	106.689	- 0.2	—	15.2	- 1.5	—	12.3	2.7
Change in stocks	- 1.300	1.3	—	1.4	0.4	—	0.5	0.8
Balance of exports and imports ¹	- 2.034	0.5	—	0.5	1.5	—	1.5	0.2

¹ Goods and services.

² Source: Central Statistical Office.

³ Estimates of Commission's Departments.

· Data not available.

security payments, the reductions in income-tax announced in the Budget and in October, the Christmas bonus for old-age pensioners.

The volume of **exports** of goods has remained buoyant in spite of sluggish growth of world trade, and is likely to have increased by some 3½% in the second half of the year, whereas **imports** could well have remained static or even declined, reflecting in particular the impact of lower imports of fuels and of food, beverages and tobacco. Nonetheless, the imports of finished manufactured products continued to grow strongly. The strengthening of the exchange rate contributed to an improvement in the terms of trade which, together with the substantial surplus on invisibles account, suggests that the **current account** of the balance of payments will register a surplus, for the second half of the year, of about £1 billion and for the year as a whole, of about £¼ billion.

Gross domestic capital formation has continued to decline as the recovery of private industrial investment has been more than offset by substantial falls in investment by the public sector and in dwellings. There is likely to have been a marked reduction in stocks after the involuntary stockbuilding in the first half-year. The level of **public consumption** has continued virtually unchanged as a result of earlier measures designed to control the growth of public expenditure.

Industrial production is likely to have recovered somewhat in the fourth quarter from the low levels recorded in the summer. **Unemployment**, after stabilizing in the first five months of the year, seems to have resumed its irregular upward trend and, in November, was equivalent to 6.2% of all employees.

After reaching a peak in the early summer, the rate of **inflation** has moved on to a declining trend; over the six months to October 1977, the index of retail prices (excluding seasonal foods) rose at an annual rate of 9.9% compared with a rate of 20.5% in the preceding six-month period. This movement reflects the fall in world commodity prices and the stability of the exchange rate, as well as the deceleration in the growth of unit labour costs under phase II of the Government's incomes policy. Indeed, over the twelve months to September 1977, average earnings increased by only 7.5%.

The substantial inward capital movements, which were a feature of the first half-year, continued in the Autumn despite the reduction of interest rates which brought the Bank of England minimum lending rate down from 8% in June to 5% by end-October. This led to a further massive increase in the **foreign exchange reserves** which reached a record level of \$ 20.2 billion at the end of October. These inflows caused the Government's target for the growth of the money supply (9-13% in the financial year 1977/78) to come under pressure.

3. Outlook

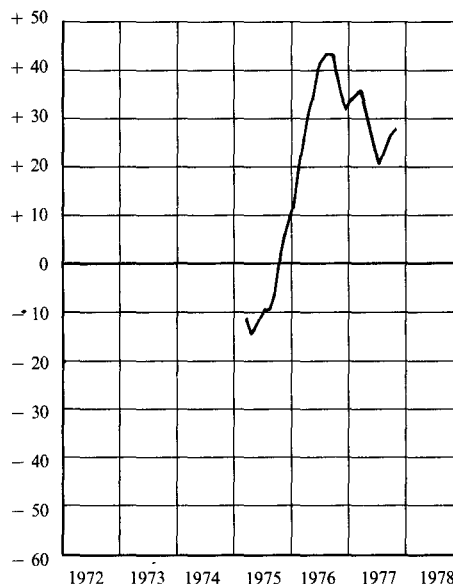
With falling rates of inflation, an acceleration in the growth of earnings, and reductions in direct taxation,

there is likely to be a relatively marked increase in domestic demand in the first half of 1978, led by an acceleration in the growth of **private consumption**. At the same time, gross capital formation should begin to recover, due largely to the expected increase in investment in manufacturing industry and private sector dwellings, together with some modest rebuilding of stocks.

On the external side, the volume of exports is expected to continue to expand but will tend to be offset by an acceleration in the growth of imports as domestic demand recovers. After making due allowance for the expected surplus on invisibles and for a further slight improvement in the terms of trade, the **balance of payments** on current account could well register a surplus, for the first half of 1978, of about £500 million.

The rate of growth of **GDP**, for 1978 as a whole, (measured at 1977 prices) could well exceed 3½%. Increased output of North Sea oil is expected to account for about one-third of this growth. However, on past experience, this increase in activity would not be expected to have any significant impact on **unemployment** until the second half of the year.

**Views of businessmen
on the production outlook
in the coming months**



NOTE:

This graph is based on answers to questions in the EEC business survey; it shows a three months moving average of the difference between "above normal" and "below normal" answers to the following question: "Do you think that over the next three or four months your firm's seasonally adjusted production trend will be:

- (1) up,
- (2) unchanged or
- (3) down?"

Although the outlook for the growth of the UK economy in 1978 has improved, the prospects for a continued fall in the rate of inflation to the levels pertaining in competitor

TABLE 3
Main economic indicators

United Kingdom	Year	Jan.	Feb	Mar	Apr.	May	June	July	Aug.	Sept.	Oct	Nov.	Dec.
Industrial production (1970 = 100)	1975	105.2	106.1	103.8	101.8	99.9	99.8	100.2	98.5	100.4	100.8	101.1	99.5
	1976	101.2	101.6	102.1	103.0	105.2	102.4	104.1	103.2	104.4	104.8	105.0	104.5
	1977	105.4	105.6	105.7	103.7	105.2	100.3	103.6	103.2	102.6			
Unemployment (1000)	1975	707.3	734.3	764.4	805.5	853.7	898.8	963.4	997.1	1 034.1	1 099.8	1 131.9	1 170.9
	1976	1 203.5	1 225.8	1 231.6	1 241.8	1 253.3	1 261.1	1 288.9	1 308.8	1 318.7	1 307.9		1 325.7
	1977	1 338.2	1 331.4	1 321.1	1 322.6	1 315.9	1 352.9	1 393.8	1 413.9	1 446.4	1 433.4		
Construction: Housing starts (1000)	1975	25.8	26.0	24.1	23.9	25.2	26.4	26.7	26.9	28.7	30.3	30.4	30.7
	1976	31.5	29.1	31.1	28.6	29.8	28.5	29.5	27.7	27.6	22.0	21.5	18.0
	1977	21.4	34.8	21.4	22.1	22.8	22.3	24.4	20.4	25.8			
Average earnings (1970 = 100)	1975	206.2	209.9	212.8	215.4	217.7	221.2	231.6	234.0	237.9	239.3	241.1	248.1
	1976	248.3	250.0	254.4	255.0	259.6	261.2	263.1	267.2	266.1	269.0	272.2	277.1
	1977	278.1	278.7	283.8	283.1	286.2	286.2	286.5	288.7	289.5			
Private consumers' expenditure: value of retail sales (1971 = 100)	1975	165.9	165.7	165.9	183.9	166.9	171.1	175.3	175.8	179.2	177.8	180.8	186.4
	1976	193.7	189.1	188.6	196.2	193.5	195.6	200.2	204.2	206.4	207.7	212.9	214.5
	1977	217.6	218.1	215.8	219.5	221.8	223.2	232.8	237.6	236.6			
Retail prices (January 1974 = 100)	1975	119.9	121.9	124.3	129.1	134.5	137.1	138.5	139.3	140.5	142.5	144.2	146.0
	1976	147.9	149.8	150.6	153.5	155.2	156.0	156.3	158.5	160.6	163.5	165.8	168.0
	1977	172.4	174.1	175.8	180.3	181.7	183.6	183.8	184.7	185.7	186.5		
Wholesale prices ¹ (1970 = 100)	1975	222.1	218.8	221.9	222.9	226.2	227.7	233.2	241.4	243.2	252.2	256.7	259.5
	1976	261.5	263.9	274.2	286.3	292.0	299.6	302.0	303.9	314.4	327.7	331.8	330.2
	1977	337.8	339.5	347.2	349.7	348.3	345.2	344.6	338.8	338.1	334.4		
Wholesale prices ² (1970 = 100)	1975	173.0	175.9	179.2	182.5	187.3	189.0	191.7	193.5	194.9	197.0	198.9	201.5
	1976	204.8	207.3	208.6	211.5	214.8	217.0	219.8	223.4	226.3	230.0	234.6	237.2
	1977	244.9	248.2	250.8	255.4	259.7	262.4	265.8	268.1	269.3	270.9		
Exports (million EUA)	1975	3 002	2 875	2 808	2 902	2 960	2 710	3 047	2 794	3 024	3 227	2 861	3 304
	1976	3 133	3 187	3 743	3 326	3 189	3 606	3 351	3 513	3 609	3 245	3 651	3 801
	1977	3 645	3 753	4 235	3 906	4 261	4 240	4 198	4 370	4 543			
Imports (million EUA)	1975	4 054	3 679	3 149	3 732	3 246	3 370	3 836	3 593	3 611	3 799	3 420	3 783
	1976	3 550	3 788	4 129	4 059	3 852	4 375	4 297	4 169	4 398	4 020	4 566	4 556
	1977	4 474	4 348	4 893	4 408	4 853	5 029	4 604	4 566	4 803			
Balance of trade (million EUA)	1975	-1 052	- 804	- 340	- 830	- 286	- 660	- 788	- 799	- 587	- 571	- 559	- 481
	1976	- 417	- 601	- 386	- 733	- 663	- 769	- 946	- 656	- 789	- 775	- 915	- 755
	1977	- 829	- 595	- 658	- 502	- 592	- 789	- 406	- 196	- 260			
Terms of trade	1975	76.2	77.2	77.2	79.1	80.2	81.4	81.8	81.7	82.1	81.0	80.8	80.3
	1976	81.4	81.7	81.7	80.2	79.7	80.1	79.5	80.7	80.4	79.3	78.4	79.3
	1977	80.8	80.3	80.0	79.4	80.7	80.2	80.1	82.5	83.4			
Exchange rate	1975	81.5	81.6	81.9	81.0	78.8	77.4	76.0	74.9	74.6	73.4	73.0	72.6
	1976	72.8	72.7	70.5	67.2	65.8	64.3	65.1	64.8	62.5	59.2	59.1	60.5
	1977	61.8	61.7	61.9	61.7	61.6	61.5	61.0	62.0	62.4	62.5		
Official foreign exchange reserves (million EUA)	1975	3 112	3 241	3 288	3 231	2 752	2 476	2 620	2 425	2 317	2 181	2 102	2 000
	1976	3 072	3 214	2 460	1 793	2 052	2 031	2 070	1 862	1 830	1 528	1 796	1 310
	1977	3 348	3 696	4 624	4 893	4 844	5 587	6 540	7 362	8 587			
Money supply (million EUA)	1975	25 384	24 749	25 505	25 998	26 668	26 126	28 020	27 962	28 323	28 036	27 887	28 864
	1976	28 110	28 942	28 663	28 869	27 667	28 151	28 948	29 190	27 902	26 190	27 232	28 415
	1977	27 803	27 604	28 107	29 193	29 230	29 994	30 189	32 664	31 808			

Seasonally adjusted unless otherwise stated

Not available.

Key to sources: (a) Central Statistical Office.

(b) Department of Employment

(c) Bank of England.

(d) Ministry of Health and Social Services (Northern Ireland)

(e) Department of Trade and Industry.

(f) Department of the Environment

(g) EUROSTAT.

— Index of industrial production (Manufacturing industry only 1970 = 100) (a)

— Unemployment wholly unemployed, excluding school-leavers and adult students (b + d)

— Construction: private and public housing starts in Great Britain (f).

— Average earnings: (all industries) Great Britain (b)

— Retail sales: index numbers of the value of sales at current prices (e)

— Retail price index (all items) (not seasonally adjusted) (b).

— Wholesale prices: (1) Input prices (all manufacturing industries) (not seasonally adjusted)

(2) Output prices (home sales, all manufactured products) (not seasonally adjusted) (a).

— Exports (fob) and imports (fob) of goods on a balance of payments basis (g)

— Balance of trade: difference between the seasonally adjusted figures of imports and exports (g)

— Exchange rate: effective exchange rate on Smithsonian basis (19 December 1971 = 100) (g).

— Official foreign exchange reserves: end-month figures (not seasonally adjusted) comprising gold IMF Special Drawing Rights, convertible currencies and, from July 1972, the UK's reserve position at the IMF. Before conversion into EUA, values have been converted into sterling at prevailing middle rates (g).

— Money supply M3 (including interest-bearing deposits) (c + g)

countries are less favourable, given the possibility of an acceleration in the rate of growth in average earnings. The Government should, therefore, maintain its present fiscal and monetary stance, which is somewhat more restrictive than would otherwise be required, until it becomes clear that labour costs are not rising at an unacceptably high rate.

Major economic policy measures

June 1977:

- On 14 June, details were announced of the sale of a 17% interest in British Petroleum (out of the Government's holding of 68%). The sale would realize about £564 million.
 - On 29 June, the Secretary of State for Employment announced new measures designed mainly to combat youth unemployment at a cost of £800 million gross over the five years from September 1978. The measures include:
 - an extension of the jobs creation programme, the work experience scheme and the youth employment subsidy for periods of between six and twelve months beyond their present respective expiry dates;
 - an increase in spending on work experience programmes and the setting up of work-preparation courses in further education establishments and skill centres.
- Also announced were two new plans to aid adult employment. These are
- provision of 8 000 places for unemployed skilled workers to instruct and supervise young people on work experience courses;
 - a special temporary employment programme to provide job opportunities for those aged 19 and over for up to one year;
 - in addition, the job release scheme due to close on 30 June will be extended to 31 March 1978.

July

- On 1 July, the Bank of England launched a new £400 million variable interest rate tap stock.
 - On 15 July, the Chancellor revealed the plans for the incomes policy for the twelve months from 1 August 1977. They comprised:
 - an orderly return to free collective bargaining;
 - a national increase in earnings of not more than 10 per cent;
 - maintenance of the rule under which 12 months must elapse between wage settlements. In addition, the Chancellor announced a set of supporting measures acting directly on disposable income and the cost of living. These were:
 - increases in personal allowances and a reduction in the basic rate of income tax from 35% to 34%;
 - increases in child benefits, the milk subsidy and the income limits on families eligible for free school meals;
 - a further £100 million to assist employment in the construction industry;
 - dividend controls to be continued for another year.
 - On 24 July, the Government decided not to draw the final \$ 400 million tranche of the \$ 1.2 billion loan negotiated with Iran in July 1974.
 - On 27 July, the Bank of England confirmed that it had stopped holding down the exchange rate of sterling in dollar terms but would continue to stabilise the value of sterling in terms of the effective exchange rate.
- On the same date, the Post Office announced record profits of £392 million. Of this sum, £101 million would be given as rebate to telephone subscribers in the autumn

August

- The Price Commission Act came into force on 1 August 1977. Under the new policy the Price Commission has been reconstituted and given wider and more flexible powers. These include:
 - wide powers to investigate current prices, price increases and profit margins with a view to deciding on the admissibility of proposed price increases;
 - the possibility that Price Commission recommendations may be enforced by statutory order;
 - powers to freeze prices during an investigation (which may not take longer than 3 months) or to recommend that a company's prices be frozen up to 12 months
- On 11 August, the Bank of England decided to suspend the "corset", the restraint on the rate of growth of the banks' interest-bearing liabilities.
- It was announced on 29 August that the Government was making another £80 million available as aid to industry. The money is channelled into three schemes:
 - a new products and processes scheme to help businesses to introduce better designed products and get them on the market more quickly;
 - the ferrous foundry scheme;
 - the machine tool scheme.

September

- The United Kingdom official reserves were reported, on 2 September, to have risen to \$ 17 171 million. The rise in August of \$ 1 430 million included official borrowing of \$ 374 million on the IMF standby facility and \$ 100 million on the second tranche of the Government's \$ 1.5 billion Eurodollar loan.
- On 7 September, the Trades Union Congress voted in favour of supporting the 12-month rule for pay settlements but called for Government action to expand the economy and reduce unemployment

October

- On 26 October, the Chancellor of the Exchequer announced measures to stimulate economic activity in the next 18 months without over-heating the economy and without exceeding the limits, agreed with the IMF, for the public sector borrowing requirement and domestic credit expansion. The cost of the measures will be about £1 billion in the current year and £2 billion in 1978/79. The measures include:
 - an increase of 12%, back-dated to April 1977, in the main personal tax allowances (cost £940 million in 1977/78);
 - a tax-free bonus of £10, at Christmas, for pensioners;
 - additional public expenditure in 1978/79 on the construction industry (£400 million), overseas aid (£20 million), social security (£20 million) and aid for small firms (£2½ million);
 - a relaxation of exchange controls (at a cost of about £400 million to the balance of payments in 1978) comprising increases in the sterling and foreign currency allowances for people going abroad on holiday or business travel and permission for all foreign-controlled manufacturing companies to borrow sterling, without restriction, for their UK business;
 - a decision not to take up any further drawings on the IMF standby although the United Kingdom's drawing rights remain until the end of 1978.
- On 30 October, the Government ended its policy of holding down the sterling exchange rate in terms of the effective exchange rate and allowed the pound to rise freely in the foreign exchange markets.

November

- On 8 November, it was announced that the Bank of England had agreed to sterling denominated securities being issued internationally. The first issue was for £15 million for 12 years for the European Coal and Steel Community.