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**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.

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**COMMISSION
OF THE
EUROPEAN COMMUNITIES**

The economic situation in the Community

JUNE 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 7 July 1977.

I — The general situation

The period of recovery which has affected the Community's economy for almost two years has been characterized by alternate phases of acceleration and deceleration. Since the beginning of this year, these last have tended to predominate. The persistence or even aggravation of strong sectoral and geographical variations in trends of income, supply and demand has prevented, up to the present, owing to the constraints imposed by inflationary pressures and excessive external imbalances, the development of the cumulative cyclical upswing noticed in former recovery periods. A slight improvement in the economic situation is expected in the second half of 1977 owing, in particular, to a more rapid growth of exports and, in certain countries, of private consumption. Nevertheless, the rate of economic growth for the full year will be only 3% in real terms for the whole Community, as against more than 4½% in 1976.

In these conditions, and in a medium-term perspective, the progress achieved towards the reestablishment of full employment has been disappointing. The propensity to engage in employment-creating investment has remained weak. Wherever employment demand has emerged, it has been satisfied, essentially, by a lengthening of hours worked by those already employed. In the spring, the seasonally adjusted unemployment rate for the Community as a whole was 5.1%, and it may increase somewhat during the second half of the year. In fact, the number of young people in search of their first jobs will probably be greater than in 1976, while a growing number of women will be seeking to enter professional employment.

Price increases have regained momentum since the autumn, although demand pressures on overall resources are no more than moderate. This acceleration is attributable in part to a scarcity of agricultural products, following the drought which parched the Community in 1976, as well as unfavourable climatic conditions which strongly affected the prices of certain tropical products. But other factors such as higher charges for public services and petroleum-product prices have also contributed. On the other hand, the influence of labour costs on the prices of manufactured goods has generally remained relatively moderate. Overall, consumer price increases in 1977 will be only very slightly lower than those of last year, despite the slowdown expected in the second half of the year as a result, especially, of a return to normal in foodstuff supplies. The rate of increase foreseen is, in fact, 9½% as against 10% in 1976.

It is on the external side, alone, that the position of the Community has evolved in a relatively satisfactory manner, following the strong deterioration observed throughout 1976. Foreign-exchange market conditions have been tending towards stability. There has been a clear improvement in the Community's trade balance, and this in spite of a deterioration in the terms of trade, owing to a reduction in the volume of purchases by the deficit countries. This positive tendency, to which north-sea oil will increasingly contribute, should result, in 1977, in the reestablishment of balance in current Community payments, which last year had been in deficit to the extent of more US 8 billion.

A — Economic policy problems in the Community

1. The Community is facing two major problems. First, it must resume growth at a rate high enough to ensure full employment while controlling inflation. Secondly, it must narrow the range of performances of the Member States'

economies through supplementation measures to regulate demand and convergent action to adapt economic structures.

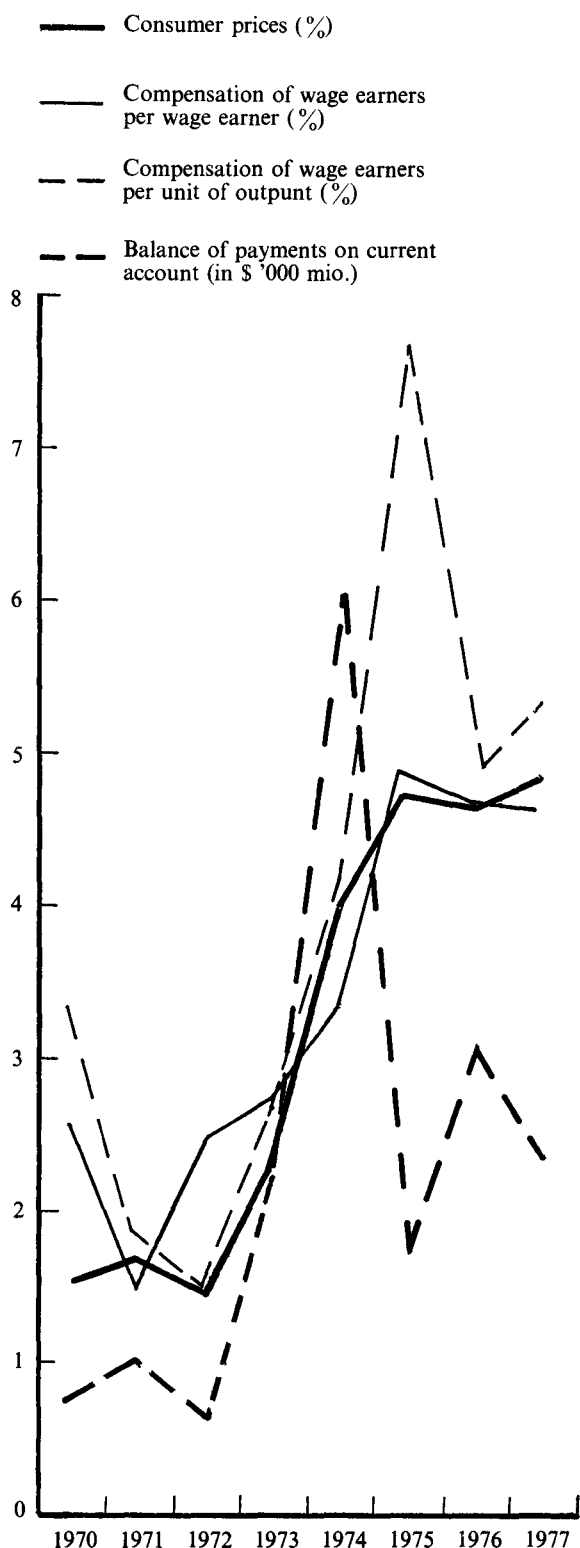
TABLE 1
Lags as regards medium-term objectives (1976-1980)
(Average annual rates)

	Development		Objectives 1976-1980	Performance required in 1978-1980 to realize these objectives
	1976	1977		
Growth of GDP in volume	4.6 %	3 %	4.5-5 %	5½ %
			End of period	
Unemployment rate	5.0 %	5.3 %	Full employment	Reduction of 1 point per year
Inflation	10 %	9½ %	4-5 %	Reduction of 1½ point per year

Source: Commission's Departments

GRAPH A

**Divergence in developments
of prices and wage costs,
and also balances of payments
on current account ¹**



¹ Dispersion with respect to the Community average as measured by the standard deviation.
Source: Commission's departments.

The difficulty of this twofold task is brought out clearly in the analysis this Survey provides of the economic situation in the Community and of the short-term outlook. Many obstacles stand in the way of achieving the objectives agreed for 1977 of limiting the rate of inflation, boosting production and employment, and reducing current-account disequilibria. ¹ Exceptional factors have forced up prices faster than was expected since last summer. The confidence of individuals and firms has been restored too slowly, partly because of the inhibiting effect on world demand of persistent balance of payment deficits in many countries. In some Member States, the budget as an instrument for guiding the economy is still inadequately controlled. All in all, in spite of government efforts to apply the Council's guidelines for economic policy, it now looks as if there is very little prospect of making good the ground that has been lost on the way to the medium-term objectives, ² particularly where growth and employment are concerned. ³

2. The economies of the Member States could be adapted more easily to the radical transformations that have taken place in the world economy if compatibility were maintained between short-term policies and the Community's medium-term strategy. The point upon which these policies converge is still the consolidation and the revival that began in the Community in autumn 1975, and the elimination of the constraints that hinder the return to lasting growth. Obviously it is important, in this context, to control inflation, for one of the unwelcome effects of rising prices is that they tend to delay the structural adjustments that are becoming increasing and urgent. But the Community must guard against the situation whereby underuse of resources would lead to a chronic weakness of the propensity to invest, and the consequent continuous increase in the rate of unemployment. The solution of this double problem requires not only coordinated deployment of all the available instruments — both general and specific — of economic policy but also the consolidation of the social consensus which the Community is trying to bring about in the Member States ⁴ so as to restore confidence as quickly as possible.

3. The protection of home industries is not the right weapon with which to fight unemployment and inflation. Indeed, the Community must be more — not less — keenly aware of the need to make an adequate contribution to the expansion of world trade, and particularly to the improvement of such markets as are available to the poorer developing countries. Since non-member countries are tending to concentrate on products with a high labour or energy content, the European countries would best serve their own interests if they steered their growth towards technological progress and research. The process will have to be supported by rapidly increasing investment in the context of growth at a rhythm once again compatible with medium-term objectives.

¹ See Quarterly Surveys No 3/1976 and No 1/1977.

² See Council Decision No 77/294/EEC of 14.3.1977 (OJ L 101 of 25.4.1977).

³ See Table 1.

⁴ See Commission Communication to the European Council Growth, stability and employment, COM(77)250 final of 23.5.1977.

TABLE 2
Main macro-economic aggregates

Country	Gross domestic product (volume) % changes				Unemployed as % of labour force ²			
	1970- 1974	1975	1976	1977	1970- 1974	1975	1976	1977
Denmark	2.8	- 1.1	4.8	1.5	1.3	5.2	5.0	6.0
FR of Germany	3.1(a)	- 2.6	5.7	3.8	1.1	4.1	4.1	3.8
France	5.1	+ 0.1	5.2	3	2.7	4.2	4.6	4.8
Ireland	3.4	+ 0.4	3.2	3.7	5.9	7.9	9.4	9.3
Italy	4.1	- 3.5	5.6	3	3.3(5.2)	3.3(5.5)	3.7(5.9)	3.9(6½)
Netherlands	4.7	- 1.1	3.7	4.2	2.1	4.3	4.6	4.4
Belgium	5.2	- 2.0	3.0	3.2	2.3	4.5	6.1	6.9
Luxembourg	4.1	- 8.4	3	2	0	0.2	0.4	0.3
United Kingdom	2.5	- 1.7	1.8	0.8	2.8	3.7	5.2	5.9
Community	4.0	- 1.8	4.6	3.0	2.4(2.8)	4.0(4.5)	4.5(5.0)	4.8(5.3)
United States	3.1	- 1.8	6.1	5	5.6	8.5	7.7	6.8
Japan	6.2	2.4	6.3	5½	1.3	1.9	2.0	2

Country	Implicit consumer price, % changes				Balance on current account (US '000 million)			
	1970- 1974	1975	1976	1977	1970- 1974	1975	1976	1977
Denmark	7.9	8.8	8.5	9	- 1.0	- 0.5	- 1.9	- 1.6
FR of Germany	6.3 ¹	6.3	4.4	4	3.1	4.4	3.2	3.0
France	8.3	11.6	9.9	9.0	- 1.1	0	- 5.8	- 3.1
Ireland	10.8	21.8	17.0	14.5	- 0.2	0	- 0.3	- 0.5
Italy	8.7	17.6	17.5	19	- 1.3	- 0.6	- 2.9	- 0.8
Netherlands	8.0	10.5	9.1	7.1	2.1	1.7	2.5	2.8
Belgium	6.3	12.1	8.8	7.5	1.0	0.3	- 0.4	0
Luxembourg	6	10.7	9.8	7.8	- 1.2	- 3.6	- 2.6	0.4
United Kingdom	7.5	23.4	15.2	15.0	- 1.2	- 3.6	- 2.6	0.4
Community	7.8	12.8	9.9	9.6	1.2	1.7	- 8.1	0.2
United States	6.0	8.0	5.1	6½	- 3.5	11.7	- 0.6	- 11½
Japan	10.5	10.9	8.3	8½	1.9	- 0.7	3.7	+ 6½

¹ 1971-1974

² The unemployment rate, indicated in brackets, is that obtained using, for Italy, unemployment figures from the labour Ministry rather than those from ISTAT
Source: Departments of the Commission.

The Community should strive to encourage investment:

- (i) by strengthening existing Community instruments, and putting them to better use;
- (ii) by creating a new instrument for Community loans to finance structural projects.¹

However, it should be recognized that conflict may arise between the need to develop new, highly competitive, products or to supply urgently required new sources of energy, and the need to reorganize traditional production operations, which are often extremely important from the point of view of employment. These conflicts will be all the more difficult to solve in the short run if the international community does not realize that the adjustment of balances of payments at world level is bound to take some time and will require appropriate

financing facilities. Moreover, unless a certain level of growth can be achieved, neither the problem of inflation nor the problem of unemployment can be satisfactorily controlled on a world level.

4. The Commission has recently submitted economic policy guidelines for 1977 and 1978 to the Council.¹ They are aimed, in particular, at reducing the wide range of performances among the various Member States² through supplementary economic policy measures de-

¹ See Commission Communication to the European Council 'Investment and borrowing in the Community', COM(77)300 final.

² See Commission Communication to the Council on economic policy for 1977 and the preparation of public budgets in 1978 (COM(77)315 final of 7 7 1977)

³ See Table 2 and Graph A.

signed to achieve agreed macro-economic objectives. It is to be hoped that instability caused by exchange rate movements will be less damaging in the future, after monetary depreciation has shown that it alone does not offer a lasting solution to the economic problems of countries with severe payments disequilibria. But other risks are now discernible. In particular, it may be feared that recent pressure on prices and costs in most of the

Member States may attenuate insufficiently, thus reducing the prospects of an improvement in the propensity to invest. These dangers require energetic action. By exploiting to the full the area of manoeuvre made available by improved control of inflation, demand regulation policy can contribute more efficiently to supporting economic activity, and thus to restoring full employment as quickly as possible.

B — The world economic situation

1. The upswing has gained strength

The recovery enjoyed by most countries outside the Community in the spring of 1975 weakened in the second half of 1976. It has since gathered momentum again and the world economic situation now shows signs of renewed strength, to which the more rapid rate of growth in the United States since last autumn has been a major contributor. However, in other countries, such as Japan, where measures to bolster the economy have been taken, and Canada, where exceptional developments curbing activity have ceased to have effect, a moderate rate of activity has been achieved. In most of the other

industrialized countries, on the other hand, activity has remained at a low level, the scope for more sustained expansion still being severely limited by inflation or an external payments deficit (Australia, Sweden, Finland, etc.).

Since the beginning of the winter, the slow deceleration of price increases noted in several countries in 1976 has been disrupted by unfavourable climatic conditions, which have forced up the prices of agricultural products sharply. World commodity spot prices have also increased fairly substantially: in the period from October 1976 to April 1977, the HWWA index of non-oil commodity prices in

TABLE 3
Economic indicators

	1975				1976				1977	
	I	II	III	IV	I	II	III	IV	I	II
GDP in volume ¹										
United States	- 9.9	5.6	11.4	3.3	9.2	4.5	3.9	2.6	6.9	(7)
Japan	- 1.2	3.5	5.7	4.4	13.3	5.5	1.5	2.8	10	
Canada	- 1.4	2.7	6.3	5.7	13.1	1.6	- 1.2	- 0.8	5.2	
Community	- 5	- 1½	- ½	9½	8½	3	1½	5½	3½-4	
Unemployment rate ²										
United States	8.7	8.6	8.3	8.2	7.5	7.5	7.8	7.7	7.3	
Japan	1.7	1.8	1.9	2.1	1.9	2.1	2.0	1.9	1.9	
Canada	6.7	7.0	7.1	7.1	6.8	7.0	7.2	7.5	7.9	
Community	3.9	4.4	4.8	5.0	4.9	5.0	5.0	4.9	5.0	(5.1)
Consumer prices ^{1,3}										
United States	6.3	7.3	7.7	6.8	2.9	6.4	6.0	4.0	9.3	
Japan	9.1	8.5	9.1	4.4	12.6	12.2	9.9	7.0	8.7	
Canada	7.6	11.8	10.8	8.2	5.2	7.1	5.6	5.5	8.5	
Community		18.0	7.3	9.5	13.3	11.8	9.0	13.7	12.3	
Trade balance ⁴										
United States	2.1	3.3	3.1	2.4	- 0.4	- 0.6	- 2.4	- 3.1	- 6.0	
Japan	- 0.1	- 0.1	- 1.0	- 0.8	0.8	1.1	- 0.0	0.3	3.0	
Canada	- 0.5	- 0.6	- 0.5	- 0.3	- 0.1	- 0.1	0.4	0.0	(- 0.1)	
Community	- 0.8	0.5	- 1.3	- 2.8	- 3.3	- 4.8	- 5.1	- 6.3	- 5.3	

¹ Percentage change on preceding period, annual rate, seasonally-adjusted data

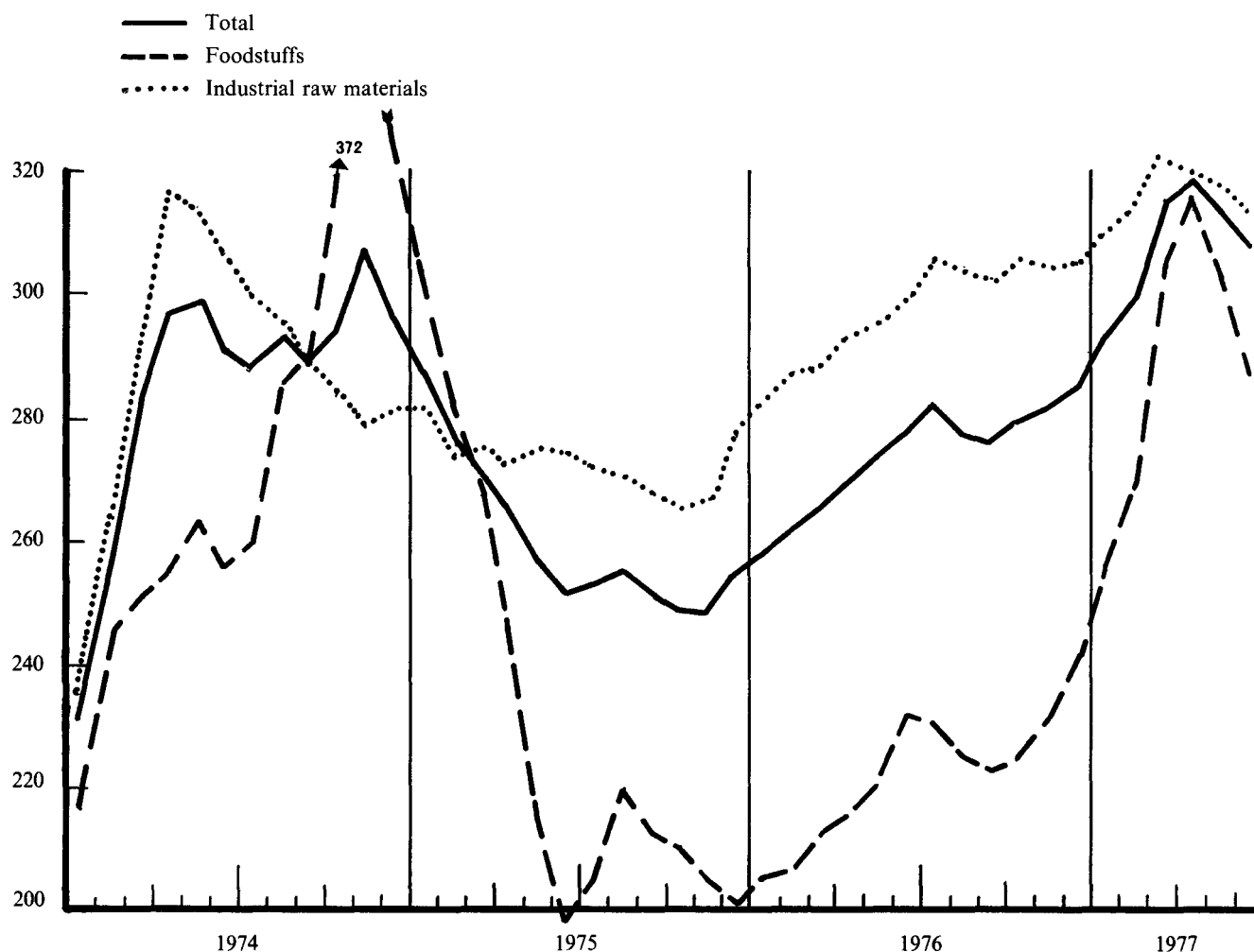
² Seasonally-adjusted data, end of period

³ Unadjusted data.

⁴ US \$ '000 million, seasonally-adjusted data

Source: Departments of the Commission.

World prices of raw materials



Source: HWWA.

dollars showed a rise of 14%.¹ Poor harvests have continued to affect the prices of some basic agricultural products such as cocoa and coffee in particular; these very sharp price rises have been passed on rapidly to the consumer, causing a rise in the prices of substitute products such as tea. After they had fallen throughout the summer and autumn of 1976, speculation led to a renewed upward movement in the prices of the most important industrial raw materials, particularly those of lead and tin. In December 1976, Saudi Arabia and the United Arab Emirates increased the price of their crude oil by 5%; the remaining OPEC countries increased their prices by 10%. Indeed, the heavy demand for oil products during the winter months means that the actual rise in crude oil prices has been near to the maximum increase announced. Since the beginning of the year, however, pressures on world commodity markets have eased, namely because of falling world demand for coffee and cocoa. Between April and June the HWWA index has thus fallen by about 4%.

In 1976 as a whole, *world trade* expanded sharply by (10½% in volume terms) after a 4% fall in 1975. Excluding the Community, whose trade increased

relatively vigorously in 1976, the volume of world imports grew by 9% compared with a fall of 3½% in 1975.¹ Since the spring of 1976, however, trade has tended to slacken, since imports in many countries have been inhibited by a slower rate of restocking and by the effects of stabilization measures; only the United States has proved an exception to this, its imports continuing to increase sharply. As in many other countries, imports of oil products played an increasing part in this process, particularly at the beginning of winter. During 1976, imports by OPEC countries slackened appreciably compared with the sharp expansion during the two preceding years and imports by the centrally planned economies have grown only very slightly. These trends have continued into the first six months of 1977. On the other hand, purchases by developing countries, which has picked up somewhat in 1976 as a result of a slight improvement in some of their financial positions, have continued to expand since last autumn.

¹ See Graph B.

² See Table 4.

There has been a sharp expansion of activity in the *United States*, but this has been accompanied by severer inflation. Following the pause in the fourth quarter of last year and despite the disruption caused by unfavourable climatic conditions, economic expansion has accelerated: in the first quarter of 1977, real GDP grew by 6.9% on an annual basis, while the figure for the second quarter has been estimated at 7%.¹ It seems that private consumption is largely responsible for this trend; despite the slow improvement in real disposable income and the shelving by the Carter Administration of the proposed tax concessions, households have sharply increased their expenditure; the propensity to save having declined further; sales of durable goods — particularly cars — have increased appreciably. Furthermore, expenditure on residential construction has expanded. Stockbuilding, moreover, increased strongly in the first quarter, although somewhat less than the movement in sales. However, an average rate of capacity utilization, which is still considered inadequate (in the region of 81% in industry), and widespread fears concerning the outcome of anti-inflationary measures and economic policy in general have curbed capital formation by firms, the expansion of which, in real terms, has remained slow. Employment has increased more sharply: in the period between November and April, more than one and a half million new jobs were created. The unemployment rate fell from 8.8% in October to 6.9% in May, despite a sharp increase in the civilian labour force.

The renewed upsurge in inflation is nevertheless once again a cause for concern. Although the prices of agricultural products and fuels were seriously affected by the cold spell and the drought which followed in the western States, prices of services also increased fairly sharply and — after several months of relative stability — the wholesale prices of manufactures also accelerated. In the period from December 1976 to April 1977, consumer and wholesale prices increased on an annual basis 9½% and 12% respectively.

The trade deficit has widened appreciably since the end of 1976. Major fuel purchases designed to replenish stocks during the period of intense cold have swollen imports, which have grown sharply. Even excluding imports of oil products, however, it would seem that for several months imports have tended to rise more strongly than exports. In the period from April 1976 to April 1977, growth of imports exceeded 31%, as against 6½% for exports which have also been held in check by the weak expansion of sales of agricultural products.

In *Canada*, too, the expansion of activity slackened in the second half of last year and, real GNP declined slightly.¹ Output has only revived moderately since the beginning of 1977. The situation on the labour market has therefore again deteriorated, with the unemployment rate reaching

¹ See Table 3

TABLE 4
World output and trade¹
(% change on preceding year)

	Real GDP ²					Volume of imports (goods)				
	1969-1973 average ³	1974	1975	1976	1977	1969-1973 average ³	1974	1975	1976	1977
United States	3.3	- 1.7	- 1.8	6.1	5	6.9	- 3.4	- 11.1	21.5	13
Canada	5.3	3.2	0.6	4.6	3½	10.0	10.0	- 5.4	7½	6
Japan	9.6	- 1.3	2.4	6.3	5½	14.9	- 0.7	- 13.5	11.5	8½
Other developed countries (excluded EEC)	6.0	3.7	0.3	2½	2½	8.9	11	- 8	6	4
Total developed countries (excluded EEC)	4.6	- 0.4	- 0.5	5½	4½	9.2	3½	- 10	12½	8
Community	4.8	1.7	- 1.8	4.6	3.0	10.3	- 1½	- 5	14	4½
Total developed countries (included EEC)	4.7	0.3	- 1.0	5.2	4	9.8	1	- 7½	13	6½
OPEC countries						7.4	38	43	16	16
Other developing countries							13	- 4	3	6
Centrally planned economies						8.4	10	6	4	4
World (excluded EEC)						8.6	9	- 3½	9	7½
World (included EEC)						9.2	5	- 4	10½	6½

¹ See Annex for definitions of zones

² Gross national product for United States, Canada and Japan.

³ Geometric mean of annual changes from 1968 to 1973.

Sources: National statistics and Commission's Departments

8.3% in April. Private consumption, which had been a major expansionary factor at the beginning of 1976, is now steady at a fairly high level. The other components of domestic demand, in particular investment by firms, have remained sluggish, with the exception of residential construction. After falling at the end of last year, exports staged a modest recovery at the beginning of this year; however, both imports and the trade deficit have continued to grow. Inflation, which had eased during 1976 mainly because wage costs were rising less sharply, was given a further stimulus at the beginning of the year by sharp rises in the prices of agricultural products. Between December and April, therefore, consumer prices increased by 11% on an annual basis.

In *Japan*, GNP expanded very slowly until the end of 1976. However, signs of a consolidation of the upswing then became discernible: between the fourth quarter of 1976 and the first quarter of 1977, GNP grew in volume terms by 10% on an annual basis, but has since shown a clearly more moderate growth. Most components of domestic demand have, in fact, remained sluggish. During the last few months, only general government investment has stimulated growth: in November 1976 and in May 1977, the Government introduced expansionary measures including notably, the stepping up of public investment, which had declined during the summer. On the other hand, private consumption, which had been a major factor in promoting expansion at the beginning of 1976, has slowed down owing to the weak growth of real disposable income. Furthermore, capital formation in the private sector — with the exception of investment in residential construction — has remained weak. The high level of stocks has also helped to curb the growth of industrial production. Exports, on the other hand, have continued to grow steadily, and with imports expanding very slowly, the trade surplus has continued to increase. Wholesale prices have remained steady owing to the easing-off of domestic demand and the appreciation of the yen, which has partly absorbed increases in import prices; consumer prices were particularly affected by the cold spell which sharply increased prices of foodstuffs during the winter. Between December and April, the rise was 8%, on an annual basis.

Although, in the *other developed countries* outside the Community, 1976 was a year of renewed economic expansion (real GNP having increased, taking all these countries together, by 2½% compared with ½% in 1975), the upturn was fairly slow and, generally speaking, tended to decelerate from the summer onwards. The main cause of this slowdown was the ending of the restocking process, which was not succeeded by a sufficiently vigorous upturn in fixed investment by firms. Furthermore, many countries, such as Australia, adopted a cautious economic policy in order to contain inflation and not to aggravate their current external payments positions. In April, the Scandinavian countries, Norway, Sweden and Denmark, jointly devalued their currencies against the German mark, in order to improve competitive positions which had deteriorated sharply, especially in Sweden, owing to increasing domestic costs. Finland followed suit shortly after.

2. The inconsistent world economic outlook

Between now and the end of the year, world *economic activity* will probably continue to expand at a rate, close

to the long term rate of 4½%. In the United States, growth will depend more on business investment, and because of the implementation of the reflationary programme for fiscal 1977-78, on public expenditure. Moreover, it is expected that in the countries which have adopted demand support measures, such as Japan and to a lesser extent Canada, the recovery in output will be maintained. However, economic growth will on the whole be limited in scale, since most of the industrialized countries are still concerned to avoid fuelling inflation. Unless a large number of industrialized countries run into additional difficulties in financing their balance of payments deficits, there is however a good prospect of rather firmer expansion towards the end of the year. Overall, the rise in the gross national product in real terms of the non-EEC developed countries is likely to be slightly slower in 1977 than in 1976, the increase being estimated at some 4½% as against 5½% last year.¹ Estimates which are still tentative put growth in 1978 at approximately 5%.

In 1977 the *South European* non-member countries will probably see their economic activity expand at a rate near to that recorded in 1976. In Greece, the growth forecast will be export-led, while in Portugal heavy building and construction demand and public investment will be the main demand components. Spain's expansion will probably continue to fall distinctly short of its earlier performances, which averaged 6.6% per annum for the period 1965-1974; a slightly more buoyant export trend should, however, produce a slightly faster rise in activity in 1977.

TABLE 5

Mediterranean countries
Gross national product (volume)
(% change on preceding year)

	1975	1976	1977
Spain	0.8	2	2
Greece	4.0	6	5½
Portugal	- 2.7	5	5

The upward movement of raw materials *prices* has recently shown signs of slackening and, in the absence of speculation or monetary disruption, these signs should be confirmed during the next few months. Stocks of the main industrial raw materials are high at present and world demand in general will remain moderate. As far as the prices of several agricultural commodities are concerned, the production outlook looks promising: however, the establishment of minimum guide prices in certain producer countries, such as in the United States for cereals, or increased local pressures on prices, might well encourage the overall upward tendency to persist. In most of the industrialized countries the upward movement of wages should continue to slacken and the increases in wage costs are likely to remain slow. Lastly, the decision of the OPEC countries, other than Saudi Arabia and the United Arab Emirates, not to increase again the price of

¹ See Table 4.

TABLE 6

Balance on current account of main countries and groups of countries ¹

('000 million US \$)

	1975	1976	1977
United States	11.7	— 0.6	— 11½
Canada	— 4.9	— 4.5	— 4
Japan	— 0.7	3.7	6½
Other developed countries (excluded Community)	— 14.3	— 16.8	— 17
Total developed countries (excluded Community)	— 8.2	— 18.2	— 26
Community	1.7	— 8.1	± 0
Total developed countries (included Community)	— 6½	— 26½	— 26
OPEC countries	34	43	42
Other developing countries	— 33	— 22	— 21
Others (centrally planned economies, errors and omissions)	— 5½	— 5½	— 5

¹ Including official transfers

Sources: National statistics and estimates of Commission's Departments.

oil in July should have a favourable effect. However, it is to be expected that inflationary factors which had already been at work since autumn 1976 will continue to force up prices during the months ahead, so that in several countries the deceleration in the upward movement of domestic prices can only be slow.

In the second half of the year, the volume of *world trade* should rise at a relatively fast rate. In the industrialized countries outside the Community, and in the United States more particularly, imports should continue to expand during the next few months, and, for the year as a whole, should thus reach some 8%, in volume. However, imports by the OPEC countries could well accelerate slightly compared with the first six months: their income has been increased both by the price rises introduced at the beginning of the year and by a higher volume of production. Within the group of non-oil producing developing countries, the situation seems to vary considerably from country to country; some of them have enjoyed an increase in income owing to rises in the prices

of certain commodities. Others are still heavily burdened by their external deficits. Nevertheless, their reserves have increased, and these countries together could well step up their purchases more than in 1976. Lastly, the expansion of purchases by the centrally planned economies will probably remain sluggish.

In general, the rate of increase of world trade, for the year as a whole, excluding the Community, will probably fall short of the 1976 figure (approximately 7½% as against 9%). By comparison, imports by the Community (including intra-Community trade) will probably register a significantly slower expansion; thus, the rate of increase of world trade, including the Community, could well be in the region of 6½% in volume, as against 10½% in 1976. ¹ If, as forecast, the growth of the world economy in 1978 is still maintained, the rate of increase of world trade could well remain close the rate anticipated for this year.

¹ See Table 4

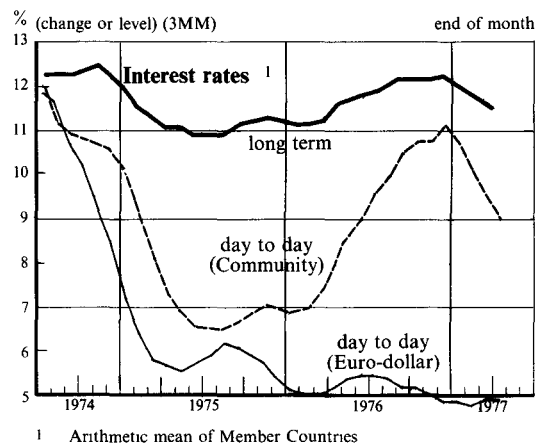
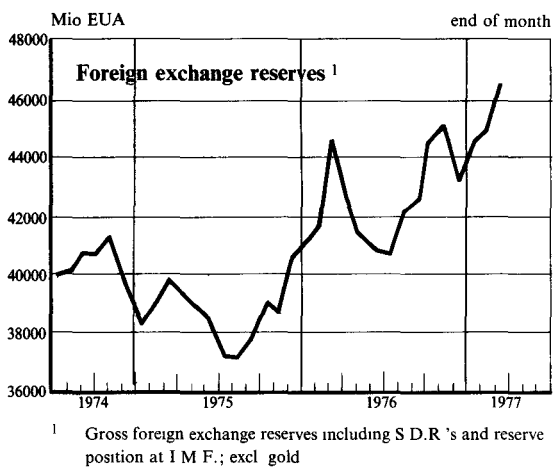
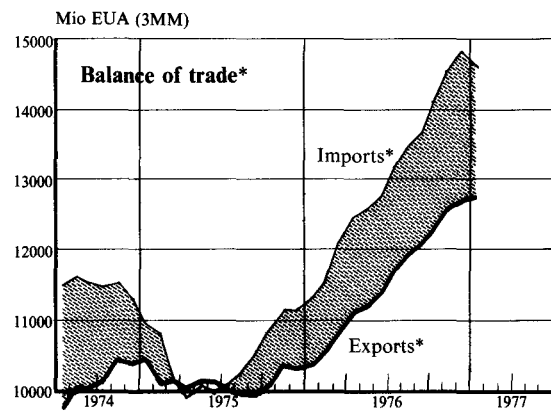
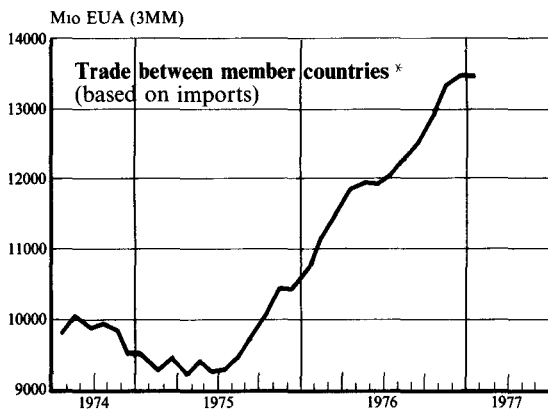
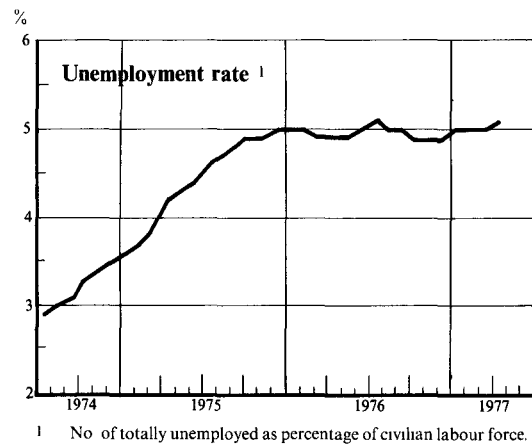
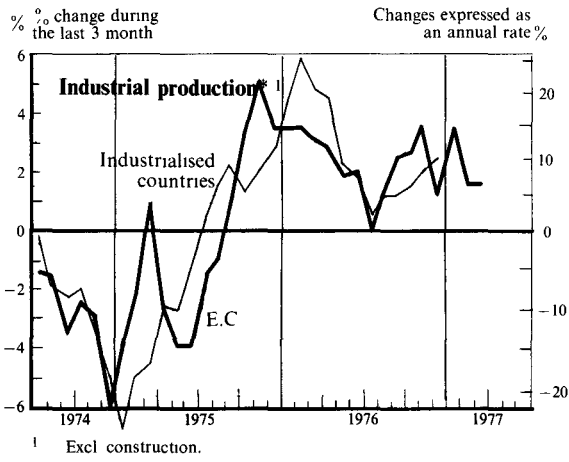
C — The economic situation in the Community

1. Recent developments

The phase of faster economic growth in the Community, following the period of generally moderate expansion which has lasted from spring to autumn of last year, proved relatively short-lived. The fact that since the beginning of the year the upturn has varied increasingly in nature, both on the sectorial and geographical planes, has tended to dampen economic activity in general. The margin of unused technical resources has, therefore, remained substantial in all member countries and the

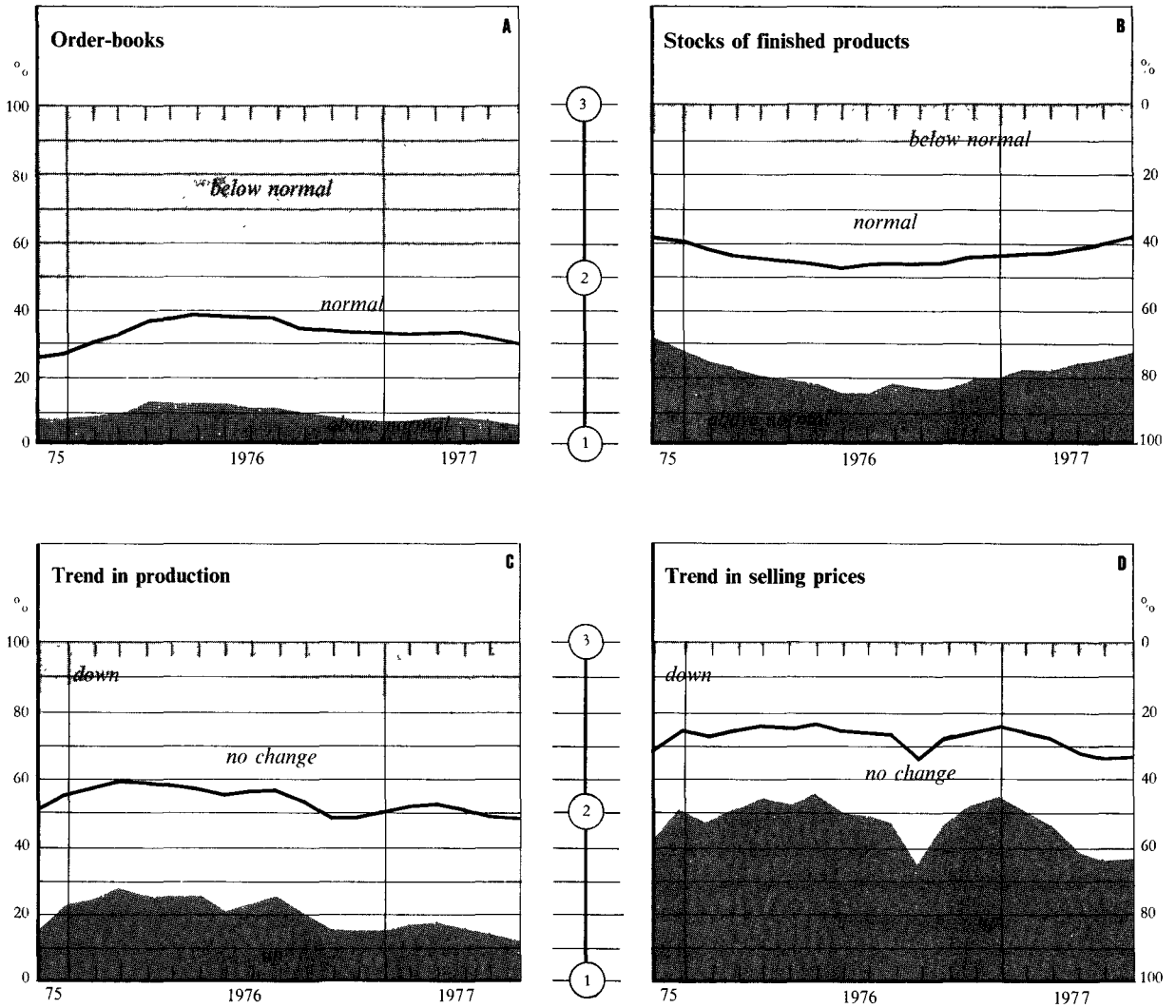
unemployment rate for the Community as a whole has remained high.

The recovery has lacked vigour because of a number of factors: the fact that the cyclical expansion of world trade has been less marked than usual, the slowness with which the confidence of economic agents, and particularly heads of enterprises, has been reestablished, a less rapid growth of real household disposable income and, finally, the fact that, in most cases, the authorities pursued a more cautious approach in respect of budgetary and monetary



*: Seasonally adjusted figures.
 3MM: Three month moving average.
 Source: services of the Commission.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



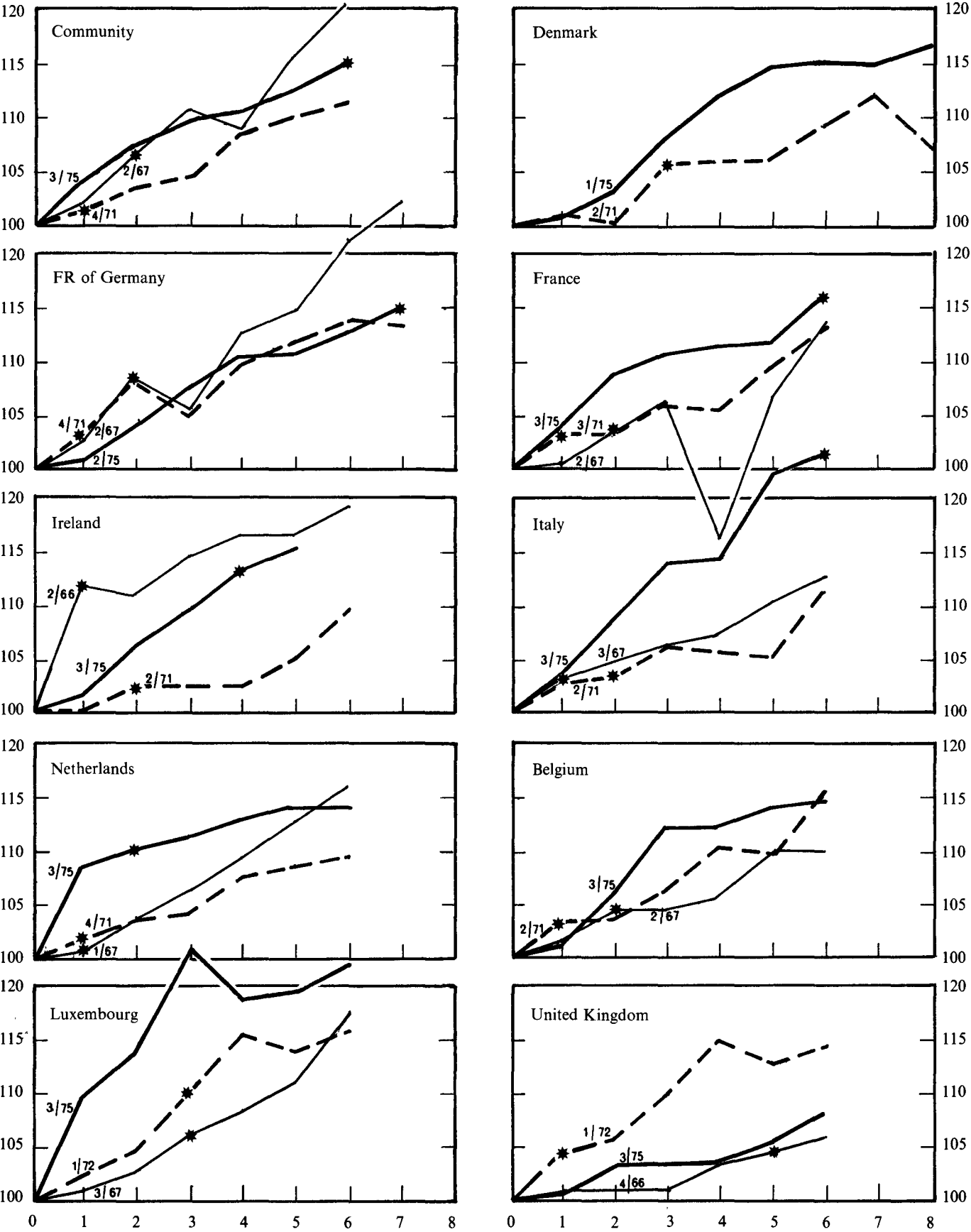
Answers to questions in the EEC business survey, carried out in the countries of the original Community, Ireland and, for "Trend in production" the United Kingdom.

GRAPHS A, B, C and D: The three zones (grey, white and black) show the percentages of the three different answers.

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

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

Comparison of periods of recovery of industrial output
Quarterly development (lowest cyclical point = 100)



The sign * indicates the point at which the previous maximum level has been reached or exceeded. Data are seasonally adjusted by EUROSTAT.
Source: Commission's departments.

policy. In spite of the fact the exchange markets have not been unsettled since the end of last year and that industrial labour costs have increased only slowly in most countries, external or fortuitous factors (sharply rising world prices, unfavourable climatic conditions) have exerted greater pressure on domestic prices, which have risen more rapidly since the autumn. The differing trends in Member States have led to a reduction of external disequilibria which, however, should not be seen as being the long term readjustment required on the balance of payments front.

(a) *The lack of buoyancy in the economy has created difficulties in the labour market*

After showing some improvement at the beginning of the year, domestic supply in the Community again slackened. According to the underlying trend, real gross domestic product for the Community taken as a whole has been rising at about 3% on an annual basis in the first half of 1977, as compared with some 3½% in the second half of 1976. In industry, orders have generally remained at a fairly low level, and a growing number of managements

have reported stocks of finished products as being above normal. Since early in 1977, when it passed the level reached before the recession, the rate of growth of industrial production in the Community has slackened appreciably.¹ During the first four months of 1977, the underlying trend of activity in Community industry has increased at an annual rate of about 6%, as against 10½% for the last four months of 1976. In April, the year-to-year increase was only 5½%. Taking the Community as a whole, the rate of physical capacity utilization in industry has stopped increasing since the beginning of the year: in the spring, it was about 79%, whereas it had reached about 86% at the peak of the earlier boom period, in 1973.

Industrial production trends have continued to vary widely. The weakening of growth factors in the Federal Republic of Germany,² Denmark, Italy and France, has contrasted with a trend towards expansion, though of a

¹ See Graph C and Table 7

² Recent changes in statistical methods may have distorted the index for this country.

TABLE 7
Industrial production
(% change on preceding period)

(Seasonally-adjusted figures)

	1973	1974	1975	1976	1975		1976				1977				April 1976 April 1977	
					III	IV	I	II	III	IV	I	Jan.	Feb	Mar		Apr.
Denmark			- 5.8	10.9	2.2	4.9	3.7	2.3	0.4	- 0.2	1.2	- 1.7	- 1.9	- 6.3		
FR of Germany	7.9	- 1.1	- 7.2	7.9	0.3	4.3	2.8	2.4	0.4	1.6	2.1	5.9	- 1.7	- 0.8		
France	7.3	3.3	- 8.1	- 8.6	- 1.0	3.7	4.8	1.5	0.6	0.6	3.6	3.5	- 0.8	1.2	- 2.2	3.1
Ireland	10.3	3.0	- 6.7	10.1	- 0.6	1.5	4.8	3.0	3.4	1.5						
Italy	10.0	4.3	- 9.8	12.2	- 0.3	3.7	4.9	4.8	0.3	6.7	1.4	- 0.9	0.0	- 1.8	- 3.3	6.3
Netherlands	6.1	3.4	- 5.0	7.9	- 2.0	8.4	1.9	1.0	1.3	1.1	+ 0.1	- 0.5	- 2.4	- 0.2	2.3	4.1
Belgium	6.3	4.0	- 10.4	8.7	- 1.0	1.5	4.9	5.3	0.1	1.7	0.4	4.8	- 1.2	- 0.1	1.5	2.9
Luxembourg	12.0	3.8	- 22.9	6.6	- 10.0	9.9	3.7	8.2	- 3.5	0.4	2.3	7.2	- 5.4	6.0	- 2.8	2.7
United Kingdom	8.8	- 3.1	- 4.8	1.7	- 0.6	0.8	2.6	0.2	0.0	1.8	2.7	1.8	+ 0.6	- 1.5	- 0.2	3.6
Community	7.7	0.6	- 7.3	7.7	- 0.5	3.9	3.4	2.2	0.5	2.0	2.4	3.1	- 1.0	- 0.4	0.4	5.4
Investment goods	6.6	2.5	- 3.9	1.9	- 1.0	1.4	0.9	1.6	- 0.5	1.7	2.9	4.9	0.0	0.2	1.1	6.6
Consumer goods	7.3	- 0.6	- 4.8	7.8	2.1	2.1	2.5	3.0	0.7	3.2	1.4	3.1	- 1.5	- 0.0	1.2	6.3
Intermediate goods	9.0	0.5	- 10.8	10.3	- 1.7	5.8	5.2	2.2	1.3	2.0	2.5	1.7	- 1.2	- 0.8	- 0.3	5.3

Source: EUROSTAT.

very moderate order, in the United Kingdom and the Benelux countries. Only in Ireland has activity been growing strongly. Furthermore, trends have again differed greatly from one industrial sector to another. Production has continued to increase in the consumer durables industry, although the pace has slackened appreciably. The production of private cars increased by about 7½%, on a year-to-year basis, during the first four months of 1977. Production of capital goods has shown a slight upturn since the beginning of the year. On the other hand activity has even tended to decline in the basic materials and producer goods industries, mainly as a result of the cautious attitude of managements towards stockbuilding. The low level of output in the steel industry

(down 4% in January/May on a year-to-year comparison) has contrasted with continuing — though somewhat slower — expansion in other industries, including chemicals. Finally, signs of weakness have again been in evidence, in the first half of 1977, in the building and construction industry, owing in particular to a continued decline in building authorizations for dwellings.

The increase in domestic production has again been largely attributable to the improved productivity of persons in employment, reflected in an increase in the number of hours worked. Since this development has been accompanied by an increase in the active population

TABLE 8

Unemployment
Unemployment rates ¹ since 1973

Country	1973	1974	1975	1976	1975		1976				1977		
	Annual average				III	IV	I	II	III	IV	I	April	May
Denmark	1.0	2.1	5.2	4.9	5.4	5.3	5.1	4.8	4.9	4.8	5.6	5.9	5.8
FR of Germany	1.0	2.2	4.2	4.0	4.5	4.4	4.5	4.0	4.0	3.8	3.8	3.8	3.8
France	1.8	2.2	3.8	4.2	3.9	4.4	4.3	4.2	4.1	4.3	4.3	4.5	4.6
Ireland	5.9	6.2	8.7	9.8	9.1	9.4	9.6	9.8	10.0	9.8	9.6	9.6	9.5
Italy	5.3	5.1	5.7	6.0	5.9	6.0	5.9	6.0	6.1	6.1	6.3	6.5	6.5
Netherlands	2.4	2.7	4.1	4.4	4.3	4.4	4.4	4.3	4.5	4.3	4.0	4.0	4.1
Belgium	2.9	3.1	5.2	6.7	5.8	6.3	6.3	6.6	7.0	7.1	7.1	7.2	7.4
Luxembourg	—	0.0	0.2	0.3	0.1	0.4	0.3	0.3	0.4	0.4	0.5	0.5	0.5
United Kingdom	2.5	2.3	3.8	5.3	4.1	4.8	4.9	5.2	5.7	5.5	5.4	5.4	5.3
Community	2.5	2.9	4.4	5.0	4.7	4.9	5.0	4.9	5.1	4.9	5.0	5.1	5.1

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

Source: EUROSTAT and departments of the Commission

greater than in 1976, the employment situation has remained disturbing in the first half of 1977. The number of wage- and salary-earners has ceased to decline in most Member States, principally because of a slightly more favourable trend in the services sector. However, the number of employees in industry and the building sector has probably continued to fall, although there has been a slight improvement in some branches, such as the car and electrical engineering industries.

Taking the Community as a whole and excluding seasonal variations, the rate of unemployment (calculated as the number of wholly unemployed as a proportion of the civilian working population) has remained high. In May, it reached about 5.1% (as against 4.9% a year earlier),¹ while the number of wholly unemployed totalled some 5.4 million (as against 5.2 million in May 1976). Further-

more, the seasonally-adjusted number of vacancies has been weak in all Member States. The tendency for the numbers on short time to decline, which began in 1976, is also no longer discernible, mainly as a result of the continuing crisis in the steel industry. Of the total number of unemployed, the proportion of workers with few skills continues to increase. In April, the number of unemployed women as a proportion of the total easily exceeded 40%; whereas the corresponding figures in 1975 and 1976 had been 35.1% and 37.8% respectively. On the other hand, the number of young people unemployed has fallen in most countries, as a result, particularly, of the specific measures taken by the authorities. The entry of school-leavers into the labour market has continued to raise

¹ See Table 8.

TABLE 9

Employment and productivity
(Percentage change on preceding year)

Country	Wage and salary earners			Productivity (GDP, in volume, per wage and salary earner)		
	1975	1976	1977	1975	1976	1977
Denmark	- 4	2.0	- 0.9	1.3	2.7	2.3
FR of Germany	- 3.3	- 0.7	0.2	0.7	6.5	3.6
France	- 1.3	0	- 0.3	0.7	5.2	3.4
Ireland	:	:	:	- 5	:	:
Italy	1.3	1.1	1	- 4.7	4.4	1.8
Netherlands	- 0.7	- 0.3	0.7	- 0.4	3.7	3.3
Belgium	- 1.4	- 1.5	0.3	- 0.7	4.6	3.2
Luxembourg	0.7	- 1.4	- 0.6	- 0.9	4.5	2.6
United Kingdom	- 0.6	- 0.8	- 0.4	- 1.1	2.6	1.2
Community	- 1.2	- 0.2	0.1	- 0.8	4.9	2.9

Source: Estimates by the departments of the Commission

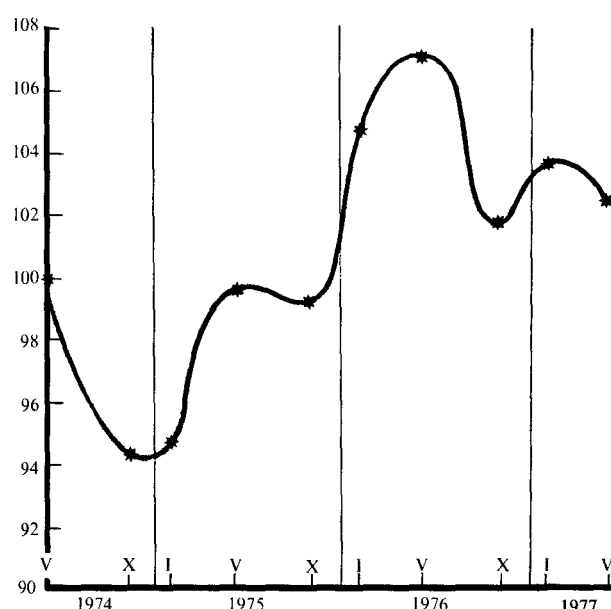
difficult quantitative and qualitative problems, as the jobs offered do not always correspond to the vocational training undergone by those seeking employment.

(b) *Strong inflationary pressures have continued despite slacker demand*

The growth of internal demand has tended to slacken again in the first half of 1977. Its rate of expansion has thus remained slower than experienced at the beginning of the recovery phase at the end of 1975 and in early 1976. The slowdown is partly the result of the stabilization programme implemented by some member countries and is also due to a spontaneous weakening of expansionary factors.

Stock changes have tended to inhibit economic activity during the last few months. Most managements now report stock levels as normal, or even slightly above normal, and this not only at factory level but also in the distribution sector. In addition, *private consumption*, which had been a major force behind the recovery — and which, in some countries, is again tending to expand more steadily towards the end of 1976 — has slackened, mainly because real disposable income has been growing more slowly but also, in some cases, because the savings ratio has stopped declining.¹ The growth of total compensation of employees is still being curbed by the relatively slow rise in take-home earnings and transfer income. Furthermore, in real terms, personal disposable income has generally been held in check by the more rapid rise in consumer prices noted since last summer. In the United Kingdom there has been an appreciable fall in consumption in volume terms since the final months of last year. In France, household expenditure has grown only slightly following the marked increase during the price freeze at the end of last year. The same applies to the Federal Republic of Germany and, to a lesser degree, to the Netherlands, although, in these countries, moderate increases in households' purchasing power have continued to accrue. Generally speaking, the slackening of

Index of European consumer's confidence



The index of European consumer's 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.

private consumption has curbed sales of durable goods. Nevertheless, taking the Community as a whole, the number of new car registrations in the first four months of 1977 was 5½% up on the corresponding figure for the preceding year.

¹ See Graph D.

TABLE 10
Consumer prices

Country	% change on preceding period														May 1976 May 1977
	1973	1974	1975	1976	1975		1976				1977				
					III	IV	I	II	III	IV	I	April	May		
Denmark	9.3	15.3	9.6	9.0	1.8	-0.7	3.1	4.0	1.5	3.9	2.3	1.0	1.5	9.9	
FR of Germany	7.0	7.0	5.9	4.6	0.8	0.9	1.7	1.5	0.1	0.5	1.9	0.5	0.4	3.8	
France	7.3	13.6	11.7	9.6	2.2	2.2	2.4	2.3	2.3	2.6	1.6	1.3	0.9	9.8	
Ireland ¹	11.3	17.0	20.9	17.9	-0.8	2.7	7.3	6.3	1.5	4.2	3.8		3.8	13.9	
Italy	10.8	19.2	17.0	16.7	1.9	2.9	4.2	6.3	2.8	6.4	4.7	1.1	1.3	18.5	
Netherlands	8.1	9.8	9.9	8.9	1.9	2.3	1.7	3.4	0.7	2.5	0.7	1.7	0.5	7.0	
Belgium	6.1	12.7	12.8	9.2	2.3	2.9	2.1	2.0	1.9	1.7	2.0	0.5	1.0	7.2	
Luxembourg	6.1	9.5	10.8	9.8	2.1	3.0	2.5	2.3	1.6	1.8	2.3	0.6	0.4	7.2	
United Kingdom	9.2	16.0	24.2	16.5	4.4	3.5	3.6	3.7	2.3	4.6	5.0	2.6	0.8	17.1	
Community	8.2	13.0	13.4	11.0	2.2	2.2	2.7	3.1	1.6	3.0	2.9	1.3	0.8	10.7	

¹ Quarterly indices
Source: EUROSTAT

The *investment* climate has remained sluggish in the first half of 1977. Managements have again been reluctant to add to capacity, despite the improvement in their finances. Nevertheless, in the last few months replacement and rationalization investment demand in industry has picked up a little, particularly in the United Kingdom, Italy and the Benelux countries. However, in the Federal Republic of Germany, the slight improvement in the underlying trend noted since 1975 seems to have weakened. As regards public investment, in particular public works, the increase in budgetary expenditure during the first half of the year has probably been accompanied by a further decline in real terms. Investment in housing, which has been declining throughout the Community since the spring of 1976, will probably continue to fall.

Taking the Community as a whole, the rise in *consumer prices* has become more rapid since last summer: in the period from October to April, it was running at 13% on an annual basis.¹ Furthermore, the wide range of inflation rates from country to country has persisted: during the period in question, the cost of living in the Federal Republic of Germany increased by 6% on an annual basis, while in Italy and the United Kingdom the corresponding rates were 19½% and 21½% respectively. Generally speaking, prices of foodstuffs have been under considerable pressure, following the sharp rise in the world prices of products such as coffee, tea and cocoa and the repercussions of last year's drought affecting many vegetable products of Community origin. The prices of services, rents and public sector charges in particular, have also increased more sharply, sometimes as a direct result of stabilization programmes designed to restrain budget deficits. This is true of the increases in the prices of petrol and public sector charges in France and Italy at the end of 1976 and beginning of 1977, and of the heavier direct taxation of luxury goods in several other countries. The increases in the prices of manufactures, at the point of consumption, have frequently been relatively small, owing, in particular, to the moderate upward pressure of wage costs, which is reflected also in the generally rather slow rise in wholesale prices. But the situation has varied from one country to the next, partly as a result of the differing impact of dearer imported raw materials, especially oil.

(c) *The slower growth of imports and the persistent growth of exports to non-member countries have led to an improvement in the external account*

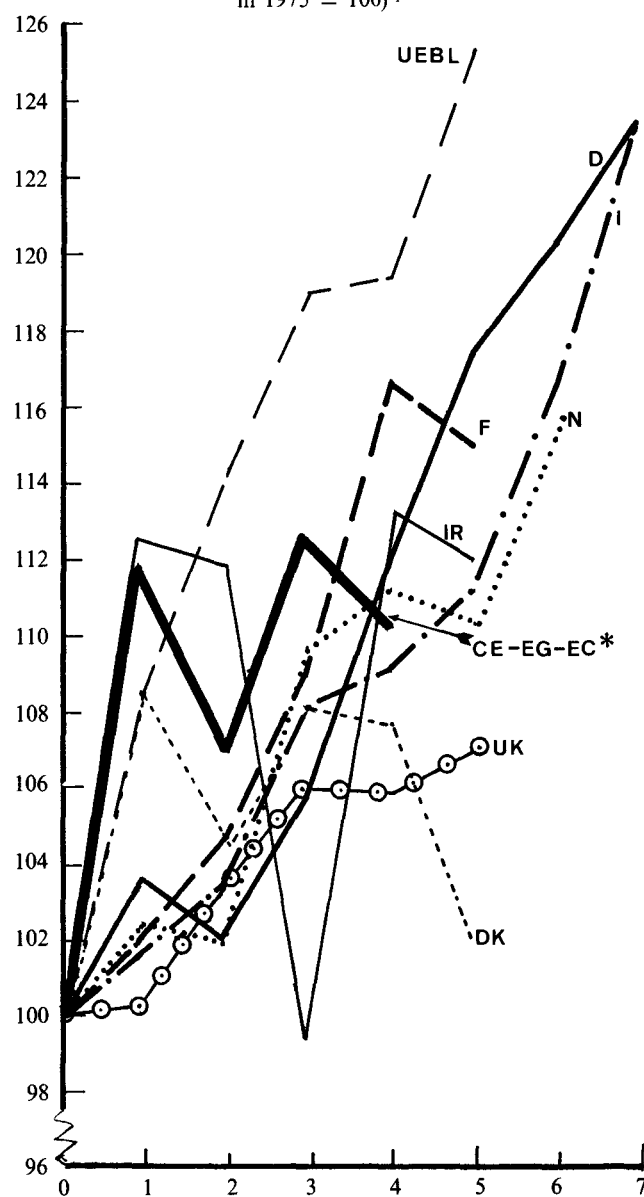
Following a period of slow growth lasting until the summer of last year, Community *exports* to non-member countries have begun to expand slightly more steadily again.² Sales by the Federal Republic of Germany have risen only a little above the high level reached in the third quarter of 1976, but the rate of growth of exports has gathered a little momentum in other Member States, notably in Ireland and the United Kingdom. Generally speaking, most progress has been made in deliveries to non-member industrialized countries, particularly European non-member countries. Exports to oil-producing countries have expanded slowly, except in the case of the United Kingdom whose sales on these markets have

increased particularly rapidly. Although deliveries to State-trading countries have remained limited, exports to non-oil-producing developing countries have shown increasingly clear signs of recovery. Exports of capital goods from the Federal Republic of Germany have expanded steadily. Most countries have increased their exports of consumer goods more than anything else; car sales in France, for example, have climbed sharply.

GRAPH E

Quarterly development of exports in volume terms

(The lowest cyclical point observed in 1975 = 100)¹



* Exports to non-member countries.

¹ Data seasonally adjusted by EUROSTAT. To determine the lowest cyclical point, refer to graph C.

Source: Commission's departments.

¹ See Table 10.

² See Graph E.

TABLE II
Balance of trade

(Seasonally adjusted, US \$ million)

Country	1973	1974	1975	1976	1975				1976				1977		
					I	II	III	IV	I	II	III	IV	I	at quarterly rates	
														March	April
Denmark	- 1 584	- 2 306	- 1 348	- 3 188	- 230	- 192	- 371	- 555	- 663	- 726	- 819	- 981	- 835	- 1 002	- 567
FR of Germany	12 976	20 260	15 448	12 994	4 758	4 257	3 302	3 131	3 075	3 131	3 314	3 473	3 451	4 250	3 765
France	- 1 428	- 7 141	- 1 894	- 8 291	- 609	91	- 174	- 1 202	- 1 460	- 1 480	- 2 400	- 2 951	- 2 518	- 2 635	- 1 928
Ireland	- 684	- 1 211	- 609	- 857	- 234	- 154	- 88	- 132	- 274	- 163	- 207	- 214	- 332	- 336	- 247
Italy	- 5 661	- 11 042	- 3 161	- 6 216	- 787	- 598	- 509	- 1 266	- 1 370	- 1 747	- 1 179	- 1 920	- 1 510	- 1 462	- 1 362
Netherlands	- 431	- 145	- 745	- 1 170	- 404	- 89	- 190	- 61	- 122	- 598	- 241	- 453	- 671	- 498	:
BLEU	362	- 1 631	- 894	- 717	231	- 321	- 449	- 355	- 212	- 243	- 209	- 52	- 345	- 127	- 483
United Kingdom	- 8 555	- 15 985	- 9 642	- 9 370	- 2 824	- 2 301	- 2 623	- 1 895	- 1 617	- 2 395	- 2 635	- 2 723	- 2 331	- 2 211	- 1 697
Community ¹	- 4 592	- 20 549	- 4 504	- 19 476	- 827	451	- 1 344	- 2 784	- 3 321	- 4 784	- 5 071	- 6 299	- 5 904	- 4 465	:

¹ Community - Extra-Community trade
Source: EUROSTAT and departments of the Commission

Imports from non-member countries have tended to level out since the autumn of 1976; indeed, in the Federal Republic of Germany, imports from the United States and from OPEC countries have actually declined. In France and especially in the United Kingdom, whose oil imports have fallen appreciably, imports from non-member countries generally have tended to decline.

Owing to the slower expansion of imports, but also because of a more sustained growth of exports, the Community's *trade deficit* (which had been at a record high level at the end of last year) has definitely tended to contract, ¹ although the terms of trade have swung a little against the Community. France and the United Kingdom, in particular, have achieved an appreciable improvement in their trade balances. In Italy, the non-oil trade balance has remained in surplus. In the Federal Republic of Germany, on the other hand, a tendency towards a reduction of the trade surplus seems to have got under way.

Although *intra-Community trade* has regained some buoyancy after the pause last summer, its rate of expansion — taking the Community as a whole — has slowed down since the beginning of the year. Thus, in France, Italy and the United Kingdom the fairly rapid growth of imports from other member countries in the fourth quarter of 1976 slackened in the following months. Imports by the Federal Republic of Germany from its Community partners have remained close to the rather high level reached at the end of last year. As regards exports, France in particular has made appreciable progress in its deliveries to other member countries.

2. Slow improvement in the monetary and financial situation

Generally speaking, economic policy pursued in the Community during the first half of 1977 can be considered, on balance, as neutral, from a conjunctural viewpoint. Although the slow pace of expansion has at times prompted the authorities to strengthen selective action to boost activity, they have generally preferred, given their partial success in curbing inflation and reducing balance-of-payments disequilibria, to maintain their overall stabilization policies. In the Member States

where disequilibria are most acute, prices and incomes policies have tended to play a greater role and the authorities have, with varying degrees of success, tried to ensure the collaboration of both sides of industry.

The unsettled conditions on *foreign exchange markets* last autumn have not persisted and fluctuations in the exchange rates of the Community currencies have remained within relatively narrow limits. ² Within the Community exchange rate scheme, it proved possible to adjust the official rates for the Danish krone (−3%), the Norwegian krone (−3%) and the Swedish krona (−6%), with effect from 4 April, to reflect respective balance-of-payments developments without any prior disruption of the exchanges. In April and May, there was occasional upward pressure on the guilder to which the Netherlands Central Bank responded by lowering interest rates. The United Kingdom monetary authorities in the framework of policy aimed at stabilizing exchange rates, undertook substantial purchases of foreign currency on the exchanges. This, coupled with borrowing abroad, boosted the United Kingdom's exchange reserves, which rose by US \$ 7 500 million in the first half year to reach US \$ 11 500 million in June. As for the lira, since the surcharge and deposit requirements in respect of purchases of foreign exchange were abolished on schedule, this currency has held steady, thanks partly to credit made available by the Community and by the International Monetary Fund, to the economic-policy undertakings entered into for this purpose by the Italian authorities and to the growth of the external debt of the banks.

The easing of strain on foreign exchange markets since last autumn has led to a relaxation of *interest-rate policies*. Discount rates have been lowered since the beginning of the year in all Member States, except France and the Federal Republic of Germany. Belgium, however, increased its rediscount quotas in January and the Federal Republic of Germany followed suit in March and again in May. The decline in interest rates was particularly marked in the United Kingdom; to stem the decline, the Bank of England on more than one occasion

¹ See Table 11.

² See Graph F.

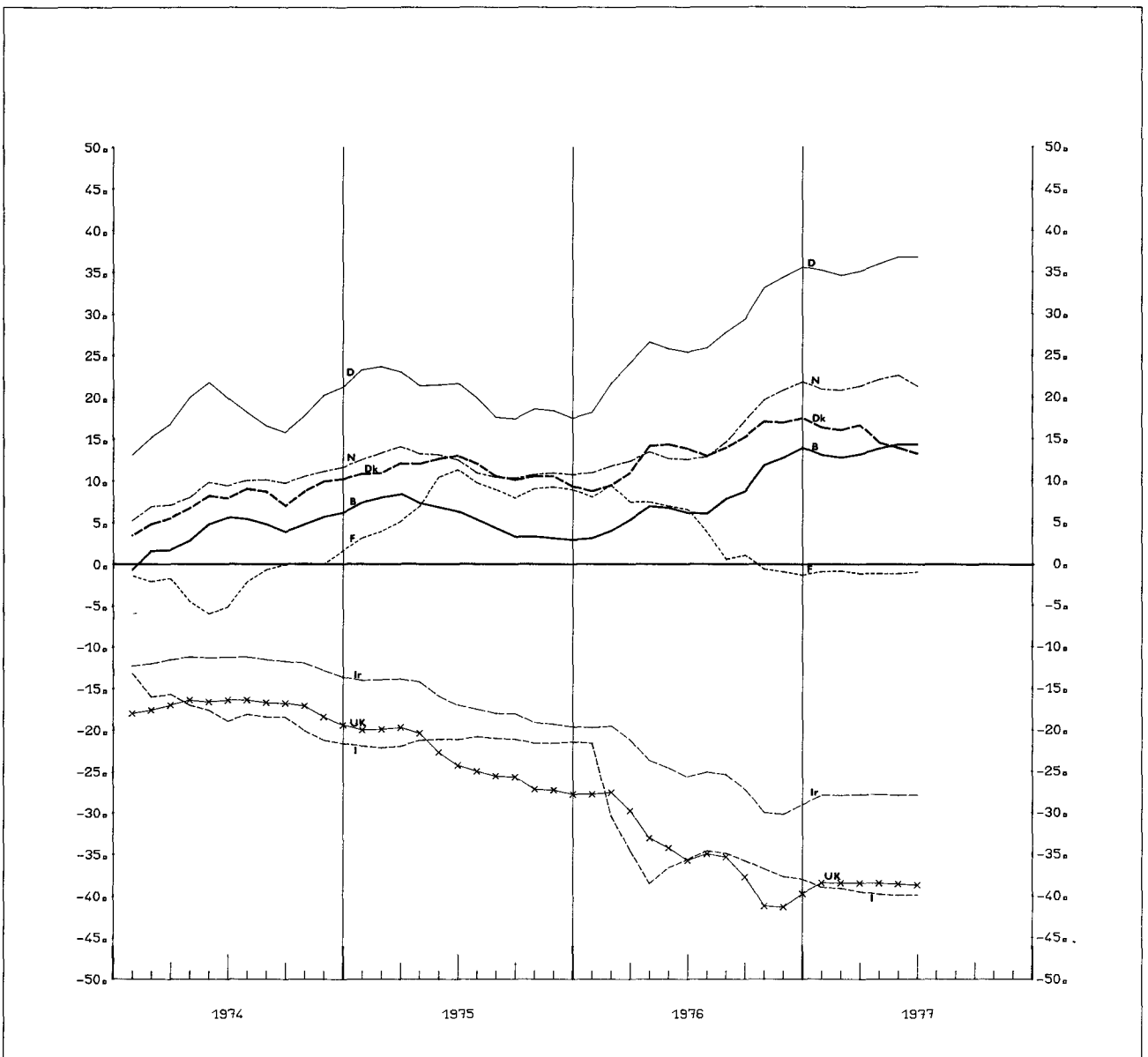
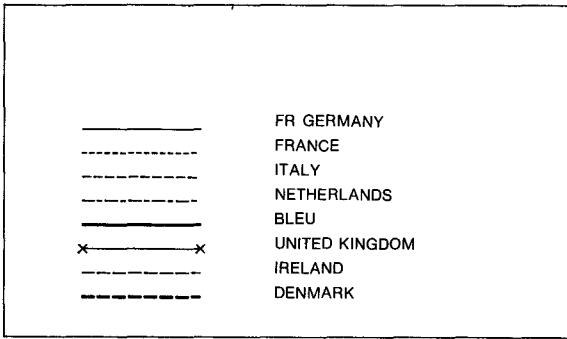
TABLE 12
Long-term interest rates
(Government stock)

	December				1977 (last month for which figures available)
	1970	1973	1975	1976	
FR of Germany	8.2	9.7	8.3	7.3	6.2
France	7.9	9.1	8.9	9.7	9.9
Italy	7.9	7.1	9.7	14.4	15.6
United Kingdom	9.6	12.5	14.8	15.5	12.4
United States	6.0	6.4	7.2	6.4	7.1
Euromarket	:	9.2	10.2	9.9	8.6

Source: Departments of the Commission

Exchange rates

(weighted change in % since 1st Quarter 1972;
weighting according to structure of exports)

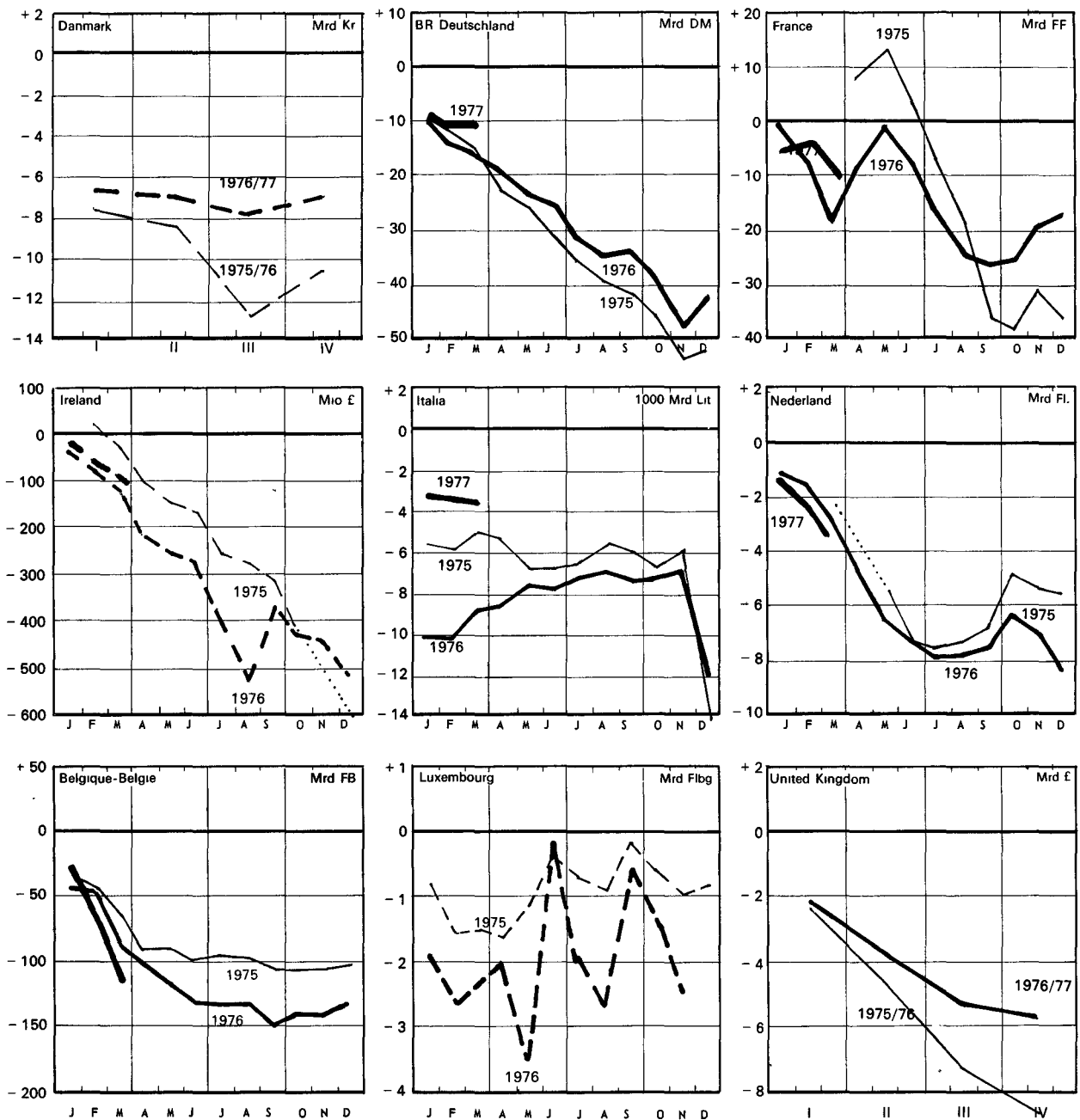


suspended the automatic link between the minimum lending rate and the average rate of discount for Treasury bills. At 8.0% in April, the average call-money rate in the Community was still above its level prior to the onset of the currency disturbances in the spring of 1976 (around 6.5% in February of that year), which followed a period during which economic policies had been on a strongly expansionary tack. The downward trend of long-term rates spread to all the member countries, except Italy and France, in the first half of 1977. The main explanations for this development, which has reduced interest rates to

their lowest level for eight years in the Federal Republic of Germany, seem to be lower capital requirements of general government, the slacker demand for long-term funds in the private sector and a more encouraging outlook with regard to inflation. The evolution of the demand for personal bank credit has differed between member countries. Although the demand for bank lending grew appreciably in a number of countries (the Netherlands, the Federal Republic of Germany and France) it remained slack elsewhere, e.g. in Italy and, at least until the spring, in the United Kingdom. In March,

GRAPH G

CENTRAL GOVERNMENT BUDGET



Budget outturn. — Cumulative figures (monthly or quarterly) Net balance. — FR Germany: Bund and Länder. — United Kingdom and Denmark: fiscal year April-March.

Source: Commission departments.

the Netherlands Central Bank imposed a quantitative ceiling on bank lending to the private sector (12.5% for 1977). The credit restrictions obtaining in Italy were extended beyond March, the maximum increase authorized until the end of March 1978 being fixed at 25%.

The *money supply* has been growing at a significantly slower rate in almost all the countries of the Community. At the beginning of the spring, the year-on-year increase of notes and coins in circulation plus sight deposits was less than 10%, except in Italy, where it was still running at some 20%. The trend of the money supply including near-money was also more moderate and less divergent between countries than a year earlier, except in Italy and, as a result of exceptional factors, in the Netherlands.

A prudent spending policy and in some countries a higher-than-forecast increase in tax revenue combined to bring about reductions in the *budget deficits* in the first

few months of 1977 exceeding the initial forecasts in several member countries, among them the Federal Republic of Germany, the United Kingdom and Ireland. ¹ The deficit in Italy behaved as expected, the effects being to pare down significantly the net borrowing requirement between 1976 and 1977. Conversely, a shortfall in tax revenue in Belgium meant a greater-than-forecast deficit.

In most member countries, especially France, the authorities used budgetary instruments in an effort to promote employment and investment by selective measures; at the same time, indirect taxes on a number of goods and services were raised in most countries, the aim being to maintain the progress made in reducing the deficits.

¹ See Graph G.

TABLE 13
Net borrowing (-) or net lending (+) by general government
(As % of GDP)

	1975	1976	1977 ¹
FR of Germany	- 5.9	- 3.7	- 3.1
France	- 2.3	- 0.8	- 0.9
Ireland	- 13.9	- 10.0	- 10.2
Italy	- 11.0	- 8.7	- 7.6
Netherlands	- 1.9	- 1.8	- 1.9
Belgium	- 3.9	- 5.3	- 5.4
Luxembourg	+ 0.2	- 0.5	- 1.0
United Kingdom	- 5.2	- 4.8	- 3.8

¹ Estimated.

Source: Departments of the Commission.

3. Prospect of further difficulties in the labour market despite a slightly more buoyant demand and production trend, but probable improvement in equilibrium during the second half of the year

Although the expansion of demand and production will probably tend to become slightly firmer in the second half of 1977, this will not be sufficient for the overall 4% growth target, set by the Council in autumn 1976, to be reached in 1977 by the Community.

Despite the general implementation of selective measures to combat unemployment, the number of unemployed could therefore increase slightly in the second half of the year. Nevertheless, against the background of an overall improvement, the differences in trend between member countries must be expected to narrow in the area of prices and the balance of payments.

Community *exports* to non-member countries will continue to rise in the second half of the year. Expansion of the principal export markets is, indeed, likely to be more buoyant than in the first half of this year. Purchases by developing countries are particularly likely to grow

more rapidly, while purchases by the EFTA countries should be boosted when the tariffs still hampering trade in most manufactured goods between these countries and the EEC are dismantled on the 1st of July. The deficit member countries have also been endeavouring to switch resources to export sales, and the overall effect is likely to be that the total volume increase in Community exports to non-member countries will be appreciably greater in 1977 than in 1976, some 8%, instead of 6%.

Private consumers' expenditure should gather a little momentum during the next few months. In the countries where the rate of inflation is expected to decelerate, rises in the household sector's purchasing power are likely to promote an increase in its demand in real terms, especially since social transfer payments in several cases will probably rise more rapidly. Moreover, in the Federal Republic of Germany, the financial resources of consumers will be improved by the repayment of the savings which had been withheld under a five-year savings scheme. In the United Kingdom, the trend of private consumer spending in volume terms is expected to pick up in the summer, mainly because of the entry into force of tax concessions linked to the continuation of a further phase

TABLE 14

Behaviour of certain major economic aggregates

Community	Unit	Average 1970-1974 ^{4 5}	1975 ⁵	1976 ⁶	1977 ⁵
Gross domestic product, in volume	change %	4.0	- 1.8	4.6	3.0
Gross domestic product per capita of the active population	change %	3.7	- 0.5	5.1	3.1
Total employment (number of persons) ¹	change %	0.3	- 1.3	- 0.5	- 0.1
Unemployment ⁶	% of active population	2.4(2.8)	4.0(4.5)	4.5(5.0)	4.8(5.3)
Income per wage and salary earner	change %	13.5	16.7	12.9	11.4
Consumer prices ²	change %	7.8	12.8	9.9	9.6
Current balance of payments		1.2	1.7	- 8.1	± 0

¹ Domestic concept

² In national accounts terms

³ Geometric average annual change between 1969 and 1974, unemployment and balance of payments arithmetic average of those five years

⁴ Source: EUROSTAT

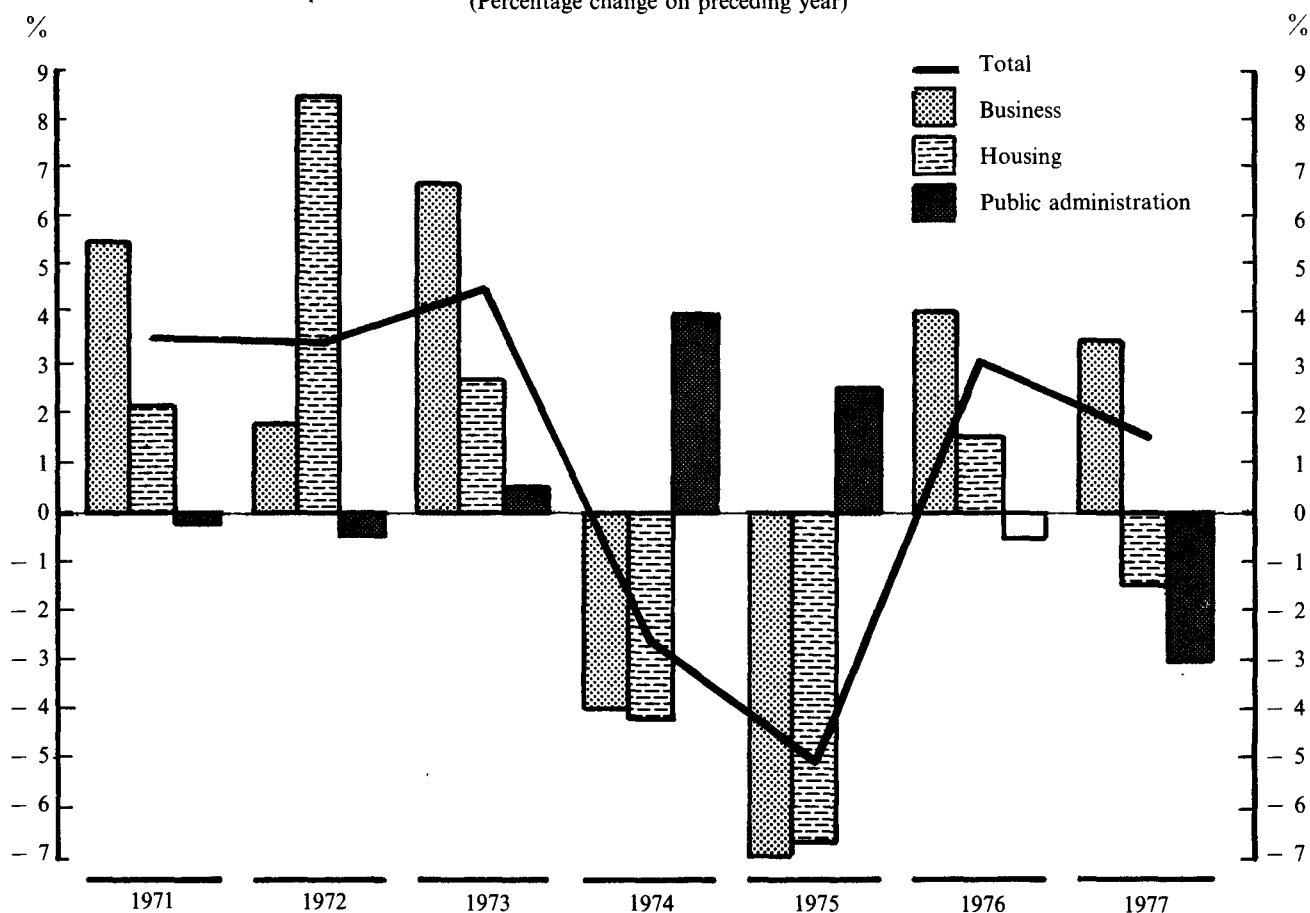
⁵ Estimates by departments of the Commission.

⁶ The unemployment rate, indicated in brackets, is that obtained using, for Italy, figures from the Labour Ministry rather than those from ISTAT

GRAPH H

Development of the volume of fixed investment in the Community

(Percentage change on preceding year)



Source: Commission's departments.

of income restraint and because of higher pensions. In other countries, however, particularly France, Italy and Denmark, the stabilization programmes now being implemented will forestall any very substantial increase in incomes and private consumption in the second half of the year.

Despite the measures which have been taken in most of the member countries to boost investment, the trend of *gross fixed asset formation* in the second half of the year will remain weak, particularly in comparison with the recovery phase of earlier business cycles. An overall decline in volume terms may even be expected in Italy and Denmark. A number of factors will again inhibit companies' propensity to invest: many firms are still working well below capacity, and the economic outlook continues to be uncertain. Thus, despite the high level of obsolete investment the underlying trend of expenditure on new equipment is not likely to improve except to a limited extent. Nevertheless, the results of the Community survey of fixed industrial investment for seven member countries suggest an improved tendency in 1977. Public investment expenditure is, in general, likely to make a major contribution to increased economic activity.¹ In the Federal Republic of Germany, however, orders for public works might well stage a recovery in the second half of the year, boosted by the recently-launched multi-annual programme under which some DM 3 500 million has been earmarked for 1977. Over the same period, judging by the trend of building permits, investment in residential construction could well continue its tendency to decline in volume. Lastly, the stimulus

provided by firms' stockbuilding will remain weak in the second half of the year.

In the second half of 1977 total *production* should recover a little of its lost vigour. However, an acceleration of overall activity at the Community level will be possible only if the effects of a strengthening of expansionary trends, foreseeable in the Federal Republic of Germany and in the United Kingdom, are not offset by the slower trend expected in other member countries and more particularly in Italy. All in all, the Community's gross domestic product for 1977 as a whole should not grow by much more than 3% in volume terms.¹ However, a slightly higher rate of growth is expected for 1978 because of the recovery which an improvement in key equilibria will make possible in some countries.

On a sectoral view, industrial production, including building, is unlikely to grow much faster than it has so far, but the trends in the services sector, and particularly in tourism, may well become more buoyant. In agriculture, the foreseeable results for the year as a whole suggest a modest recovery after production losses suffered in 1976 by all the member countries.

The foreseeable increase in economic activity in the second half of 1977 and the persistent weakness of the propensity to expand production capacities suggest that no improvement can be expected in the *Labour market*.

¹ See Graph H.

² See Table 14.

TABLE 15
Supply and use of resources

Community	1974 ²	1975 ³			1976 ³			1977 ³		
	At current prices EUA (000 million) ⁴	Percentage change from preceding year								
		Vol	Price	Val	Vol	Price	Val.	Vol	Price	Val
Private consumption	586.4	1.4	12.8	14.4	3.4	9.9	13.6	2.7	9.6	12.5
Public consumption	148.5	4.2	15.5	20.4	3.2	9.0	12.5	2.4	8.7	11.3
Gross fixed asset formation	220.2	- 4.9	11.7	6.2	2.8	9.2	12.2	1.3	8.3	9.7
Final domestic demand (excluding stock changes)	955.1	0.3	13.3	13.6	3.3	9.5	13.1	2.4	9.1	11.7
Final domestic demand (including stock changes)	968.8	.	.	.	5.1	9.7	15.3	2.2	9.1	11.5
Exports ¹	271.5	- 5.0	8.9	3.5	9.8	9.1	19.8	7.3	8.4	16.3
Imports ¹	274.2	- 5.3	5.2	- 0.4	11.8	11.2	24.3	4.6	9.2	14.1
Gross domestic product at market prices	966.1	- 1.8	13.9	11.8	4.6	9.1	14.2	3.0	8.9	12.1
Distribution of the change in gross domestic products										
Final domestic demand (excluding stock changes)		0.4			3.3			2.3		
Changes in stocks		- 2.2			1.8			- 0.1		
External balance ¹		0			- 0.5			0.8		

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

Production will probably grow just enough to prevent the number of wage- and salary-earners from falling and to stabilize short-time working. All in all, the unemployment rate in seasonally adjusted terms (number of wholly unemployed as a percentage of the civilian labour force) is likely to rise slightly in the second half of the year and to reach 5.3% for the year as a whole instead of 5.0% in 1976.¹ School-leavers seeking their first jobs from the middle of the year onwards will have great difficulty, in all the Member States, in finding work. For demographic reasons, their numbers will be distinctly higher than in preceding years and, since the number of retirements will fall in this and following years, it is to be feared, despite the measures taken, that the already high proportion of

young people in the total number of unemployed in the Community will again increase.

A decelerating *price* trend is foreseeable during the next few months as a result of the developments expected, in particular, in the United Kingdom, Italy and France, where stabilization programmes are likely to have a more marked effect. Apart from unforeseeable outside pressures, most of the factors influencing the price level are likely to grow less severe. World commodity prices, in particular, are unlikely to rise much further, in view of the level of stocks and the foreseeable trend of demand. Even

¹ See Table 14.

TABLE 16
Main monthly indicators

	Year	Jan.	Feb.	Mar	Apr.	May	June	July	Aug.	Sept.	Oct	Nov	Dec
Industrial production (1970 = 100)	1975	108.6	109.6	109.4	105.7	105.2	105.0	104.0	104.3	105.9	107.4	109.5	109.6
	1976	111.2	113.5	113.0	114.3	115.6	115.3	114.3	114.2	118.1	117.4	118.3	118.1
	1977	121.7	120.5	120.0									
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							
Unemployment rate	1975	3.6	3.7	3.9	4.2	4.3	4.4	4.6	4.7	4.8	4.9	4.9	5.0
	1976	5.0	5.0	4.9	4.9	4.9	5.0	5.1	5.0	5.0	4.9	4.9	4.9
	1977	5.0	5.0	5.0	5.1	5.1							
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	0.9	1.0	1.3	1.0	0.8
	1977	1.2	1.0	0.7	1.3	0.9							
Wholesale prices	1975	1.5	0.3	0.3	0.2	0.7	0.0	0.3	0.8	0.5	0.7	0.6	1.3
	1976	1.1	1.4	1.6	2.2	1.4	0.2	1.1	0.9	0.9	1.0	1.3	0.4
	1977	1.2	1.0	0.1									
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	13 328	14 776									
Exports of goods (million EUA)	1975	10 301	10 179	9 835	10 433	9 824	10 204	10 342	9 500	9 980	10 319	9 942	10 852
	1976	10 190	10 155	11 441	10 943	10 973	11 670	11 602	11 850	12 347	11 905	12 619	13 420
	1977	12 142	12 651	13 975									
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	11 042	11 247	12 401	12 669	12 234	13 004	13 059	13 474	13 870	13 611	14 773	15 219
	1977	14 521	14 216	15 303									
Trade balance (million EUA)	1975	- 796	- 74	214	- 158	337	165	- 92	- 308	- 735	- 736	- 791	- 841
	1976	- 852	-1 092	- 960	-1 726	-1 261	-1 334	-1 457	-1 624	-1 523	-1 706	-2 154	-1 799
	1977	-2 379	-1 565	-1 328									
Gross official reserves (gold excl., million EUA)	1975	38 216	39 071	39 928	39 258	38 863	38 445	37 130	37 053	37 809	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	44 663	44 962	46 473									
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	1.666
	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							

: No data available.

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

TABLE 17

Community trade balance 1974, 1975, 1976 and 1977¹

Mio EUA

Monthly average

With respect of	Balance of	Year	FR of Germany	France	Italy	Netherlands	BLEU	United Kingdom	Ireland	Denmark
INTRA-EEC										
FR of Germany		74		59	4	- 2	- 8	22	12	- 21
		75		50	5	- 2	- 11	24	15	- 24
		76		99	4	- 1	- 6	29	23	- 4
		77		82	4	- 1	- 11	36	24	3
France		74	- 57		- 159	- 10	- 115	85	- 38	- 145
		75	- 56		- 106	- 1	- 5	121	- 20	- 102
		76	- 94		- 203	- 0	- 27	212	- 18	- 114
		77	- 76		- 183	- 0	- 24	205	- 48	- 159
Italy		74	- 8	174		- 8	- 108	60	36	- 70
		75	- 7	106		- 3	- 34	63	13	- 66
		76	- 6	232		- 2	- 24	112	87	- 48
		77	- 6	233		- 3	- 39	121	71	- 42
Netherlands		74	2	9	6		- 2	4	1	32
		75	1	- 2	1		- 1	2	- 1	22
		76	2	- 3	1		- 1	- 1	- 4	51
		77	1	1	1		2	1	- 2	39
BLEU		74	5	101	97	- 3		44	10	- 37
		75	10	- 28	19	- 1		36	- 2	- 38
		76	4	2	25	- 2		55	16	- 40
		77	18	17	60	- 3		53	24	- 50
United Kingdom		74	- 25	- 48	- 35	- 1	- 29		- 5	- 37
		75	- 23	- 97	- 46	5	- 22		44	- 33
		76	- 29	- 168	- 79	4	- 40		71	- 34
		77	- 38	- 147	- 99	- 2	- 32		- 20	- 86
Ireland		74	- 16	45	- 12	0	- 17	5		41
		75	- 15	28	12	3	- 3	- 44		29
		76	- 24	34	- 37	5	- 12	- 71		58
		77	- 24	54	- 20	1	- 18	118		7
Denmark		74	16	131	45	- 20	23	85	- 14	
		75	37	87	56	- 7	22	80	- 5	
		76	23	108	16	- 34	19	65	- 30	
		77	- 4	144	12	- 77	29	53	- 34	
EEC Total		74	- 83	471	- 54	- 44	- 252	305	2	- 237
		75	- 53	144	- 59	- 6	- 54	282	43	- 212
		76	- 124	304	- 273	- 30	- 91	401	146	- 131
		77	- 129	384	- 225	- 85	- 93	587	15	- 288
EXTRA-EEC										
USA		74	- 11	91	- 130	- 0	- 57	- 115	- 24	- 122
		75	- 10	- 28	- 136	- 6	- 71	- 169	- 50	- 141
		76	- 8	- 93	- 164	- 9	- 76	- 186	- 70	- 141
		77	- 14	- 36	- 189	- 11	- 46	- 204	- 71	- 145
Japan		74	- 12	- 6	- 34	- 2	- 8	- 17	- 9	- 46
		75	- 6	- 53	- 42	- 3	- 11	- 24	- 18	- 59
		76	- 17	- 79	- 60	- 4	- 20	- 33	- 28	- 65
		77	- 11	- 94	- 61	- 3	- 27	- 47	- 33	- 66
OPEC ²		74	- 55	- 274	- 355	- 15	- 430	- 270	- 131	- 468
		75	- 23	- 96	- 321	- 10	- 279	- 243	- 82	- 189
		76	- 22	- 109	- 469	- 4	- 291	- 341	- 101	- 194
		77								
Other		74	6	1 111	89	- 21	0	87	50	- 225
		75	- 7	1 059	416	- 16	174	105	48	- 148
		76	- 69	1 003	326	- 18	- 3	64	1	- 207
		77								
EXTRA EEC Total		74	- 72	922	- 430	- 38	- 495	- 315	- 114	- 861
		75	- 46	882	- 83	- 35	- 187	- 331	- 102	- 437
		76	- 116	722	- 367	- 35	- 390	- 496	- 198	- 607
		77	- 124	724	- 537	- 39	- 373	- 760	- 215	- 394
WORLD										
		74	- 155	1 393	- 484	- 82	- 747	- 10	- 112	- 1 098
		75	- 99	1 026	- 142	- 41	- 241	- 49	- 59	- 649
		76	- 240	1 026	- 640	- 65	- 481	- 95	- 53	- 738
		77	- 253	1 108	- 762	- 124	- 466	- 173	- 200	- 682
Food, beverages and tobacco		74	114	- 406	198	41	- 251	134	- 42	- 444
		75	136	- 450	110	66	- 252	169	- 50	- 436
		76	130	- 605	105	64	- 299	195	- 71	- 444
		77		- 526	- 30	49		196		- 485
Raw materials		74	- 6	- 403	- 183	- 8	- 386	- 45	- 140	- 329
		75	- 5	- 364	- 147	- 1	- 292	- 39	- 109	- 249
		76	- 9	- 458	- 194	- 5	- 389	- 56	- 135	- 328
		77		- 479	- 193	- 9		- 43		- 355
Other industrial products		74	- 115	1 033	41	- 42	263		402	- 72
		75	- 108	663	133	- 35	534	- 40	321	24
		76	- 168	703	- 85	- 41	535	- 74	357	84
		77		648	- 71	- 52		- 31		117

¹ 1977/ January-March² OPEC Includes Algeria, Abu Dhabi, Dubai, Ecuador, Gabon, Indonesia, Iran, Iraq, Qatar, Kuwait, Nigeria, Saudi Arabia and Venezuela.

No data available

Source EUROSTAT

within the Community, the agricultural market forecasts indicate that prices will not rise sharply, owing, notably, to the small price increases decided under the common agricultural policy. Moreover, the trend of industrial wage costs will probably remain steady and appreciably below the trend of the general level of prices; however, for 1977 as a whole, a slight acceleration is expected in certain countries, particularly in the Federal Republic of Germany; moreover, the tendency for profit margins to widen is likely to be generally accentuated. In the United Kingdom, Ireland and Italy, the greater stability of the exchange rate, noticeable since the beginning of the year, should have a favourable effect on the trend of import prices. Nevertheless, the increase in prices at the point of consumption will average about 9½% for the year, a rate which is close to that recorded in 1976.¹

Given the foreseeable trend of activity for all the Member States, *intra-Community trade* is likely to go on increasing in the second half of the year but at a rate distinctly slower than that observed in 1976 (up 16% in volume terms). The only exception to this trend which will, nevertheless, be sustained, by the elimination on 1 July of custom's tariffs on trade between the States of the enlarged Community, will be Ireland, where exceptional factors curbed exports to other member countries last year. The foreseeable slowdown in the volume growth of imports from non-member countries will be even more marked than the slowdown in *intra-Community trade*, this being partly a matter of lower oil purchases by the United Kingdom.

Since the swing in the terms of trade against the Community is also likely to be smaller, the deficit on the Community's *balance of trade* with non-member countries will probably go on declining in the months ahead. In Denmark and Italy in particular, exports will tend to expand faster than imports. For 1977 as a whole, the improvement in the current account of the deficit Member States should bring the Community's balance of payments on current account near equilibrium, instead of a deficit of some US \$ 8 000 million in 1976.¹

¹ See Table 15

Major economic policy measures

March 1977:

— On 14 March, the Council carried out the first quarterly examination of the economic situation, and:

- (i) approved the Commission Communication Summary account and Degree of Convergence of the economic policies pursued in the Member States in 1976 and adopted the Decision concerning the adjustment of the economic policy guidelines for 1977 which commits the Member States to implement policies which conform to the guidelines agreed by the Council;

- (ii) adopted the Fourth Medium-Term Economic Policy Programme which will provide a framework for economic action by the Community for the years 1976 to 1980;
- (iii) adopted in all official languages a Decision converting a tranche of a Community loan from variable to fixed rates of interest. This operation involves a second US \$ 100 million tranche of the US \$ 300 million variable rate Community loan granted to Italy and Ireland under the Council Decision of 15 March 1976;
- (v) took note of the provisional report from the Chairman of the Monetary Committee on Mr Duisenberg's statement at the Council meeting of 26 July 1976. The Council asked the Monetary Committee and the Committee of the Governors of the Central Banks to continue their work and report back at regular intervals;
- (vi) reviewed the preparation of various subjects which were likely to be on the agenda of the IMF Interim Committee and noted that major progress had been made. The Monetary Committee was instructed to continue preparations and submit a final report to the next Council meeting on 17 April, which would be chiefly devoted to these preparations.

— On 29 March, the Council empowered the Commission to contract loans, on behalf of the European Atomic Energy Community (Euratom), within specified limits, the proceeds to be on-lent for the purpose of financing investment projects connected with the industrial production of nuclear-generated electricity and industrial fuel cycle plants. The Commission may borrow no more than the amount needed to cover the loans for which it receives applications. Under the basic decision, loans may be raised up to a total of 500 million EUA.

April:

— On 6 April, the Commission approved a number of steel policy increases in accordance with the guidelines adopted in March, including:

- (i) the introduction of automatic licences, the purpose being to monitor the imports of certain steel products from all non-member countries;
- (ii) the introduction of minimum prices for concrete reinforcing bars, manufacturers being forbidden to align their prices on offers from non-member countries;
- (iii) the publication in the Official Journal of guide prices for certain rolled products, the Commission urging steel undertakings to make a voluntary commitment to abide by them.

— On 18 April, the Council:

- (i) approved the statement to be made by the President on behalf of the Community at the next meeting of the IMF Interim Committee on 28 and 29 April in Washington;
- (ii) instructed the Permanent Representatives Committee to make the necessary contacts with a view to setting a date in the second half of June for a tripartite conference;
- (iii) approved the economic policy conditions which the Italian Government intends to observe in 1977 and confirmed its authorization for the Commission to float a US \$ 500 million loan for Italy;

— On 25 and 26 April, the Council applied an average increase of 3.9% to agricultural prices for the 1977-1978 campaign.

May:

— On 16 and 17 May, the Council adopted the sixth VAT directive which assures progress in the area of tax harmonization and is a key to the application of the full own-resources system of the Community.

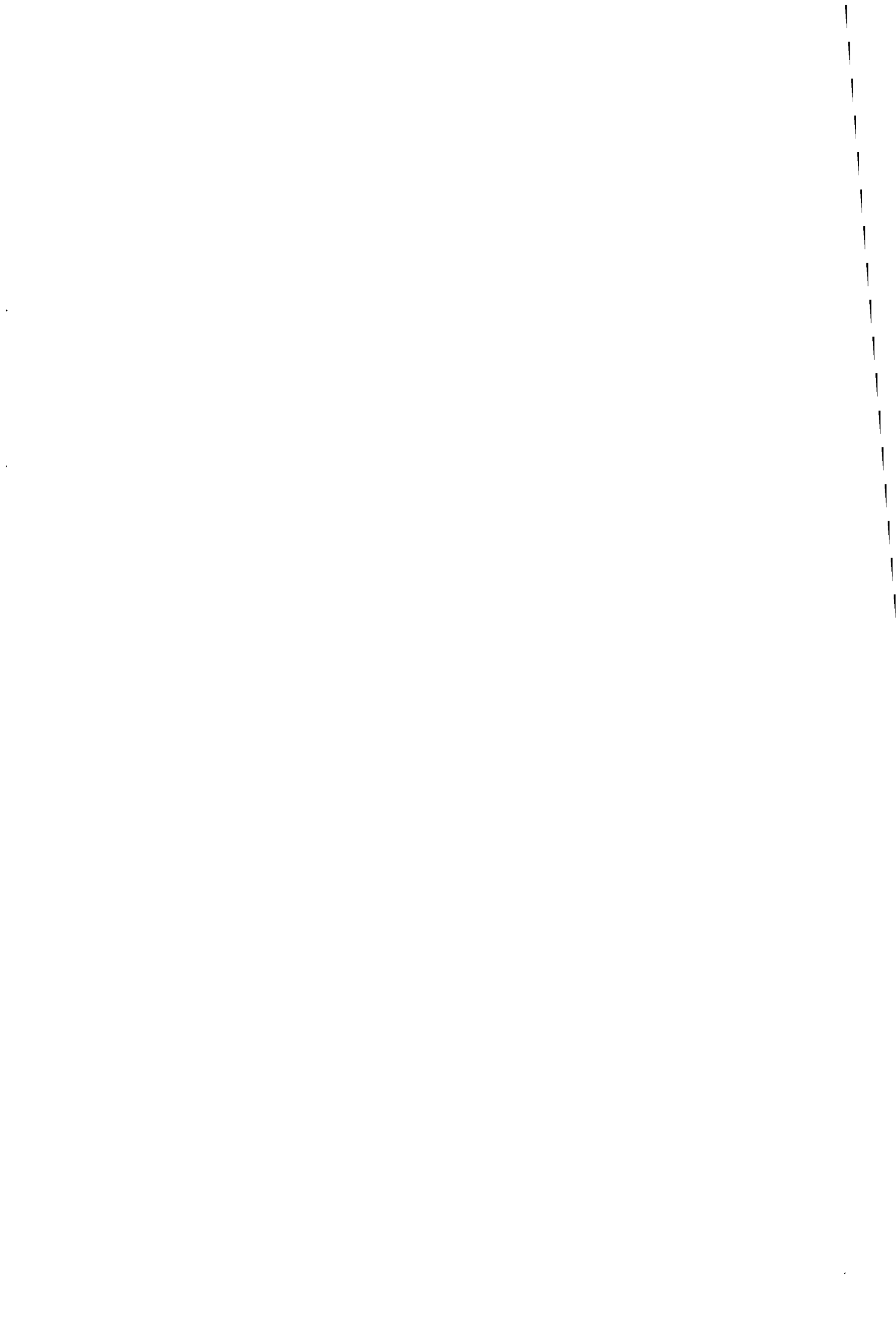
June

— On 20 June, the Council discussed in depth the topic of the tripartite conference of June 25, "Growth, stability and employment - the situation and outlook".

— On 27 June, the tripartite conference between employers, employees, and governments and the Commission took place.

July:

— On 1 July, the process of reducing customs duties in accordance with the Treaty of Adhesion of the United Kingdom, Denmark and Ireland was terminated. On the same day, customs duties between the EFTA countries and the Community were eliminated on most industrial products.



II — The situation in each of the Community countries

A — Denmark

The growth of the Danish economy has been very weak over recent months. The employment situation has deteriorated and the number out of work continues to grow. The rise in prices has tended to become stronger under the influence of certain temporary factors. Due to a more moderate development of imports the trade deficit has fallen slightly.

As far as the priority objective of a reduction in the external deficit is concerned, the authorities have endeavoured to pursue a restrictive demand management policy accompanied by certain selective measures to encourage employment. In addition incomes policy has been implemented by the renewal in April of the national agreement on the basis of the guidelines adopted in August 1976 by Parliament but the risk of increases above the norm exists in the private sector.

Little or no change should be apparent in the coming months when exports will constitute the most important element supporting activity. Thus the unemployment rate will remain high. Important upward factors are likely to influence the development of consumer prices. The balance of payments deficit could fall slightly faster, although it would still be at a relatively high level.

1. Overall assessment and main policy issues

In the course of the past few months the overall performance of the Danish economy has been very modest. At the same time the external constraint has remained very tight, even though a downward trend in the trade deficit has appeared recently. In order to alleviate this, two fundamental conditions were set out in the quarterly report of December 1976: a sufficiently dynamic world demand and a severe incomes policy to

moderate costs. However, recent developments in the international economic situation and in particular the major markets (Sweden, United Kingdom, F.R. of Germany) have not permitted the acceleration of Danish exports expected.

In addition, in the private sector the effective increases in salaries could be higher than those decided in April within the framework of the renewal of collective agreements

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	1.5
of which: industry ¹		4.0	— 5.5	7.4	4.5
Gross domestic product in volume per person in employment	% change	2.3	0.9	3.0	2.3
Total employment (number of persons) ²	% change	0.6	— 2.0	1.7	— 0.8
— Independent entrepreneurs		— 2.2	1.1	— 1.3	— 0.6
— Wage and salary earners in company sector		— 0.5	— 5.2	1.7	— 1.9
— General Government		6.5	3.1	3.8	1.5
Unemployment	as % of labour force	1.3	5.2	5.0	6.0
Compensation of employees per wage and salary earner	% change	12.5	15.0	11.1	7.5
Price index of private consumption ³	% change	7.9	8.8	8.5	9.0
Current account balance	DKr. '000 mio.	— 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

based on the guidelines adopted in August 1976 by the Parliament and could result in appreciable rises in costs.

The inflation rate which moderated substantially due to the effect of the price freeze from 1 December 1976 until 1 March 1977 has accelerated more recently. This movement has been aggravated by the rapid increase in prices of imported raw materials at the beginning of the year and the depreciation of the kroner.

The primary objective of an improvement in the balance of payments has led the authorities to maintain their restrictive demand management policy which is reflected in a relatively weak level of activity. On account of the substantial financing needs brought about by the external deficit, monetary policy has been severe as regards domestic lending and interest rates in order to encourage firms to borrow abroad. Thus the cost of financing new investment has remained high. Certainly, investment support measures in particular sectors have been taken at the beginning of the spring, in conformity with the Commission's Communication to the Council of last March. They have not, however, been sufficient to improve the employment position, and the growing unemployment rate has not ceased to be a major worry for the authorities.

The 3% devaluation of the Danish kroner on 1 April within the Community exchange rate system does not in

itself constitute an autonomous exchange rate policy measure. It was prompted by the devaluation of the Swedish kroner by 6%, which could have created speculative risks and led to a deterioration in competitiveness *vis-à-vis* Denmark's largest trading partner in terms of industrial sales. The consequence of the adjustment was to increase the weight of the already considerable external debt expressed in national currency terms. In the longer term the combination of the two devaluations (October 1976 and April 1977) should, however, if accompanied by progress as regards costs, make for a more satisfactory development of exports.

2. Recent developments

After the disappearance of the stimulus which had acted for the major part of 1976 both on consumption and investment, and in conjunction with the more restrictive character of fiscal policy, the Danish economy has entered, since the autumn, a phase of very weak growth. Private consumption has only progressed slowly and residential construction has suffered a quite pronounced decline. The weakness of the internal market has only been partly compensated for by the strengthening of foreign demand which is still slow in developing. As a result, the level of industrial production has scarcely grown at all. Due to a break in the growth of imports the trade balance position has improved a little.

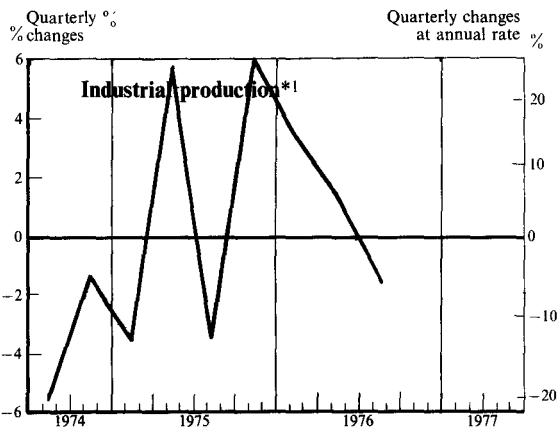
TABLE 2
Demand for and supply of goods and services

Denmark	1974 ²	1975 ²			1976 ²			1977 ³		
	At curr prices DKr. mill	% change on preceding year								
		Vol	Price	Value	Vol	Price	Value	Vol	Price	Value
Private consumption	104.8	4.3	8.8	13.5	6.3	8.5	15.3	1.0	9.0	10.0
Public consumption	43.8	4.0	13.9	18.5	2.6	9.5	12.3	2.0	7.5	9.5
Gross fixed asset formation	40.8	-11.3	11.6	- 1.0	16.6	6.6	24.3	0.5	7.5	8.0
— Enterprises	21.2	-13.2	10.7	- 3.9	19.9	5.3	26.2	6.5	7.0	14.0
— Dwellings	9.5	-17.9	11.1	- 8.8	27.1	7.5	36.6	-12.5	8.5	- 5.0
— General Government	10.1	- 1.2	12.0	10.7	2.5	8.0	10.7	1.0	8.0	9.0
Domestic final uses (excluding change in stocks)	188.8	0.8	10.7	11.7	7.4	8.3	16.3	1.0	8.5	9.5
Domestic final uses (including change in stocks)	190.8	- 2.1	10.8	8.5	9.6	8.3	18.7	0.5	8.5	9.0
Exports ¹	66.1	- 2.5	8.3	5.6	2.7	8.6	11.5	5.5	7.5	13.5
Imports ¹	71.0	- 5.4	5.8	0.1	16.4	6.8	24.3	2.5	7.0	10.0
Gross domestic product at market prices	185.9	- 1.1	12.0	10.8	4.8	9.0	14.2	1.5	8.5	10.0
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	188.8	0.9		11.7	7.5		16.7	1.1		9.7
Change in stocks	2.0	- 3.1		- 3.0	2.1		2.1	- 0.3		- 0.3
Balance of exports and imports ¹	- 4.9	1.1		2.0	- 4.8		- 4.5	0.7		0.8

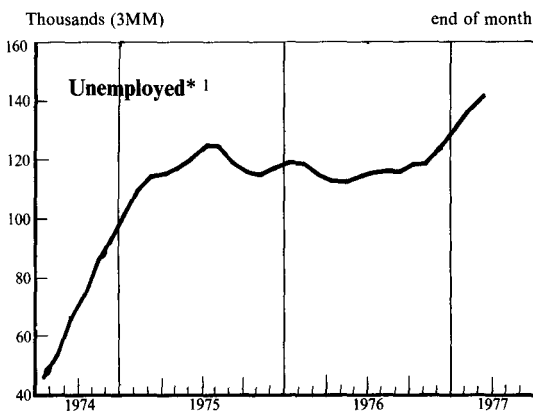
¹ Goods and services

² Source: Danmarks Statistik.

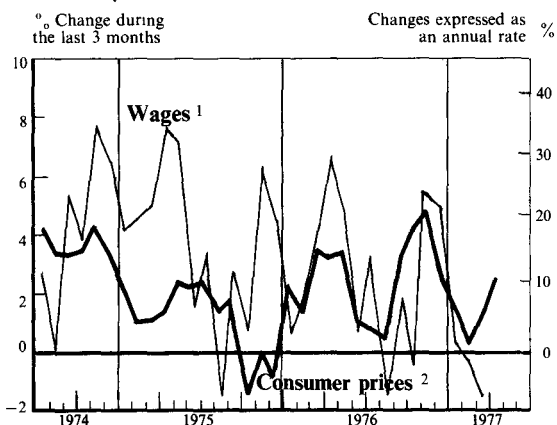
³ Estimates of Commission's Departments



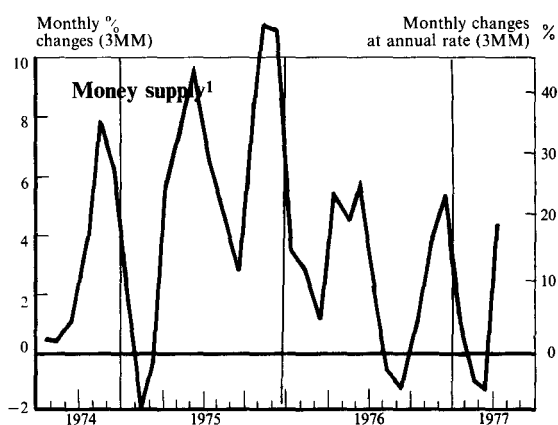
1 Volume of sales, manuf. industry
Source: Danmarks Statistik



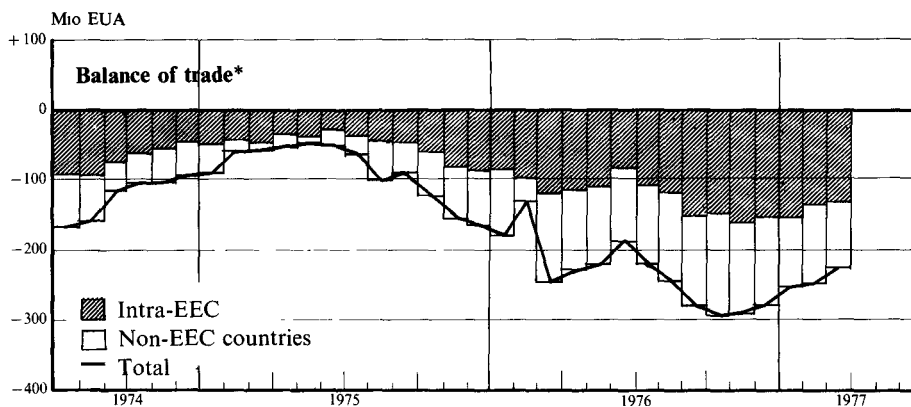
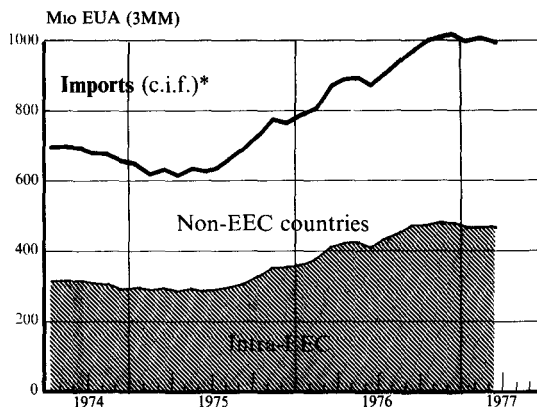
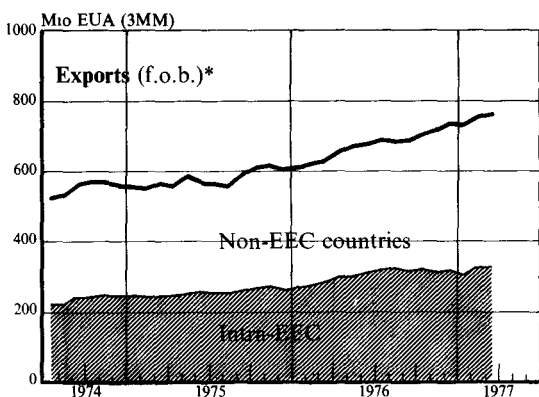
1 Insured unemployed



1 Hourly earnings in industry
2 Including changes in indirect taxation, in particular the reduction in V A T from October 1975 to February 1976
Source: Danmarks Statistik



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



*: Seasonally adjusted figures.
3MM: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

Growth in total *exports*¹ has been relatively slow. In the period February to May they only grew by 2.2% in value, seasonally corrected, on the preceding four months. This development hides divergent trends; a slow-down in agricultural deliveries and an appreciable growth in industrial exports in spite of the weakness of demand on the British and Swedish markets, which together account for 30% of Danish industrial exports.

After the fall which followed the tightening of fiscal policy in August 1976, private consumer expenditure has risen slightly, the reduction in real incomes having apparently been compensated for by a moderation in the savings ratio. In the period February-April the index of the volume of retail sales grew by 1.3% on the preceding three months but still remains at about the average 1976 level. On the other hand the number of new car registrations, seasonally adjusted, has tended to stabilize in the course of the past few months.

Despite the prolongation of several incentive measures *investment* has, in total, been weakening markedly. In the first quarter, new buildings in the industrial sector, on the basis of figures for surface area, declined by 11%. In the same period the number of housing starts was further reduced by 10%, reflecting a persistence of the fall starting in the second quarter of 1976, which is undoubtedly tied up with the development of incomes and present financial conditions. On the other hand, on the basis of industry surveys investment in equipment seems to have continued to rise. Similarly in the agricultural sector investment has been maintained at a high level.

Reflecting the weakness in internal demand *industrial production* has slowed down progressively in the past few months. Agricultural production has remained stagnant, due to the mediocre harvest and undoubtedly also as a result of growing competition in certain product areas.

The *employment* situation has deteriorated. In May the number out of work, seasonally adjusted, reached 146 800 (or 5.8% of the labour force) as against 128 100 in December 1976 (5.1% of the labour force).

After the end of the freeze in February, the rise in *prices* tended to accelerate a little. In May the consumer price index was 9.9% above the level of the previous year.

In conjunction with the development of demand and production, *imports* have moderated; in the period February-May their value,¹ adjusted for seasonal variations, only increased by 0.7% on the preceding four months. Accordingly, and despite a tendency towards a deterioration in the terms of trade, the trade deficit was some DKr. 1 400 million lower in the period in question. However, given the increase in interest payments on the external debt, the current balance of payments deficit has only fallen by around DKr. 300 million in the first quarter, the deficit reaching DKr. 2 700 million as against DKr. 3 000 million in the preceding quarter. Up to October the major part of the deficit has been financed by public authority borrowing outside the country. Of late short term loans to the private sector from abroad have increased markedly. Thus, total foreign currency reserves have progressed to reach a level of DKr. 12 300 million at the end of May.

Since March, the central government budget deficit was only partly financed by sales of internal state securities and this, together with higher borrowing abroad resulted in an appreciable growth in the money supply (M2) which reached a yearly rate of 9% in March (as against 6.9% in February) and has since stabilized at this level. Long-term interest rates have tended to rise slightly and at the end of May were around 15%.

¹ Excluding ships and aircraft.

TABLE 3
The Central Government Budget

Denmark	1976-1977			1977-1978	
	Original budget		Provisional outturn	Original budget	
	DKR mio.	% change ²	DKr '000 mio.	DKR mio.	% change ²
Expenditure ¹	79 270	+ 16.7	79.9	86 857	+ 9.6
of which:					
— current expenditure					
— capital expenditure					
Revenue	66 996	+ 8.0	73.2	77 526	+ 15.7
of which:					
— direct taxes	31 655	+ 11.0	33.6	33 125	+ 4.6
— indirect taxes	33 146	+ 5.8	37.8	42 651	+ 28.7
Net borrowing requirement	— 12 274		— 6.7	— 9 331	

¹ Disregarding debt extinction

² On the preceding year's original budget

Note The figures in this table are based on the national budgets and are recalculated on the basis of Community definitions

TABLE 4
Main economic indicators

	Year	Jan.	Feb.	Mar	Apr	May	June	July	Aug.	Sept.	Oct.	Nov	Dec.
Industrial production (1970 = 100)	1974	112	113	126	113	115	113	77	115	117	117	109	95
	1975	97	98	100	105	100	108	76	106	117	121	111	108
	1976	99	109	124	113	115	127	79	123	132	122	123	115
	1977	107	109	129	105	:	:	:	:	:	:	:	:
Unemployed* (1 000)	1974	15.7	15.5	15.9	20.2	29.2	35.5	43.2	51.2	61.5	77.2	88.0	97.1
	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	:	:	:	:	:	:	:	:
Construction*	1974	2 823.8	2 943.5	1 817.3	3 180.8	1 691.6	2 263.0	1 643.4	1 506.8	1 577.6	1 309.0	1 315.6	1 462.9
	1975	1 832.5	2 156.4	1 526.8	2 287.8	2 878.0	2 699.7	3 013.4	2 744.3	2 713.8	3 069.3	3 862.1	3 262.1
	1976	3 132.1	3 776.1	5 710.8	2 135.3	2 321.3	2 931.7	3 011.5	2 813.8	2 654.1	1 795.8	3 032.7	2 873.5
	1977	4 272.5	1 909.3	:	:	:	:	:	:	:	:	:	:
Private consumers' expenditure* (1970 = 100)	1974	141.6	142.4	140.0	145.6	148.8	143.2	146.4	145.6	144.8	148.8	150.4	148.8
	1975	157.6	160.0	158.4	160.0	159.2	164.8	165.6	164.8	162.4	176.8	176.8	176.0
	1976	177.6	202.4	170.4	184.0	177.6	190.4	189.6	190.4	191.2	188.8	195.2	196.8
	1977	196.8	201.6	202.4	200.0	:	:	:	:	:	:	:	:
Consumer prices (1970 = 100)	1974	133.6	134.0	135.1	137.4	139.2	141.6	143.3	144.2	146.6	148.5	150.5	151.5
	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	:	:	:	:	:	:	:	:
Visible imports* (million EUA)	1974	720.9	708.2	708.6	772.1	711.6	664.3	721.8	708.3	672.1	708.8	667.4	666.8
	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	:	:	:	:	:	:	:	:	:
Visible exports* (million EUA)	1974	470.8	525.6	541.8	531.8	547.6	523.1	517.8	550.4	557.5	592.8	581.2	551.2
	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	:	:	:	:	:	:	:	:	:
Balance of trade* (million EUA)	1974	-250.1	-182.6	-166.8	-240.3	-164.0	-141.2	-204.0	-157.9	-114.6	-116.0	-86.2	-115.6
	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	:	:	:	:	:	:	:	:	:
Foreign exchange reserves (million EUA)	1974	997	974	921	892	925	884	876	867	848	871	978	939
	1975	896	825	792	774	753	745	783	800	074	829	857	757
	1976	817	799	674	635	563	632	733	760	535	552	724	794
	1977	885	984	1 113	1 300	1 510	:	:	:	:	:	:	:
Money supply (million EUA)	1974	5 077	5 001	4 954	5 198	5 182	5 319	5 181	5 162	5 337	5 370	5 649	5 722
	1975	5 210	5 219	5 423	5 659	5 683	6 303	6 184	6 012	6 259	6 711	6 914	7 224
	1976	6 693	6 901	6 868	7 123	7 197	7 462	7 126	6 863	7 099	7 041	7 006	7 367
	1977	6 875	6 726	7 006	6 963	:	:	:	:	:	:	:	:

() Provisional

. Not available

* Seasonally adjusted

Source: EUROSTAT (except as otherwise indicated).

— Industrial production: volume of sales in manufacturing industry (shipyards excl.); Danmarks Statistik

— Unemployment: Number of registered unemployed

— Construction: number of dwellings authorized

— Private consumers' expenditure: Retail Sales Index, in value, Danmarks Statistik

— Consumer prices: Consumer price index, including VAT

— Imports cif, exports fob

— Balance of trade: difference between exports and imports

— Foreign exchange reserves: not reserves of convertible currency, holdings in special drawing rights and reserve position at the IMF; 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

3. Outlook

The economic situation is unlikely to change markedly over the coming months. Domestic demand will remain

weak. Due to the moderate growth in salaries, private consumption will only grow slightly, the same being true for public consumption. Investment could fall back, in particular in the construction sector.

Exports will be the most important element supporting the economy. Industrial sales should, in particular, develop a little more rapidly given the hypothesis expected of a strengthening of demand on certain important markets and the improvement foreseen in the competitive position.

In total, growth of GDP for the year as a whole is unlikely to exceed 1½% in real terms. The employment position will undoubtedly continue to deteriorate and the numbers out of work could still grow to reach a level of 155 000 at the end of the year (about 6% of the labour force).

Given the effect of the increases in agricultural and import prices, accentuated by the devaluation of the kroner, the price rise could remain around about the present level (+9% in annual terms).

Despite a less favourable development in the terms of trade the current balance of payments should continue to improve on account of the moderate behaviour of imports.

As before, the fundamental problem of economic policy will be to prepare the conditions for a return to a more equilibrated balance of payments position, the deficit of which still represents in 1977 nearly 3.7% of gross domestic product. To lighten this constraint, which limits the scope of the authorities and creates difficulties for the adoption of even selective stimulatory measures, the expansion of world demand will be far from being sufficient. Thus the objective of the authorities must be to ensure that the policy fixed for incomes is respected in the coming months and is reflected in continued progress on the costs front. Such a development would consolidate the competitive advantages obtained by the means of the two devaluations of the kroner in October 1976 and April 1977 and thus permit an appreciable transfer of resources into exports.

Major economic policy measures¹

February 1977:

— A package deal including measures to stimulate employment in particular within the construction sector, was introduced. Taking into account the indirect effects, the package itself is estimated to reduce government expenditure by DKr. 500 million in 1977/78, despite a direct increase of DKr. 1 000 million.

March:

— The discount rate was decreased by 1% to 9% with effect from 3 March;

— The credit ceiling was raised by 3% to DKr. 96 900 million from 9 March.

— The government budget 1977/78 was adopted implying total current expenditure of DKr. 86 900 million. The net borrowing requirement will amount to DKr. 9 300 million.

April:

— With effect from 4 April Sweden, Norway and Denmark devalued their currencies against the other members of the European joint float. The Swedish kroner was devalued by 6% and the Norwegian and Danish kroner by 3% each. The Danish "green" kroner was likewise devalued.

— The Parliament adopted on 15 April the draft proposal on the new two-year wage agreement presented by the mediator. The new agreement foresees *inter alia*:

— a half-yearly adjustment of the hourly wages by DKr. 0.70 (March and September);

— a basic minimum salary of DKr. 29 per hour;

— an increase in holiday payment.

This implies an annual wage increase of 2% in real terms. Following an earlier decision (August 1976) one portion at most will be paid each half-year according to the index system, additional portions being paid by the government into the Supplementary Pension Fund and credited to the employee's individual accounts.

¹ During August a special parliamentary session will be devoted to a further revision of economic policy.

B – Federal Republic of Germany

The economic revival in the Federal Republic of Germany is more subdued and shows sharper fluctuations than in previous phases of recovery. The brisk pace noted towards the end of 1976 thus slackened somewhat in the early months of the year. Private-sector investment demand in particular seems to have lost a good deal of momentum. Economic activity will probably accelerate again in the months ahead; this is suggested, among other things, by the encouraging outlook for the economies of some of the Federal Republic's important trading partners. As capacity utilization rates increase and sales prospects become more favourable, the investment climate too should improve. Real gross national product is likely to grow by an average of around 4% in 1977.

With the upswing generally moderate, there is a chance of achieving steady growth — without the risk of rapid overheating and subsequent readjustment — and of progressively bringing back price stability. As a corollary, however, the situation on the labour market will show little, if any, improvement. It will also be aggravated by the continuing rationalization drive and the renewed increase in the labour force expected over the next few years.

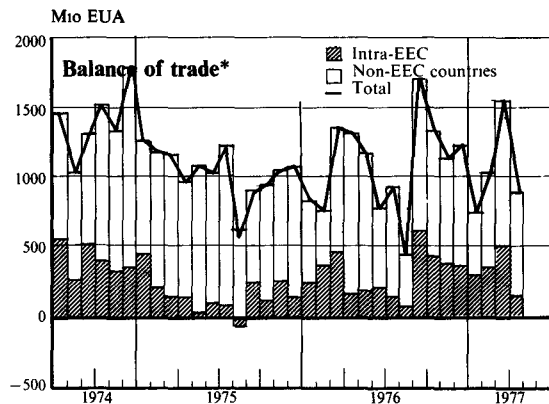
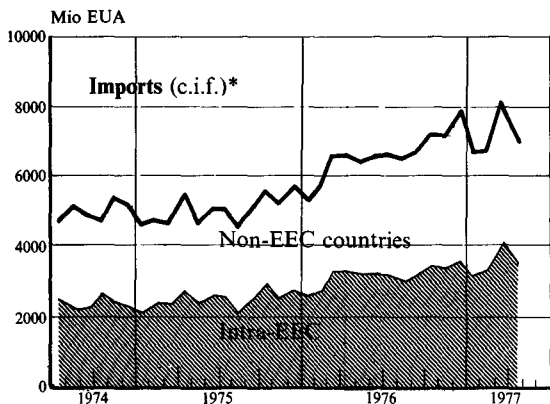
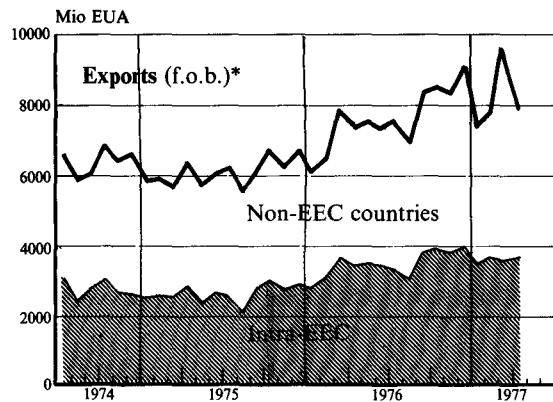
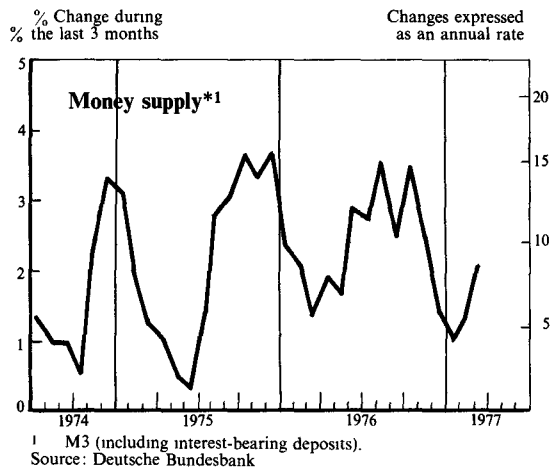
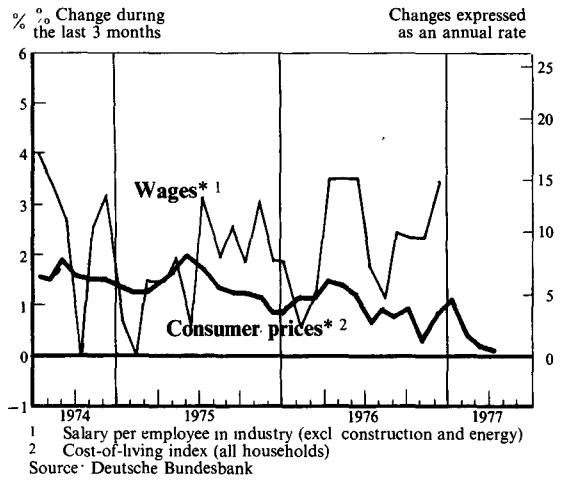
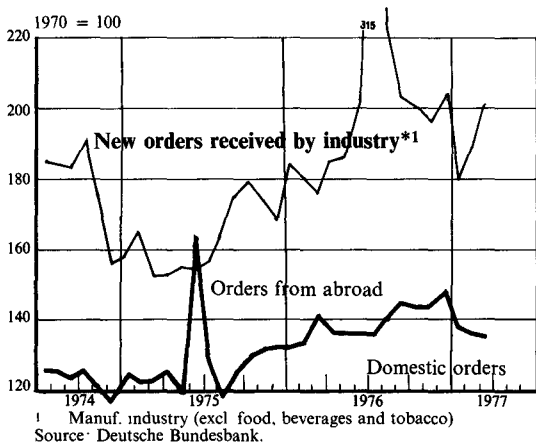
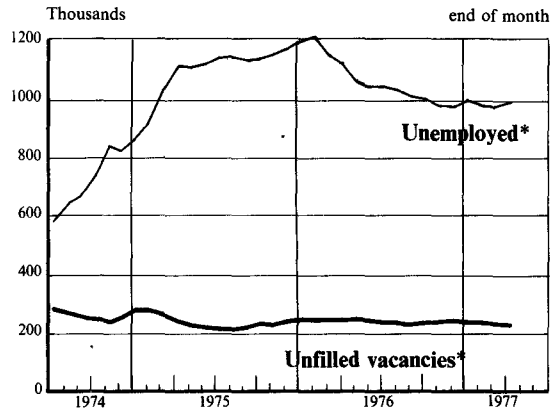
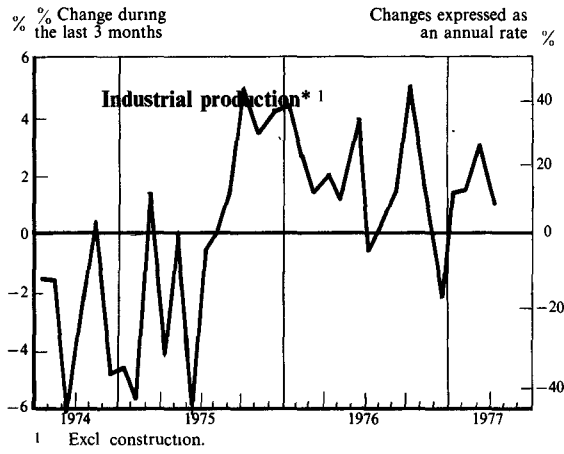
A return to full employment seems possible only as part of a medium-term policy. It is particularly important in this context to boost the private-sector propensity to invest and to expand public capital expenditure, which in recent years has fallen considerably behind.

1. Overall assessment and main policy issues

The Federal Republic's economy is still on an upward trend. Compared with previous periods of expansion, however, the revival is more subdued and shows sharper

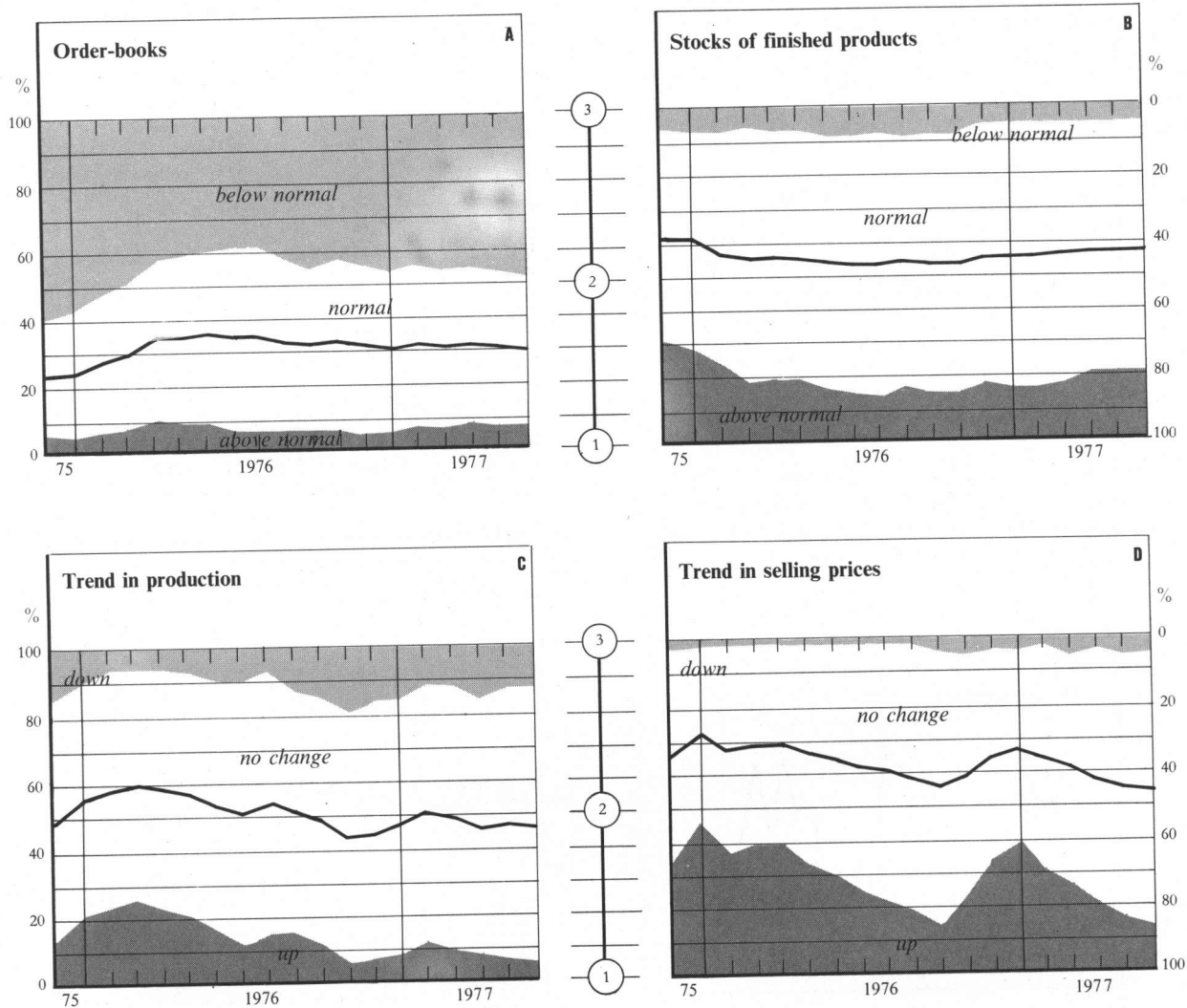
fluctuations. After a clear acceleration towards the end of 1976, economic expansion thus slackened again in the first few months of the year. Despite a slight pick-up, export demand provided distinctly a weaker stimulus than in the same period last year. Private sector

Federal Republic of Germany



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

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

GRAPHS A, B, C and D: The three zones (grey, white and black) show the percentages of the three different answers.

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

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

investment demand again lost momentum and remained unsatisfactory. Following a very sharp decline last year, the situation in building and construction has recently improved a little. With the growth of demand generally weaker, output too rose more slowly. The situation on the labour market therefore remained disappointing. The latest data and the relatively favourable outlook in the Federal Republic's important trading partners suggest a possible strengthening of expansionary forces in the months ahead. For this to materialize, however, there will have to be a clear revival in business investment. Private consumption may probably make a greater contribution than before to sustaining economic activity. Even assuming a relatively sharp improvement in economic activity in the coming months, real growth in 1977 is unlikely to exceed an average of 4%.

With the upswing generally moderate and the slack in the economy being taken up only gradually, there is a chance, provided economic policy is kept on the appropriate tack, of achieving steady, moderate growth without alternating between rapid overheating and subsequent readjustment, and of progressively bringing back price stability. However, the very slow restoration of business confidence in the prospects for sales and profits, coupled with a very cautious improvement in the readiness to invest, is having a particularly adverse impact on the situation on the labour market. In addition, the rationalization drive triggered by the sharp rise in the cost of labour is continuing and will coincide with a renewed increase in the size of the labour force over the next few years. A return to full employment thus seems possible only as part of a medium-term policy. It is particularly important in this context to boost the private-sector propensity to invest and also to expand public capital expenditure,

which in recent years has fallen considerably behind. Under the circumstances, the decision by the Federal Government to step up public capital expenditure by DM 16 000 million in the period 1977-1980 is to be welcomed. This programme, under which contracts totalling DM 3 500 million are still to be awarded this year, is expected to contribute in the period ahead to underpinning activity, particularly in building and construction.

As the economic outlook is only moderately favourable and public budget trends are relatively encouraging, the goal of reducing the budget deficits should not be pushed too far. The modified proposals for changes in taxation submitted by the Federal Government, are likely to contribute to an expansionary budgetary posture. It is now planned to raise the general rate of Value Added Tax from 11 to 12% and the reduced rate, — mainly applied to food and services — from 5½% to 6%. At the same time, — as already previously planned — children's allowances are to be improved, specific allowances against income tax are to be increased and taxes on businesses and wealth are to be eased. The total net effect of these measures is likely to lead to a loss of receipts of about 1 billion DM. However, should the foreseen increase in private investment lag behind expectations, then a supplementary tax stimulus should be considered with a view to a sustained strengthening of private investment.

The Bundesbank's monetary and credit policy continues to be geared to a moderate expansion in the money supply to finance real growth against the background of a further deceleration in the rate of price increases. The target for the growth in the central bank money stock in 1977 is again an average of 8%. As part of this policy and in order

TABLE 1
Key indicators

FR of Germany	Unit	1971-1974 average ^{4 5}	1975 ⁵	1976 ⁵	1977 ⁶
Gross domestic product, volume	% change	3.1	— 2.6	5.7	3.8
of which: industry ¹		2.6	— 6.2	7.8	5.0
Gross domestic product in volume per person in employment	% change	3.5	0.7	6.7	3.9
Total employment (number of persons) ²	% change	— 0.4	— 3.3	— 1.0	— 0.1
— Independent entrepreneurs		— 2.1	— 3.3	— 2.6	— 1.5
— Wage and salary earners in company sector		— 0.7	— 4.5	:	0.2
— General Government		3.7	1.8	:	0.5
Unemployment	as % of labour force	1.2	4.1	4.1	3.8
Compensation of employees per wage and salary earner	% change	11.7	7.7	8.0	8.2
Price index of private consumption ³	% change	6.3	6.3	4.4	3.8
Current account balance ³	'000 mio.	11.2	10.7	8.1	8

¹ Construction included

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: Statistisches Bundesamt Wiesbaden: Wirtschaft und Statistik 4/77.

⁶ Estimates of Commission's Departments

: No data available.

to avoid temporary strains on the money market, the Bundesbank recently decided to lower the minimum reserve requirements and to increase rediscount quotas. The very favourable terms on which finance is at present available should help to encourage investment activity particularly if interest rates continue to decline in the financial markets.

In view of the depressed situation on the labour market, special importance attaches to the unions' wage policy. Any further erosion of profit margins through a more rapid increase in wage costs will not only significantly curb investment but also put existing jobs at risk.

2. Recent developments

Merchandise exports continued to expand, with their value in the first five months of the year some 8% up on a year earlier. However, this rate failed to match the very brisk growth recorded last year. This slackening was apparent in exports both within the Community and to other industrialized countries. Purchases by the OPEC and state-trading countries remained stagnant at a high level while export business with developing countries maintained its downward tendency. Export prices, which had been relatively stable until the turn of the year, edged up again, particularly in the case of finished products.

Business demand for *investment in plant and machinery*, expressed in terms of the domestic orders placed with the

capital goods industry, has fallen significantly. Even allowing for a greater margin of error because of changes in the official statistics, the marked revival of investment activity noted last autumn has thus come to a halt. After deteriorating appreciably last year owing to the expiry of most of the public support programmes introduced during the recession, activity in commercial and industrial building and also in residential construction has recently revived a little. Building demand from the public authorities has also shown some improvement. The stimulus provided by stockbuilding have probably slackened further.

With minor fluctuations, *private consumers' expenditure* has continued to expand since the end of 1976. Retail sales in the first four months of the year were 4% higher in value than a year earlier: adjusted for the rise in prices, this gave an increase of only 1% or so. Sales of new cars picked up significantly: in the first five months of the year, new registrations were almost 9½% up on the already very high figure recorded a year earlier.

With the high propensity to save virtually unchanged, the growth in private consumers' expenditure was attributable to the more rapid rise in wage incomes. There was probably also the impact of the sharp increase in funds released under premium-carrying savings contracts.

With overall demand growing more slowly, *industrial production* rose only sluggishly. Output in manufacturing

TABLE 2
Demand for and supply of goods and services

FR of Germany	1974 ²	1975 ²			1976 ²			1977 ³		
	At current prices '000m DM	% change on preceding year								
		Vol.	Price	Value	Vol.	Price	Value	Vol.	Price	Value
Private consumption	527.55	2.5	6.3	8.9	3.6	4.4	8.2	4.2	3.8	8.2
Public consumption	194.02	3.8	6.6	10.6	2.6	3.5	6.2	3.0	4.5	7.6
Gross fixed asset formation	216.39	- 4.2	3.4	- 0.9	5.1	3.2	8.5	3.0	3.8	6.9
— Enterprises	111.24	- 1.3	4.8	3.5	7.4	3.4	11.1	4.7	4.0	8.8
— Dwellings	64.47	-10.4	2.5	- 8.2	6.7	3.3	10.3	3.0	4.0	7.1
— General Government	40.68	- 3.2	2.2	- 1.1	- 3.9	2.6	- 1.4	- 2.6	3.0	0.4
Domestic final uses (excluding change in stocks)	937.96	1.1	5.8	7.0	3.8	4.0	7.9	3.7	3.9	7.8
Domestic final uses (including change in stocks):										
Exports ¹	259.84	- 7.0	5.7	- 1.7	12.2	1.8	14.3	6.8	3.0	10.1
Imports ¹	216.17	+ 4.6	0.4	5.1	11.8	5.1	17.5	7.2	3.7	11.1
Gross domestic product at market prices	987.13	- 2.6	7.1	4.3	5.7	3.1	8.9	3.8	3.7	7.6
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	937.96	1.0	—	6.7	3.7	—	7.7	3.6	—	7.5
Change in stocks	5.50	- 0.8	—	- 0.8	1.5	—	1.5	0.1	—	0.1
Balance of exports and imports ¹	43.67	- 2.8	—	- 1.6	0.5	—	- 0.3	0.1	—	0.0

¹ Goods and services

² Sources: Statistisches Bundesamt Wiesbaden *Wirtschaft und Statistik* 4/77.

³ Estimates of Commission's Departments

(excluding building and construction), which, on the new statistical basis, comprises industrial firms with twenty or more employees, was some 5½% higher in the first four months of the year than in the same period last year.

Overall, the slow increase in output was accommodated by drawing on existing productivity reserves, with the result that there was no significant improvement in the situation on the *labour market*. The decline in unemployment in the spring hardly exceeded the seasonal norm. At the end of May, there were still 947 000 people out of work, or 4.1% of all employees, and the number of persons on short time stood at 317 000. Firms' reluctance to recruit more workers was reflected in the number of unfilled vacancies, whose trend was weaker than is normal for the season. At the end of May job vacancies notified to employment offices numbered 243 000.

Owing to the sluggish growth in overall demand at the beginning of the year, the growth in *merchandise imports* also slackened. In the period January-April, their value was some 8% higher than a year earlier. Demand for foreign cars and electrical goods was still very brisk.

The situation as regards *prices* remained decidedly favourable. Industrial producer prices rose only moderately between the autumn of 1976 and the end of May, when they were 3% up on a year earlier. The cost-of-living index rose somewhat more rapidly at the beginning of the year, boosted by the increase in the excise duties on tobacco and spirits, but the deceleration has since continued. In May, consumer prices were 3.8% higher than a year earlier.

In the period January-May, the *trade balance* showed a surplus of DM 15 500 million, an increase of almost DM 1 500 million on a year earlier. Owing to a slightly greater deficit on the services balance, the current account surplus was of the same order as a year earlier. Since the

deficit on capital account broadly matched the surplus on current account the gross gold and foreign exchange reserves held by the Bundesbank have shown little, if any, change since the beginning of the year; at the end of May, they totalled DM 88 500 million.

As deficits were being reduced further, *public budgets* had an increasingly contractionary effect. On a cash basis, Federal Government revenue in the period January-April was some 8½% higher than a year earlier while Federal Government expenditure was only a little over 2½% higher. At DM 11 500 million, the cash deficit showed an improvement of almost DM 2 000 million over 1976.

The slower growth in lending to private industry produced a more settled pace of *monetary expansion*. In addition, the foreign exchange markets remained relatively quiet and external payments transactions were broadly in equilibrium. In the period January-May, the central bank money stock was some 8½% above the level of a year earlier. The growth in the money supply is, therefore, on course for the Bundesbank's target of an average of 8% for 1977. Interest rates on the bond market have continued to fall.

3. Outlook

In the months ahead, the reduced pace of growth experienced at present will probably quicken again somewhat, with the trend of export demand to play a key role. As economic activity picks up in the industrialized countries of the West, particularly those outside the Community, German merchandise exports to these countries should expand more rapidly again. German exports to developing, State-trading and OPEC countries are also likely to grow at a more buoyant rate as the year progresses.

TABLE 3
The Central Government Budget

FR of Germany	1976			1977	
	Original budget		Provisional outturn	Original budget	
	'000 mil.	% change ²	'000 mil.	'000 mil.	% change ²
Expenditure ¹	164.0 ³	5.7	161.7	171.3 ³	4.5
of which:					
— current expenditure	140.3	10.0	136.5	144.5	3.0
— capital expenditure	26.3	— 8.4	25.1	29.3	11.4
Revenue	131.3	1.4	135.8	150.2	14.4
of which:					
— direct taxes	53.1	— 7.2	55.8	64.6	21.7
— indirect taxes	73.8	7.6	75.1	80.8	9.5
Net borrowing requirement	— 32.7	.	— 25.9	— 21.1	.

¹ Disregarding debt extinction.

² With reference to preceding budget proposals.

³ Assumes that, in carrying out the budget, overall reductions in expenditures of DM 2 550 million in 1976, and DM 2 500 million in 1977 will be realized.

Note: The figures in this table are based on the national budgets and are recalculated on the basis of Community definitions.

TABLE 4
Main economic indicators

	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	119.1	117.0	116.1	120.1	:	:	:	:	:	:	:	:
New orders received* (1970 = 100)	1974	137	140	143	142	144	144	139	145	137	141	134	127
	1975	133	131	129	132	128	160	135	128	138	141	141	142
	1976	144	144	148	148	148	151	175	158	158	157	155	162
	1977	148	148	150	:	:	:	:	:	:	:	:	:
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	143	140	138	:	:	:	:	:	:	:	:	:
Unemployed* (000)	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	995.9	:	:	:	:	:	:	:	:
Unfilled vacancies* (000)	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	:	:	:	:	:	:	:	:
Construction permits for residential construction* (000)	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	28.5	30.9
	1977	28.3	:	:	:	:	:	:	:	:	:	:	:
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	157	157	158	157	160	162	157	164	164
	1977	167	167	172	:	:	:	:	:	:	:	:	:
Consumer prices* (1970 = 100)	1974	123.5	124.4	124.8	125.4	126.3	126.8	127.4	128.2	128.6	129.4	130.1	130.6
	1975	131.1	131.6	132.2	133.1	133.9	134.9	135.3	135.7	136.5	136.9	137.2	137.6
	1976	138.0	138.7	139.3	140.1	140.6	141.0	140.8	141.9	142.0	142.1	142.3	143.1
	1977	143.7	144.3	144.8	145.3	:	:	:	:	:	:	:	:
Visible imports* (million EUA)	1974	4 396	3 935	4 828	4 821	5 327	4 708	5 146	4 821	4 700	5 401	5 121	4 877
	1975	4 541	4 712	4 619	5 490	4 660	5 071	5 016	4 459	5 118	5 786	5 215	5 673
	1976	5 260	5 711	6 555	6 571	6 356	6 557	6 635	6 480	6 662	7 158	7 167	7 869
	1977	6 643	6 798	8 072	6 978	:	:	:	:	:	:	:	:
Visible exports* (million EUA)	1974	5 533	5 580	6 350	6 352	6 954	5 542	6 600	5 845	6 024	6 917	6 452	6 646
	1975	5 781	5 892	5 783	6 433	5 724	6 086	6 231	5 027	6 017	6 719	6 248	6 729
	1976	6 082	6 451	7 886	7 362	7 514	7 316	7 553	6 914	8 351	8 488	8 288	9 084
	1977	7 384	7 815	9 639	7 843	:	:	:	:	:	:	:	:
Balance of trade* (million EUA)	1974	+ 1 137	+ 1 646	+ 1 523	+ 1 532	+ 1 628	+ 834	+ 1 454	+ 1 024	+ 1 324	+ 1 516	+ 1 331	+ 1 769
	1975	+ 1 240	+ 1 180	+ 1 165	+ 943	+ 1 064	+ 1 015	+ 1 215	+ 568	+ 899	+ 932	+ 1 033	+ 1 056
	1976	+ 823	+ 741	+ 1 330	+ 792	+ 1 158	+ 759	+ 918	+ 434	+ 1 690	+ 1 331	+ 1 121	+ 1 216
	1977	+ 741	+ 1 017	+ 1 567	+ 865	:	:	:	:	:	:	:	:
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	:	:	:	:	:	:	:	:
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	:	:	:	:	:	:	:	:	:

() Provisional

· 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 fob, 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

The still unsatisfactory level of investment activity continues to give cause for concern. However, a number of factors suggest that, as the upswing gradually gathers momentum, firms' purchases of plant and machinery will also rise somewhat more briskly. In particular, the very favourable terms for borrowing — interest rates on the capital market are now down to a level last recorded in 1968 — and the continuing improvement in the rate of capacity utilization will probably have a favourable impact of firms' investment decisions. In 1977 as a whole building investment will rise only a little and will continue to act as a brake on economic growth. While the deadlines applicable under the investment premium scheme will probably still ensure more buoyant building activity in the first half of the year, activity in industrial and commercial building and also in residential construction is expected to fall off in the second half. However, the sharply reduced cost of building finance may provide some stimulus to private demand for owner-occupied homes and apartments; the recent measures taken by the Federal Government in respect of subsidized housing will probably also help to underpin building demand. Building investment by the public authorities will probably decline further during the remainder of the year since the contracts worth DM 3 500 million which are still to be awarded this year under the multiannual investment programme are for the most part unlikely to affect production before 1978.

Private consumers' expenditure will probably grow somewhat more rapidly, making a continued contribution to the upswing. This is suggested by the expected increase in actual earnings and the continuing rapid rise in transfer incomes, which, with the upward movement of prices moderating further, will bring about faster growth in real personal incomes. In addition, a further substantial volume of funds will be released in the second half of the year under premium-carrying savings contracts. On the other hand, official measures to trim public budgets will continue to have a dampening effect on public consumption.

With the expansion in demand a good deal slower than in 1976, real gross domestic product is still likely to grow by an average of around 4% in 1977. In view of the spare capacity available, this rate can be achieved, in the economy generally, without an increase in the numbers employed. No fundamental improvement can therefore be expected in the situation on the labour market.

Given the more vigorous trend of domestic activity, imports will probably grow more rapidly again in the months ahead. Taking the average for the year, however, their increase will be somewhat smaller than in 1976, so that the external surplus is likely to be of much the same order as last year (some DM 27 000 million) despite the weaker growth in exports.

The rate of price increases will remain moderate. Disregarding the impact of the increase in the excise duties on tobacco and spirits, the rise in the cost of living will again decelerate a little in 1977.

Major economic policy measures

January 1977:

— On 26 January the Federal Government adopted the 1977 annual economic report. The annual projection for the general economic trend

suggests that real gross domestic product will grow by some 5% in 1977. The likely increase in consumer prices is put at 4%. Gross compensation of employees is expected to rise by 8.9% and gross property and entrepreneurial income by 9-10%.

February:

— Employers and unions in the metal-working industry agreed on wage increases of 6.9%. Together with the higher benefits under the scheme to promote personal asset formation and higher special payments by firms negotiated in October 1976, this means an extra burden of 8-8.5% for firms.

— The Federal Labour Office announced its intention of safeguarding or creating around 82 000 jobs in 1977 by means of work procurement measures. An amount of DM 700 million is to be earmarked for the scheme. In 1976, the Federal Labour Office provided assistance in respect of some 75 000 jobs.

March:

— On 2 March public service employers and unions agreed on improvements worth 6.3%. These are made up of an across-the-board wage and salary increase of 5.3%, DM 150 holiday allowance and up to two days additional paid annual holiday for those in the lower wage groups. A one-off payment of DM 100 was awarded to compensate for the longer period (13 months) for which the agreement is to run.

— On 2 March the Federal Government adopted a draft law extending depreciation allowances in respect of owner-occupied homes under section 7b of the Income Tax Law. Backdated to 1 January 1977, relief is to be granted in respect of the acquisition of single-family and two-family homes and owner-occupied apartments. In addition, the acquisition of owner-occupied homes is to be exempted from real estate transfer tax. In its first year of application, the law will cost some DM 750 million in lost tax revenue.

— On 3 March the Bundesbank raised rediscount quotas by DM 2 500 million, to DM 18 500 million.

— With effect from 10 March, the Bundesbank, in an attempt to prevent further liquidity strains, again granted advances against the pledge of bills of exchange. The bills were accepted as collateral for 20 days, at 4%.

— On 23 March the Federal Government adopted a public investment programme of around DM 16 000 million to provide for growth and environmental protection during the period 1977-80. The Federal Government reckons that, by 1980, the programme, designed primarily to improve the transport and communications system, water management, energy supply and use and housing and town planning policy, will generate an extra increase in gross domestic product of around DM 30 000 millions. The first contracts, worth DM 3 500 million, are to be awarded in 1977 already. Furthermore, the Federal Government laid down new guidelines for rolling forward the energy programme. The aim is to reduce the share of oil in total energy consumption and to close the energy gaps that threaten to develop in the 1980s by greater use of coal and nuclear energy for the generation of electricity.

April:

— On 29 April employers and unions in the building and construction industry negotiated a 6.4% increase in agreed wages and a further 0.8% increase in the wages paid for the "thirteenth" month. The cost of this settlement to the building and construction industry is 7.2%. In addition, with effect from 1 May 1978, the wages of skilled workers are to go up by a further 1.5%.

— On 27 April the Federal Government adopted a four-year energy research programme under which, in the period 1977-80, an amount of DM 6 500 million is to be made available for research into rational uses of energy, research relating to coal, the development of new sources of nuclear energy and other work in the field of energy research.

May:

— On 13 May the Bundestag passed the draft laws aimed at reorganizing the statutory pension insurance scheme and curbing the cost of medical welfare services. Retirement pensions under the statutory insurance scheme and under the war victims' pension scheme will be increased by 9.9% on 1 July. The next uprating of pensions has been put back until 1979. The contribution from the pension insurance scheme towards sickness insurance for pensioners — at present 17% of expenditure on pensions — will be lowered to 11%. The resulting shortfall in revenue for the sickness insurance scheme is to be met by raising the earnings ceiling for contributions, increasing the rates of contribution and applying the cost-curbing programme.

— On 18 May, the Central Bank Council took the following decisions:

- with effect from 1 June, minimum reserve ratios will be lowered by 5%, thereby releasing DM 2 300 million of Central Bank money;
- likewise with effect from 1 June, the rediscount quotas for credit institutions will be increased by DM 2 500 million;
- the current facility under which the Bundesbank agrees, as part of its open market operations, to grant credit institutions advances against the pledging of bills of exchange will lapse on 31 May.
- On 25 May the Federal Government decided to extend the regional programme for publicly assisted housing, which, initially, was to run until the end of 1977: In the next few years, the Federal Government will make available to the Länder each year a sum of DM 1 100 million with which to subsidize the building of 60 000 dwellings. An extra DM 600 million is to be allocated this year to promote the building of more than 30 000 dwellings.
- The Federal Labour Office's labour market programmes, which benefit mainly young people, elderly clerical workers and women, are to be continued. The Federal Government will make available an additional

DM 500 million to the Federal Labour Office, which still has DM 100 million left over from previous programmes.

June:

- On the 16 June the Bundestag ratified a tax amendment law which should come into effect on the 1st of January. The measures provide for an increase in the general rate of value added tax from 11 to 12% and in the reduced rate, — mainly for food and services — from 5½ to 6%. At the same time children's allowances are to be improved, specific allowances against income tax are to be increased and taxes on businesses and wealth are to be eased. The total net effect of these measures in 1978, will be to reduce receipts by DM 1 billion.
- On the 16 June, the Bundestag decided to adjust rent subsidies to allow for the increases in rents and incomes that have occurred since 1974, the date of the last change. The law will come into effect on 1 January 1978. After the modification, expenditures for 1978 and for the following year are estimated to DM 800 million and DM 700 million respectively.

C – France

For some months now in France, economic activity has only advanced slowly. The trade deficit has been reduced. There have been tentative signs of a slow-down in the upward movement of costs, but inflationary strains remain severe. The number of jobless has continued to rise and the French Government has implemented a programme to boost employment, though the main principles of the plan for restoring equilibrium adopted last September have not been altered.

In coming months, external balance should be consolidated and progress may be expected in the drive to curb inflation. A modest rate of economic growth can be expected, but there are no real grounds for predicting an improvement with regard to the unemployment situation.

1. Overall assessment and main policy issues

Over the last several months there has been a slackening in the expansion of the French economy, which began

again in the summer of 1975. This has facilitated the restoration of external equilibrium, but the employment situation has further deteriorated. The French Government has in recent months laid before Parliament a

TABLE 1
Key indicators

France	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁵	1977 ⁶
Gross domestic product, volume	% change	4.8	0.1	5.2	3
of which: industry ¹		5.7	– 9.3	7.7	3
Gross domestic product in volume per person in employment	% change	5.6	1.2	5.1	3.7
Total employment (number of persons) ²	% change	0.8	– 1.1	0.1	– 0.7
— Independent entrepreneurs		– 2.7	– 2.3	– 2.3	– 2.5
— Wage and salary earners in company sector		1.7	– 1.4	0.6	– 0.9
— General Government		1.9	1.5	0.8	2.6
Unemployment	as % of labour force	2.7	4.2	4.6	4.8
Compensation of employees per wage and salary earner	% change	12.8	17.7	14.8	11.8
Price index of private consumption ³	% change	8.3	11.6	9.9	9
Current account balance ³	Mrd FF	– 5.4	– 0.3	– 27.5	– 15.5

¹ Excluding construction

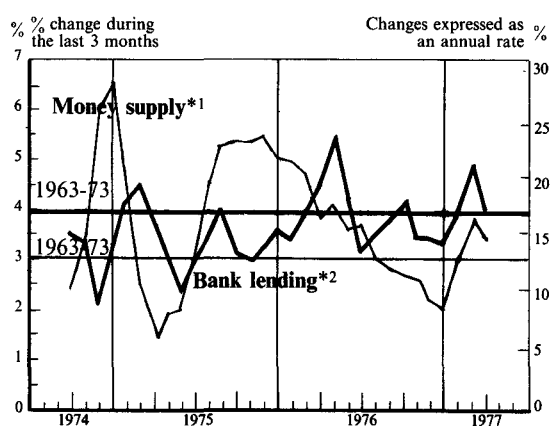
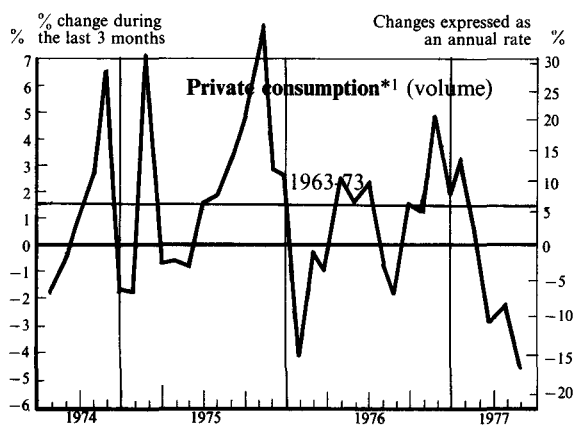
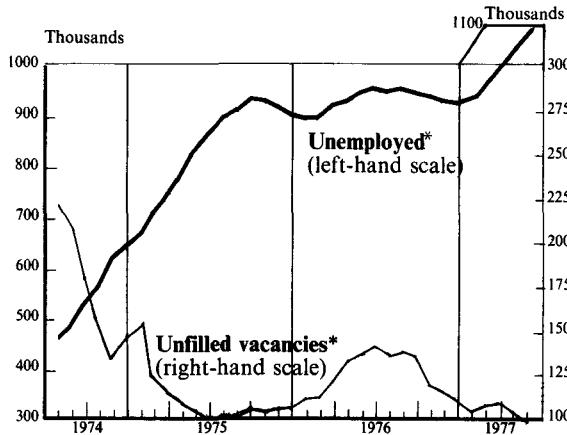
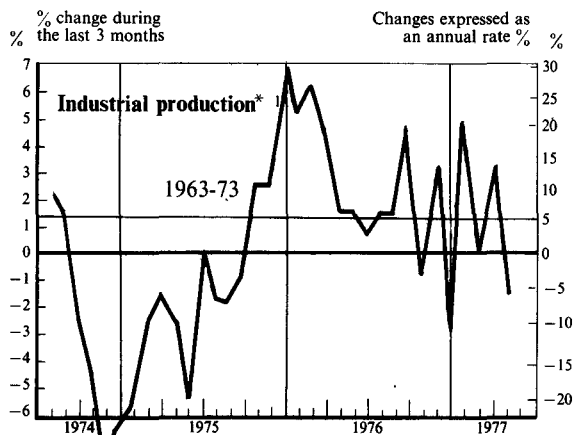
² Domestic concept.

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

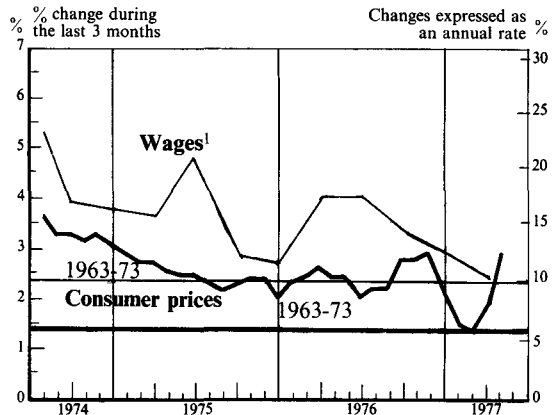
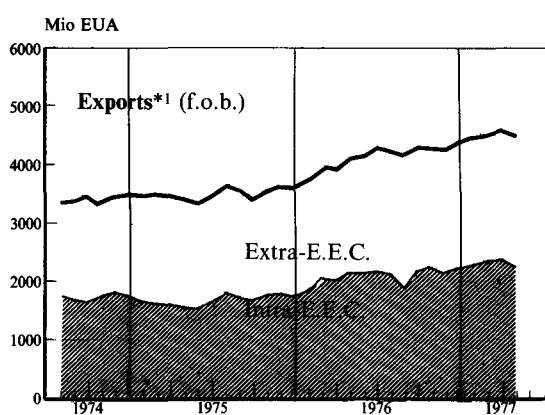
⁵ Source: Rapport sur les comptes de la nation de l'année 1976

⁶ Estimates of Commission's Departments.



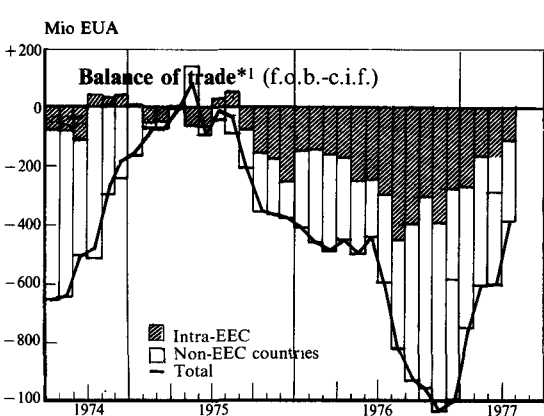
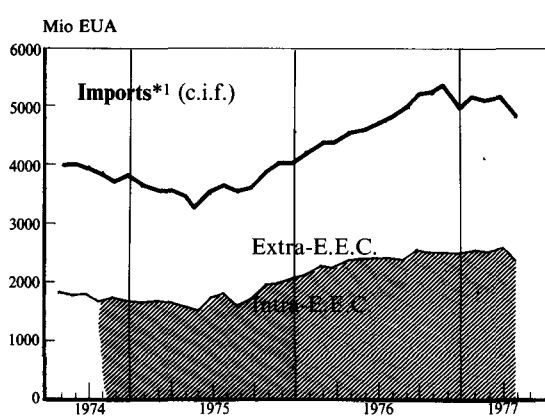
¹ Consumption of manufactured goods

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.

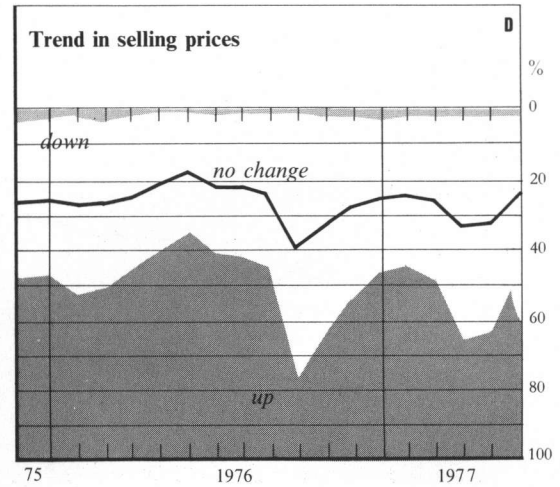
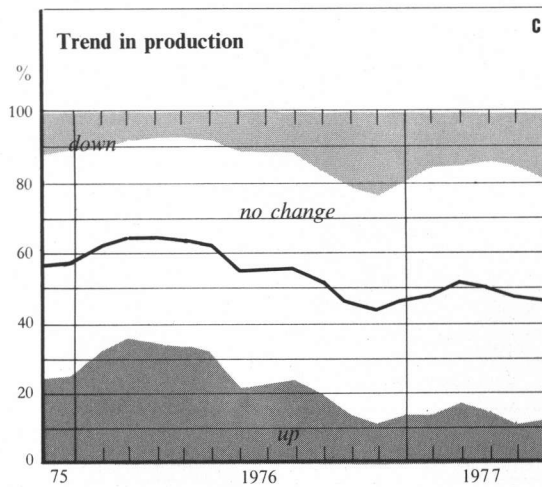
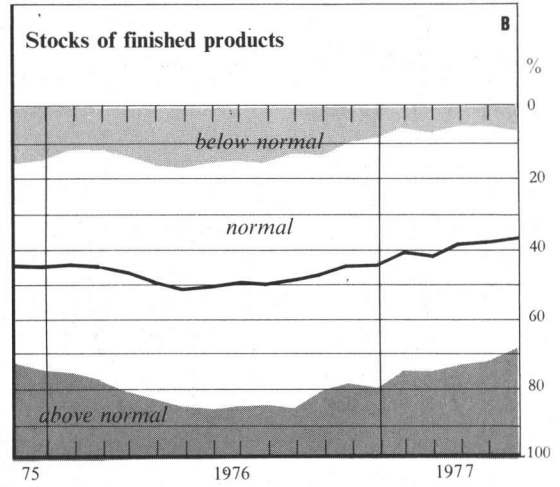
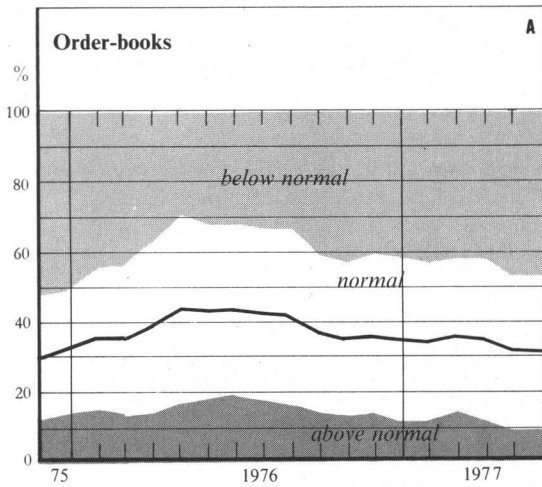


¹ Excluding military supplies.

¹ Excluding military supplies.

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

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

GRAPHS A, B, C and D: The three zones (grey, white and black) show the percentages of the three different answers.

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

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

number of measures whose main objectives were to sustain investment and to reduce unemployment. These measures supplement the plan for restoring equilibrium adopted in September 1976 (based on growth and employment hypotheses which subsequent developments showed to be ill-founded). As for investment, the measures essentially consisted of the loan on preferential terms of FF 4 000 million for the financing of new projects. As regards unemployment, the main measures adopted, at an estimated cost of FF 3 300 million for 1977 (0.2% of GDP), are ¹:

- the recruiting of 20 000 temporary employees in the public sector, the suspension of the employer's share of social security contributions in respect of the wages of young people newly recruited, a temporary facility making pension rights available at the age of 60, and a 'home return' bonus to out-of-work immigrant workers;
- the release of blocked public appropriations earmarked for spending on plant and equipment;
- an upgrading of various social security benefits to stimulate the consumption expenditure of households and of pensioners.

It is true that the macro-economic impact of this second group of measures will be small, but they have the merit of avoiding any threat to the restoration of external equilibrium, which is now under way. Moreover, the budget deficit will be affected to only a modest extent: the deficit should not exceed 0.8% of the GDP in 1977, compared with 1% in 1976. This means that this year France will once again rank as the Community country with the smallest budget deficit, expressed in relative terms. A final point is that the deficit will be financed by non-inflationary means, through loan issues and Treasury Bonds.

So far, monetary policy has remained mainly a dear-money policy designed to stabilize the franc and to attract foreign capital to finance the current payments deficit. These objectives have now been achieved. The increase in gold and foreign exchange reserves and an expansion of lending to industry and commerce has entailed a growth rate in the money supply (M2) close to the norm adopted for the full year of 12.5%.

Generally speaking, economic policy as redefined last September has yielded a number of initial successes in the drive to restore the main equilibria, particularly with regard to trade, and there are also tentative signs that the upward cost movement is slowing down. However, price inflation still remains substantial.

2. Recent developments

The key features of the first half of the year have been a spectacular contraction of the trade deficit, a slowing down of economic growth, growing unemployment and a temporary acceleration in the upward price movement.

In recent months, *domestic demand* has remained sluggish. Indeed, there is some evidence of a slight decline. For example, *consumption* expenditure has definitely slowed down and the demand for manufactured goods has even fallen. This movement should, however, be seen as a pause after the upsurge of purchases in the preceding

period when prices were blocked and the VAT rate lowered (see graph). It looks as if demand from *firms* has also lacked vigour. Most managements think their stocks are too high relative to present demand. The progress of investment expenditure has probably been moderate. The 'wait-and-see' attitude of managements in this connection is obviously connected with uncertainties as to political and social developments and with the high level of long-term *interest rates*, which have held firm despite the downward trend in the other Member States (except Denmark and Italy). Lack-lustre domestic demand was, however, offset to some extent in the first quarter by the strength of exports.

All in all, economic activity has only increased moderately. However, it should be noted that the production of consumer goods, at least at the beginning of the first semester, exceeded by a considerable margin the previous peak, reached in the summer of 1974. Some firms in this sector were operating at full capacity. This impression is corroborated by the persistent vigour of consumer goods imports in the first quarter. It is true that heavy imports are also partly accounted for by the fact that in the traditional industries certain countries with much lower costs enjoy a competitive edge. Moreover, these industries in France have suffered severely in recent years from the very sharp upward movement of the lower range of wages. Resulting efforts to achieve more rapid reorganization of production have naturally been concentrated on achieving productivity improvements and have involved little in the way of job creation. However, most large firms still employ excessive labour which discourages them from further hiring. Thus, the number of *job applicants* has again shown a marked increase since the beginning of the year, reaching 1 097 000 in May (seasonally adjusted), as against 930 000 at the end of last year. Nevertheless the labour market is still characterized by large structural disequilibria. In the construction industry alone more than 18% of firms declared last April that they could not increase their output due to difficulties of hiring qualified manpower, a figure unequalled at the same season since April 1974. The lack of skills is also demonstrated by the fact that in the same enquiry 81% of firms announced that they were experiencing difficulties in recruiting skilled workers.

Price inflation has remained serious and even worsened during the period. Nevertheless some progress has been made. The reduction in the standard VAT rate has been reflected in retail *prices*.² However the upward price movement gathered appreciable momentum in March/April for several different reasons — the inevitable catching-up process after the price freeze, the impact of higher raw material prices (a 95% rise between March 1976 and March 1977), a strong rise in food prices and the increase of public service charges in April by 6.5%, the maximum increase allowed for the entire year. In these circumstances, it is not easy to discern the underlying

¹ See also 'Main economic policy measures', annexed to this chapter.

² In most other Member States, the state of public finance inevitably entailed measures to step up revenue, including higher VAT rates. The healthy *public finance* situation in France enabled the authorities in January to lower the standard VAT rate — it was admittedly one of the highest in Europe — without jeopardizing efforts to scale down gradually the budget deficit. This measure has been costed at about FF 7 000 million.

TABLE 2

Demand for and supply of goods and services

France	1974 ²	1975 ²			1976 ²			1977 ³		
	At current prices bills FF	% change on preceding year								
		Vol.	Price	Value	Vol.	Price	Value	Vol.	Price	Value
Private consumption	776.9	3.1	11.6	15.1	4.9	9.9	15.3	3.5	9.0	12.8
Public consumption	174.2	5.5	14.2	20.5	4.8	11.1	16.3	4.1	9.3	13.8
Gross fixed asset formation	312.1	- 3.4	11.2	7.5	4.5	9.1	14.0	0.4	8.4	8.9
— Enterprises	170.2	- 7.4	11.5	3.2	7.2	6.2	13.8	0.7	7.5	8.3
— Dwellings	105.1	- 2.6	10.7	7.8	- 0.1	12.9	12.8	—	—	—
— General Government	41.4	10.5	12.3	24.1	5.4	10.4	16.4	3.5	9.5	13.3
Domestic final uses (excluding change in stocks)	1 263.2	1.8	12.0	14.0	4.8	9.9	15.2	2.9	8.9	12.1
Domestic final uses (including change in stocks)	1 290.7	- 1.2	11.8	10.5	7.0	9.8	17.5	2.2	8.9	11.3
Exports ¹	261.9	- 3.0	6.3	3.1	9.4	8.6	18.8	8.8	11.6	21.4
Imports ¹	280.8	- 8.7	1.1	- 7.7	19.5	9.5	30.9	3.9	12.5	16.9
Gross domestic product at market prices	1 271.8	0.1	12.9	13.0	5.2	9.6	15.3	3.1	8.7	12.1
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	1 263.2	1.8		13.9	4.8		15.2	2.9		12.1
Change in stocks	27.5	- 3.0		- 3.2	2.1		2.2	- 0.7		- 0.7
Balance of exports and imports ¹	- 18.9	1.3		2.3	- 1.8		- 2.0	0.9		0.7

¹ Goods and services

² Source: Comptes de la nation 1976.

³ Estimates of Commission's Departments

trend of prices. Some slowing down is however discernible. This is likely to continue as regards manufactured goods, for which the anti-inflation levy will probably be reactivated. The upward movement of *wages* has also begun to slow down: in the first quarter, for the first time in six years, the index for workers' hourly wage rates — increases in which are always higher than increases in average wages and salaries¹ — rose at an annual rate falling short of 10%.² Moreover, despite strikes, the Government and those responsible for public and private undertakings have in general shown firmness in applying the norm of a stable purchasing power in 1977. All in all, however, inflationary strain is still severe and a good deal more marked than in the countries belonging to the 'snake'.

External equilibrium has been restored very quickly, and the current account deficit is a good deal smaller — FF 6 900 million in the first quarter comparing with FF 10 000 million in the preceding quarter — due to the speedy reduction of the trade deficit (see graph). Success has been achieved in this area because the economy has moved beyond the exceptional situation which developed in the second half of 1976 as a result of the drought and the 'J-curve' effect of the decline in the value of the franc. In terms of value, *imports* have fallen from the abnormally high level reached at the end of last year. This indeed has also been the case in most of the other Member States. On the other hand, the expansion of French

exports — particularly to non-member countries — gathered momentum between December and March to reach an annual rate of increase of nearly 30%, implying, in terms of volume, nearly 20%. This record performance, which cannot last at a time when world trade is sluggish, is accounted for mainly by the competitive advantage gained by French exporters since the franc fell last summer, by the spontaneous recovery of exports of agricultural products and by the slackening of domestic demand, particularly for consumer goods. Since the second quarter, however, exports have lost a good deal of their vigour. This has not hampered the restoration of external equilibrium, which should be consolidated in the second half of the year.

3. Outlook

A further reduction of inflation and consolidation of external equilibrium should be achieved in the second half of the year. Growth remains moderate, and there is therefore little real prospect of an improvement in unemployment.

In coming months, domestic demand should gain strength. The consumption expenditure of households

¹ According to the Ministère du Travail earnings survey.

² It is true that the first quarter rise was influenced by the excellent results for prices in November, December and January.

TABLE 3
The Central Government Budget

France	1976			1977	
	Original budget		Provisional outturn ¹	Original budget	
	Mrds FF	% change ²	Mrds FF	Mrds FF	% change ²
Expenditure ¹	306.5	+ 18.7	351.5	349.5	+ 14.0
of which:					
— current expenditure	261.3	+ 18.6	294.9	—	—
— capital expenditure	45.2	+ 19.3	56.6	—	—
Revenue	306.2	+ 18.0	329.7	348.8	+ 13.9
of which:					
— direct taxes	125.9	+ 30.7	129.4	142.5	+ 13.2
— indirect taxes	147.5	+ 8.0	151.0	170.8	+ 15.8
Net borrowing requirement	0	—	-17.3	0	—

¹ Disregarding debt extinction.

² Relative to the original budget of the preceding year.

Note. The figures in this table are based on the national budgets and are recalculated on the basis of Community definitions.

should start expanding again, though at a moderate rate, in particular owing to the rise in social transfer payments from the middle of the year. There is still some uncertainty as to the investment decisions of private firms. But their finances are now in better shape, and for some of them, particularly in the consumer goods sector, the degree of capacity utilization is satisfactory. These conditions are necessary but not sufficient for a substantial recovery of investment, as long as the sales and profits outlook remains doubtful. Moreover, monetary policy is likely to remain restrictive: the non-inflationary financing of the budget deficit will tend to curb any tendency for interest rates to ease. It is certain that managements will not run down their stocks substantially, since policies with regard to stock levels have been extremely cautious since the last recession, but, for the full year, the increase in stocks should be smaller than that recorded in 1976. The 'mechanical' effect of this justifies the forecast of moderate growth—about 3%—of the GDP in 1977. Nor will this entail the creation of new jobs, since managements are unlikely to change their policy this year of relying on productivity gains to get their finances back on a sound footing. There is, therefore, no reason to expect a decline in the number of job applicants.

Good results should be achieved with regard to external trade, which in the last six months taken together: the expansion of imports will be modest and, for the full year, the import growth rate should, in annual average terms, exceed GDP growth by only a small margin. The exceptionally low elasticity of imports is mainly due to the lack of vigour of investment, especially in stocks. Exports will continue to expand at a rate exceeding slightly that of the growth of world trade: French exporters will probably not have completely exhausted the exchange rate 'premium' that accrued to them in 1976. For the full year, the current account deficit might well fall short of FF 15 000 to 18 000 million, compared with FF 27 500 million in 1976.

Some progress should be made in efforts to combat inflation. This should be the case with regard to the prices of manufactures, the increase in which for the full year may not greatly exceed the official norm of 6.5%. This achievement, however, is consistent with the reduction in the rate of price increases over the two years preceding the adoption of the government's plan last September. The upward movement in the prices of this category of products declined from 9.2% between September 1974 and September 1975 to 7.5% between September 1975 and September 1976.¹ The prices of manufactures are rising relatively slowly mainly because the domestic market is exposed to keen competition from outside, but also partly because productivity gains achieved in the recovery phase have largely made up the losses suffered during the recession. On the other hand neither of these factors had much impact in respect of food and services prices. Hence the corresponding increases in the two periods were 11.7% and 10.7% for food and 12.5% and 12.2% for services. It is therefore clear that any vigorous curtailment of the upward movement of retail prices as a whole will be impossible without far-reaching reform measures designed to eliminate certain structural rigidities in these two sectors.

Major economic policy measures

January:

— The standard VAT rate was lowered from 20% to 17.6%.

— A number of industries signed price agreements with public authorities (5.5% to 6% increase in 1977). Managements failing to respect these undertakings will be brought back under the administrative price control scheme.

February:

— More credit was assigned to encouraging exports. FF 3 000 million of new credit at the reduced rate of 9% are earmarked for the financing of the

¹ The two twelve-month periods coincide roughly with the recession and recovery stages: prices were frozen only in the last quarter of 1976.

investments of firms undertaking to export more and FF 1 800 million of new credits at the special rate of 3% are made available to developing countries buying French plant and equipment.

— Several improvements were made to the arrangements for compensation for shorttime working. The minimum hourly wage will be raised from FF 8.40 to FF 8.60 on April and FF 8.85 on 1 September.

March:

— Parliament adopted an Amending Finance Act for 1977 showing a budget deficit of about FF 10 000 million.

— The government provided FF 4 000 million for financing new investments of which FF 2 000 million is earmarked for small firms and handicrafts and FF 2 000 million for large firms.

April:

— The minimum hourly wage (SMIC) was raised from FF 8.94 to FF 9.14, an increase of 2.10% since 1 July.

— Most public service charges were raised on 1 April by 6.5%, the maximum increase authorized for the entire year.

— Issue of a public loan of FF 2 000 million, the yield of which will be made available to small and medium-sized enterprises for the financing of job-creating investment.

May:

— Parliament adopted a plan designed mainly to combat unemployment. It includes the following measures:

Direct support of employment:

— charging to the budget until 1 July 1978 the employer's share of social security contributions relating to the wages of young persons taking their first job between the dates on which the law was adopted and the end of 1977 (providing there is an actual increase in the numbers employed by the firm).

— charging to the budget, throughout the apprenticeship, of employer's social security contributions relating to wages paid to apprentices recruited between the date of the voting of the law and 31 December 1977.

— negotiations with employers' and workers' organizations designed to achieve temporary extension of early retirement arrangements (70% of the wage for employees released after the age of 60 for economic reasons) to any employee under 65 wishing to avail himself of the arrangements (the income cannot be combined with any other income from work).

— Organization of traineeships for persons under the age of 25 wishing to supplement occupational training received (pay will be 90% of the SMIC).

— Granting of FF 10 000 aid to redundant immigrant workers wishing to return home.

— Exemption from social security costs until 31 December 1977 for firms recruiting workers between the date of the voting of the law and 31 December 1977 for the purposes of employing them abroad; they also qualify for a mobility premium.

— Recruitment in the public sector of 20 000 additional temporary employees on a full-time or part-time basis.

— Extension of employment training contracts (now available to women under 25 years of age) to widows and women living alone, whatever

their age, having at least one dependent child and wishing to resume paid employment.

Assistance for families:

— 10.2% increase in family allowances.

— Increase in funds available to the National Fund for Health and Social Action, mainly designed to facilitate an increase in the number of family assistants and an increase in the number of nurseries.

— The threshold for full cumulative entitlement to reversionary pensions and personal pension rights was raised on 1 July 1977 to 60% of the maximum pension paid by the general scheme.

— Improvement in the family supplement and in temporary leave for mothers.

Aid to the elderly:

— Increase in the minimum old age pension from FF 9 000 to FF 10 000 for a person living alone on 1 July 1977, and to FF 11 000 on 1 December 1977.

— Improvement in living conditions (housing, home help arrangements, cancellation of the 'liable relative' rule, and improvement, for elderly and handicapped persons and persons living alone, of the telephone service and of the warden scheme).

— Flat-rate 5% increase in pensions paid before 1 January 1973, from 1 October 1977.

— FF 5 000 tax reduction on the income from the last year of work.

Investment support:

— Increase in payment appropriations by a total amount of FF 625 million.

— Use of the Economic Action Fund up to FF 1 250 million, of which FF 600 million in payment appropriations.

The cost of these measures will be about FF 3 300 million in 1977. FF 1 500 million should be financed as follows:

— Higher taxes on petroleum products (by from FF 0.04 to 0.06 per litre).

— Adjustment of the arrangements for recovering certain insurance and banking fees.

The budget deficit would thus rise from FF 10 000 million (Amending Finance Act of March 1977) to FF 11 800 million. The deficit will be financed as follows:

— Issue of an FF 8 000 million 15 year 8.8% loan (guaranteed by indexation of the capital against the European Unit of Account).

— The residue (about FF 4 000 million) to be recovered by drawing on short- and medium-term savings (including Treasury Bonds).

June:

— Fruit and vegetable wholesale margins are blocked at their 1976 level.

— The Government imposed import quotas on certain textile products with the share in the market of non-Community countries limited to the 1976 level. To prevent this measure leading to price increases, these will be blocked.

— The Government took a series of measures against the structural causes of inflation, notably as regards distribution networks, labour mobility and waste of raw materials.

D – Ireland

Most recent developments in the Irish economy have been an improvement in growth and some small reduction in unemployment which, however, still stands at about 9½%. The rate of inflation remains rapid although there is some deceleration in the year to year increase. The current balance of payments deficit is quite high, given that the economy is operating below capacity growth rates.

The main thrust of the authorities' action has been in the area of income policy where a moderate wage agreement for 1977, linked to tax changes and increases in public expenditure aimed at employment creation, has been agreed. In addition, considerable incentives have been offered to enterprise, to improve output and take on more employees.

The outlook is for a higher rate of growth in coming months (resulting in nearly 4% growth for the year as a whole), mainly due to investment and exports and some decrease in the inflation rate from the high level of the first half of the year, due to the working through of the impact of the pay agreement and the stability of sterling. Unemployment is likely to fall but still be around the 100 000 level at the end of the year and the balance of payments deficit for the year should be about £ 280 million.

1. Overall assessment and main policy issues

Most recent developments in the Irish economy appear more promising than was the case in the Commission's review published in December 1976. At the time the most urgent problem was cited to be 'to curb the growth in nominal incomes in order to improve exports thus avoiding any worsening in unemployment' and at the same time reduce inflation. Since then the negotiations for a national pay agreement¹ which will cover the period to the end of 1977 have been completed and the overall outlook now for cost developments is more favourable. One of the other points mentioned in the December survey was that incomes restraint should not be confined exclusively to the industrial sector and that net agricultural incomes should also be affected. A further step in this direction was taken in the Budget of 26 January when the Minister for Finance extended agricultural taxation to include 9% of farmers, instead of the 5% affected up to that time. Nevertheless this year agricultural incomes are expected to grow by about 35% while wages and salaries progress by a more modest 14-15%.

The inflationary problem, although being less pronounced now than at the middle of last year, still remains. Inflation has stayed high as import prices still reflect the depreciation of sterling in the second half of 1976. The rise in food prices resulting from recent green pound alterations and this year's agricultural price review are also making themselves felt although they have been cushioned by increased food subsidies introduced by the Irish authorities.

The fall in jobless during the initial part of the year was more modest than normally expected, given that in-

dustrial production has now passed beyond its pre-recession peak, and recent figures point to a slowing in the downward fall. This development may be due to certain exceptional factors but even taking these into account the problem remains pressing. The authorities, in addition to placing reliance on their incomes policy strategy, have introduced certain employment creating measures² designed to alleviate the situation where 9½% of the labour force is out of work. These projects include additional government expenditure, employment premiums and reduced corporate taxation.³

However, perhaps the most notable change in government strategy in the period covered was the increased tax reliefs offered to enterprise and wage and salary earners, whereas budgets in the recent past had concentrated on developing social services.

As was stated in the Commission's Communication to the Council on the adjustment of economic policy for 1977, budgetary policy fits well into the framework of the guidelines set out in the Annual Report. However, the advice in the former that the Finance Act should not contain concessions which would increase the borrowing requirement does not appear to have been followed in the case of receipts from agricultural taxation. Nevertheless, it is expected that this shortfall in receipts, together with the higher subsidies recently announced to insulate households from increases in agricultural prices, will not inflate the borrowing requirement.

¹ The new national agreement is described in the Section 4.

² See list of measures below (January and May).

³ Details of these measures are to be found in the annex.

TABLE 1
Key indicators

Ireland	Unit	1970-1974 average ^{4,5}	1975 ⁵	1976 ⁶	1977 ⁶
Gross domestic product, volume	% change	3.6	0.4	3.2	3.7
of which: industry ¹		4.1	- 6.2	9.0	8.0
Gross domestic product in volume per person in employment	% change	3.6	1.3	4.2	3.2
Total employment (number of persons) ²	% change	0	- 1.8	- 1.0	0.9
— Independent entrepreneurs		:	:	:	:
— Wage and salary earners in company sector		:	:	:	:
— General Government		:	:	:	:
Unemployment	as % of labour force	5.9	7.9	9.4	9.3
Compensation of employees per wage and salary earner	% change	12.2	24.6	18.0	12.0
Price index of private consumption ³	% change	10.8	21.3	18.0	14.5
Current account balance ³	£ mio	-109.4	- 18.0	- 150	- 280

¹ Value added at constant prices, including construction.

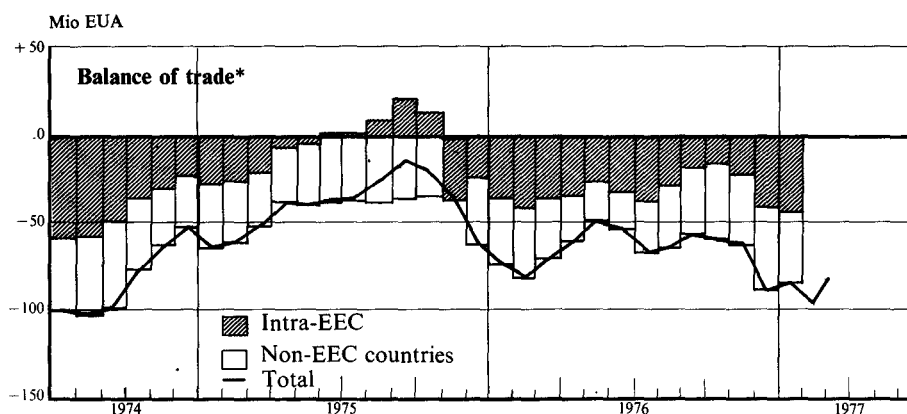
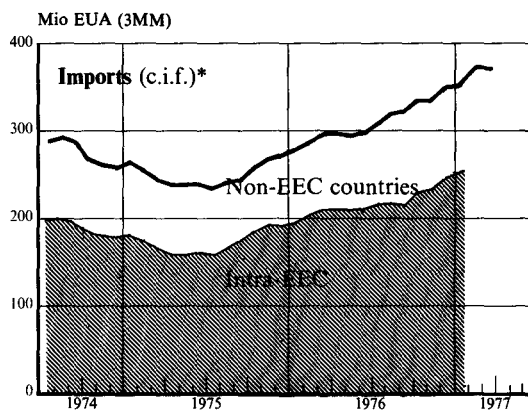
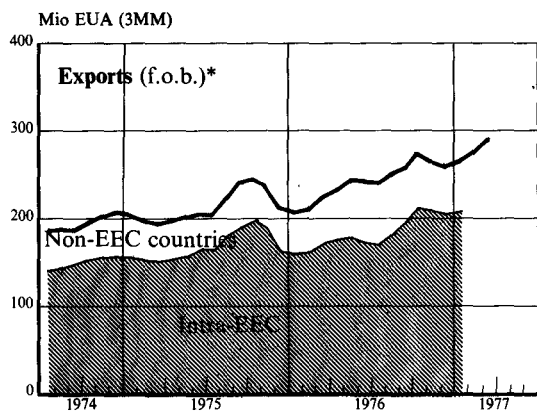
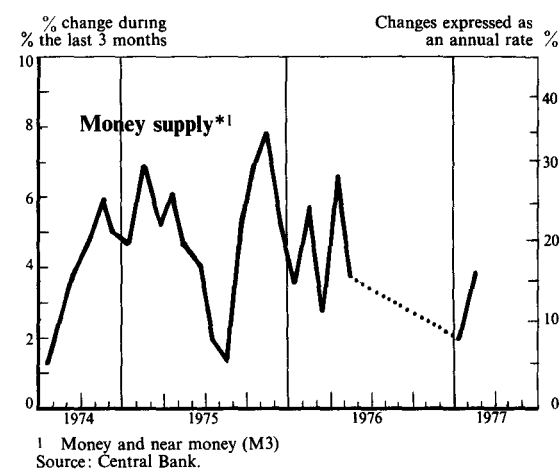
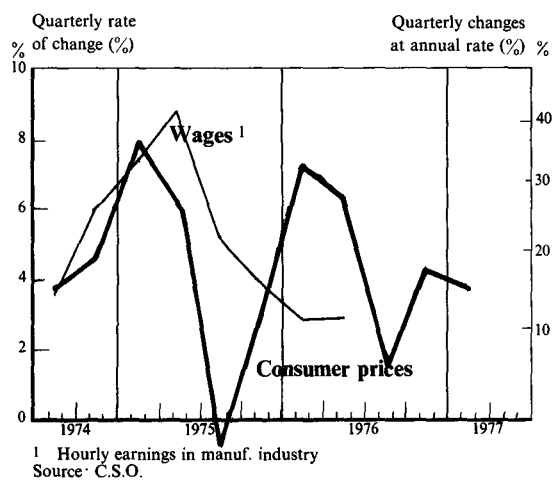
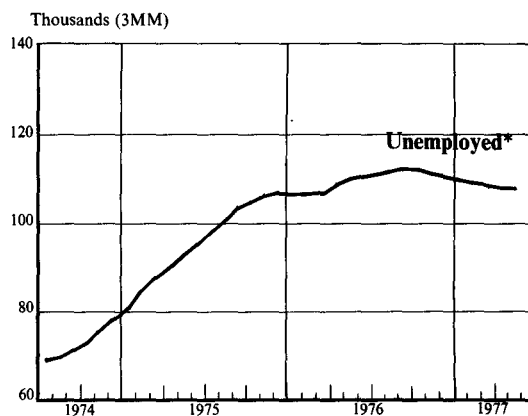
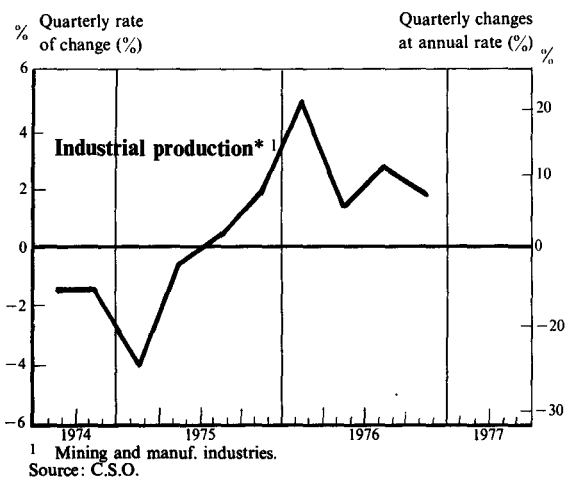
² Domestic concept

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

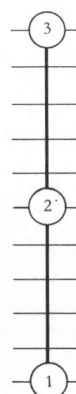
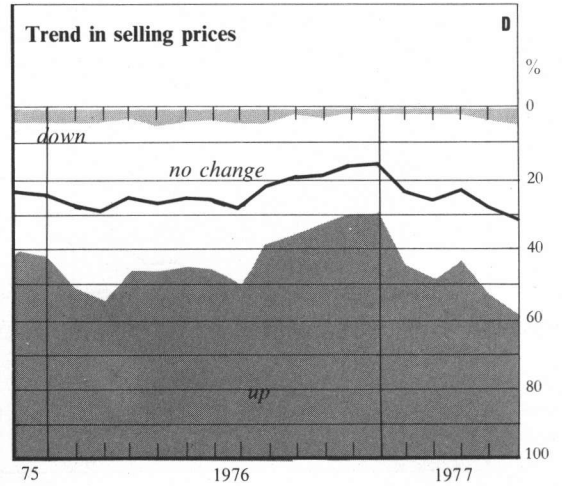
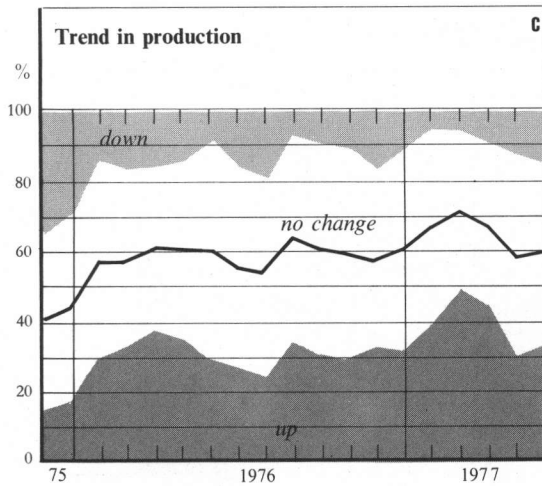
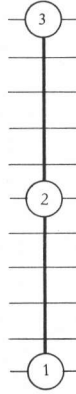
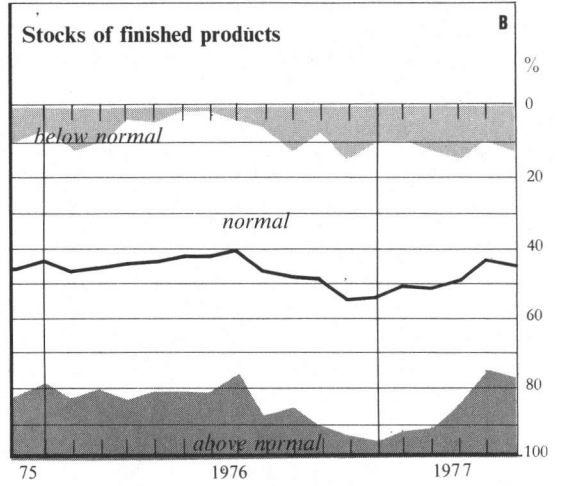
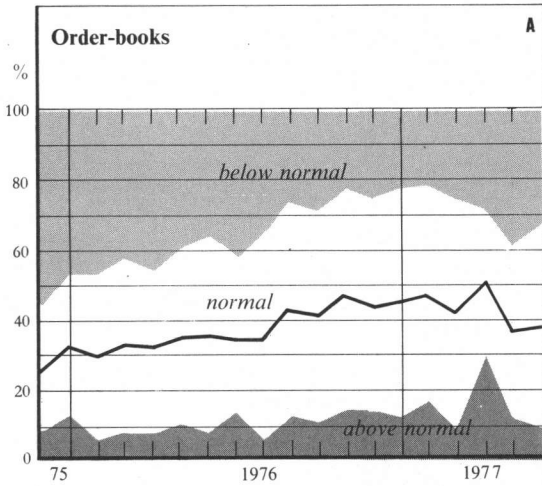
⁵ Source: Estimates of Commission's Departments

No data available



*:Seasonally adjusted.
3MM: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to questions in the EEC business survey, carried out in Ireland by the CII-ESRI.

GRAPHS A, B, C and D: The three zones (grey, white and black) show the percentages of the three different answers.

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

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

2. Recent developments

Latest trends suggest that the economy is growing at a level nearer its long-term trend rate. Most of the stimulus has come from investment and exports in recent months. Consumption has been relatively static; the private sector feeling the squeeze on disposable incomes and the public sector still subject to strict budgetary control. Production is progressing satisfactorily on the industrial front, although not maintaining the exceedingly fast pace of last year. In common with experience elsewhere, employment is increasing but not at the rate which might have been expected in this phase of the cycle. Prices rose at a quarterly rate of 3.8% in February and May. The trade deficit was particularly high in the first five months of the year and, although, to some extent due to the sluggishness in agricultural exports caused by institutional factors (i.e. the Community price review), it reinforces the view that the balance of payments deficit could become a major constraint in capacity growth conditions.

Exports progressed by 11%¹ in value in the three months to May compared with the period December-February. Industrial exports grew by 10%. This rate when expressed in annual terms is about the same as the rise recorded in 1976, despite a slower growth in export markets (7½% foreseen as against 11% last year). Agricultural sales abroad recovered in this period and were 13% higher than in the preceding three months.

Retail sales in volume in the first quarter of the year showed no change on the previous three months. Data for *consumption* after the implementation of the tax changes and the main increases under the national pay agreement is not yet available but it is not expected to have picked up very sharply except perhaps for consumer durables.

Investment in general appears to be accelerating sharply. However, conflicting movements in its components are apparent. Machinery and equipment installation is growing vigorously. Replies by managements to the business survey carried out in the Community support the evaluation that investment in equipment is booming. Thus only 12% of managements regard production capacity as being more than sufficient compared to a Community average of 38%. In addition, Irish entrepreneurs are the most optimistic regarding production activity in the coming months, 36% on balance with higher expectations as opposed to a Community average of 2%. On the other hand, residential construction is relatively sluggish. Public investment in value for the first quarter of the year is slow but it is unlikely that last year's experience where investment funds budgeted for were not actually spent, will arise again.

The latest available *industrial production* figures are for the first quarter of 1977 and show a quarter-to-quarter

¹ Seasonally adjusted.

TABLE 2
Demand for and supply of goods and services

Ireland	1974 ²	1975 ²			1976 ²			1977 ³		
	At current prices £ mio	% change on preceding year								
		Vol.	Price	Value	Vol.	Price	Value	Vol.	Price	Value
Private consumption	2 007.6	- 3.3	21.8	17.8	2.8	17.0	20.2	2.0	14.5	16.8
Public consumption	523.0	5.6	26.7	33.8	2.0	19.7	22.1	2.0	16.0	18.3
Gross fixed asset formation	776.3	- 6.5	20.3	12.5	4.4	17.9	23.1	8.0	18.0	27.4
— Enterprises	:	:	:	:	:	:	:	:	:	:
— Dwellings	:	:	:	:	:	:	:	:	:	:
— General Government	:	:	:	:	:	:	:	:	:	:
Domestic final uses (excluding change in stocks)	3 306.9	- 2.6	22.3	19.1	3.0	17.7	21.2	3.4	15.6	19.5
Domestic final uses (including change in stocks)	3 400.4	- 8.0	23.7	13.8	6.7	16.4	24.3	4.6	15.6	20.9
Exports ¹	1 274.1	6.6	20.1	28.0	8.4	21.8	32.1	9.0	17.5	28.1
Imports ¹	1 718.3	-11.6	20.8	6.8	15.4	17.6	35.7	10.0	20.0	32.0
Gross domestic product at market prices	2 956.2	0.4	23.5	24.0	3.2	18.3	22.0	3.7	14.0	18.2
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	3 306.9	- 2.9		21.4	3.2		22.8	3.6		20.8
Change in stocks	93.5	- 6.3		- 5.5	3.9		2.8	1.4		1.7
Balance of exports and imports ¹	- 444.2	9.6		8.1	- 4.0		- 3.6	- 1.2		- 4.3

¹ Goods and services.

² Source: Economic Review and Outlook - June 1977.

³ Estimates of Commission's Departments.

: No data available.

increase of 1.3%. Again judging from the surveys, on balance 2% of industrialists report orderbooks above normal at a time when the Community average is 33% below. The investment and consumer goods groups are more buoyant while the intermediate goods sector is still affected by insufficient demand. Within the various groups non-electrical machinery and furniture are the most dynamic areas of activity while textiles and clothing are at the other end of the scale suffering mainly from the weak domestic market.

The unemployment situation, after a decline from 111 000 in December has tended to stabilize at 109 000 of late. ¹ This may, to some extent, reflect the indirect effect of strikes in certain areas but it would seem that the industrial revival has not had, so far, the expected effect on *unemployment*. This is mainly due to the high growth in the labour force but may also reflect a greater proportion of capital intensive investment and, perhaps, a greater reluctance to hire employees because of the expense involved in dismissing them.

The quarter-to-quarter increase in *prices* in the second three months of the year was the same as in the first quarter, i.e. 3.8%, but this brought the year-to-year increase down to 13.9%. The effect of food subsidies in holding down the rise should, however, be mentioned.

Imports have been relatively buoyant, increasing by 5.6% in the period March-May on the previous three months. The trade deficit has been £160 million for the three months in question.

Despite this development and no external government borrowing, official external *reserves* increased by £5 million from February to May, reflecting increased capital inflows, mainly through the banking system. Broad *money supply* was relatively restrained in the early part of the year but accelerated more recently to 15½% on a year-to-year basis in May as a result of a greater demand for private credit. In addition, the level of official

balances with the Central Bank is still quite high. A reduction of these to a working balance level would give a substantial boost to the money supply. The Annual Report on the Economic Situation in the Community adopted by the Council stated that the increase in the money supply should be kept below the growth of GDP in value and this seems likely to be realized in 1977. Interest rates have been reduced successively in recent months.

3. Outlook

Developments in the coming months should result in a higher growth rate than previously forecast. This will be mainly due to a more sustained performance of exports and private consumption on the demand side and some recovery in agriculture as far as output is concerned.

Exports will progress considerably more rapidly than in the early months of the year and their market share should increase markedly. Consumption should be more buoyant in the second half of the year, as the tax and other measures come through, although the 2% real growth rate contained in the annual forecast is thought to be in the upper region of the possible range. The performance of investment should weaken slightly in the second half of the year as order books begin to thin out.

Industrial production should on the other hand continue at much the same level but perhaps taper off somewhat towards the end of the year. Agricultural output will increase rapidly as producers take advantage of the considerably higher prices to boost their sales. Unemployment is expected to fall, although official figures could still be around 100 000 seasonally adjusted at the end of the year.

Consumer prices are likely to slow down dramatically, given the absence of external shocks, since unit wage costs should be relatively stable.

¹ Seasonally adjusted figures.

TABLE 3
The Central Government Budget

Ireland	1976			1977	
	Original budget		Provisional outturn	Original budget	
	£ mio	% change ²	£ mio	£ mio	% change ²
Expenditure ¹	2 164	20.5	2 197	2 563	16.7
of which:					
— current expenditure	1 751	24.2	1 748	2 118	21.2
— capital expenditure	413	7.3	449	445	— 0.9
Revenue	1 512	5.7	1 717	2 000	16.5
of which:					
— direct taxes	660	23.4	705	877	24.4
— indirect taxes	677	15.7	749	878	17.2
Net borrowing requirement	652	79.1	480	563	17.3

¹ Disregarding debt extinction.

² On the preceding year's original budget.

Note: The figures in this table are based on the national budgets and are recalculated on the basis of Community definitions.

TABLE 4
Main economic indicators

	Year	Jan.	Feb	Mar	Apr	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec
Industrial production* (1970 = 100)	1974		121.4			118.8			116.9			115.1	
	1975		110.4			109.8			110.3			112.5	
	1976		118.2			120.0			123.5			125.8	
	1977												
Unemployed* (1 000)	1974	64.4	65.4	65.2	66.0	67.3	68.4	69.3	70.8	74.0	75.3	78.3	80.3
	1975	85.1	87.6	90.9	93.7	96.8	99.7	100.9	103.1	104.5	106.8	107.0	108.1
	1976	105.3	107.6	109.4	110.3	110.4	110.7	113.0	113.2	112.0	111.9	111.5	110.7
	1977	108.5	108.0	108.4	108.0	107.6	:	:	:	:	:	:	:
Construction*	1973	3 501	4 945	4 229	1 670	2 127	1 271	1 900	2 079	2 750	2 333	2 027	2 019
	1974	2 164	1 157	2 741	2 833	2 310	2 102	2 110	2 215	2 407	2 078	1 875	1 951
	1975	1 646	1 223	1 536	2 451	1 839	2 403	1 886	2 135	2 187	1 888	1 757	2 451
Private consumers' expenditure* (1970 = 100)	1974	152.6	157.8	156.1	165.4	161.6	163.1	168.1	168.4	171.0	171.8	175.7	176.8
	1975	179.7	177.1	180.8	183.3	194.5	189.4	195.6	194.1	206.2	207.6	211.5	226.4
	1976	222.2	232.7	218.2	230.3	232.3	238.7	229.7	225.3	247.2	247.2	257.4	257.4
	1977	245.8	255.4	:	:	:	:	:	:	:	:	:	:
Consumer prices (1970 = 100)	1974		143.5			151.5			157.3			164.5	
	1975		177.8			188.6			187.1			192.2	
	1976		206.2			219.1			222.4			231.8	
	1977		240.6			:			:			:	
Visible imports* (million EUA)	1974	217.8	234.6	257.9	284.6	288.1	269.1	297.2	300.0	281.9	282.9	250.5	257.1
	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	:	:	:	:	:	:	:	:	:
Visible exports* (million EUA)	1974	163.3	168.5	167.7	177.0	178.2	177.5	200.2	183.6	183.6	199.3	206.0	203.4
	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	:	:	:	:	:	:	:	:	:
Balance of Trade* (million EUA)	1974	- 54.8	- 66.1	- 92.5	- 109.9	- 114.4	- 92.1	- 97.7	- 104.5	- 93.5	- 83.7	- 44.5	- 53.7
	1975	- 62.4	- 70.9	- 48.0	- 41.1	- 28.7	- 48.9	- 26.8	- 24.6	- 21.8	+ 7.1	- 43.7	- 76.0
	1976	- 66.2	- 74.7	- 102.9	- 41.0	- 45.9	- 62.3	- 54.8	- 78.3	- 50.6	- 33.9	- 90.3	- 71.9
	1977	- 121.0	- 85.2	- 100.3	:	:	:	:	:	:	:	:	:
Official foreign exchange reserves (million EUA)	1974	854	800	847	802	827	787	924	1 041	978	998	1 000	992
	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	:	:	:	:	:	:	:	:
Money supply (million EUA)	1974	1 052	985	1 050	1 011	1 000	1 015	1 002	1 018	1 038	1 016	1 022	1 051
	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	0	0	0	0	1 071	1 099	1 191
	1977	1 152	1 121	:	:	:	:	:	:	:	:	:	:

Not available

* Seasonally adjusted

Source: EUROSTAT (except as otherwise indicated).

- Industrial production CSO, Mining and manufacturing industry
- Unemployment Number of registered unemployed
- Construction Total of dwellings begun or authorized
- Private consumers' expenditure Retail Sales Index in value
- Visible trade Imports cif, exports fob
- 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

Imports will undoubtedly be more restrained but, given the buoyant rate of investment activity, their year-to-year growth rate for 1977 should still be substantial. Despite some improvement projected in the terms of trade, the current balance of payments deficit will remain high and the annual outturn is expected to be of the order of £280 million. EEC net transfers at about £160 million will play

an important role in containing the deficit at this level in 1977.

The major problem facing the authorities is to ensure that the current national pay agreement is strictly observed by the social partners and that further moderation is forthcoming in 1978. This should be facilitated by further

progress registered in the fight against inflation and by way of a more even distribution of the tax burden by sector of activity. Given the spontaneous dynamism of the economy in the second half of the year, demand management policy will play a particularly important role. In the hypothesis that stimulatory measures are proved to be advisable to stimulate employment further, it would be appropriate to avoid creating risks for the balance of payments through an unduly rapid expansion of private demand.

Major economic policy measures

January 1977:

— On 21 January agreement was reached at the Employer Labour Conference on the final text of a new national pay agreement. The agreement provides for a pay pause of three months and two phased increases of 2 ½% plus £1 per week, the first increase to be paid immediately after the pause, and the second seven months later. Each phase is subject to a minimum increase of £2 a week and a maximum of £4.23. The agreement lasts for fourteen months and applies to some workers from 1 November 1976 and the majority from 1 January 1977. The increases in average terms correspond to two increases of approximately 4 ½%.

— The main objectives of the budget presented by the Minister for Finance on the 26 January 1976 were to improve the rate of economic growth by encouraging incomes restraint, by providing effective incentives for enterprise, and by continuing with the realignment of public expenditure towards maximization of investment and a reduced dependence on borrowing. The main instruments used to achieve those objectives were reductions in personal and corporate taxes, a special package of public expenditure allocations designed to maximize job-creation and a number of measures designed to reduce household living costs. The principal elements were:

- an increase of 21 ½% of *current expenditure*; the most significant rises being in the health and education areas. Expenditure was also provided for a new scheme to increase employment and for fishery protection. Food subsidies were increased and the State will also bear one-quarter of the local authority rates. Social welfare transfers were raised and the qualifying age for old age pensions is to be reduced from 67 to 66 years in October.
- an increase of 21.7% in *capital expenditure* with specific expenditures designed to increase employment. These included an extra £12 million for industrial investment, £12 million for construction, £5 million for infrastructural development and £5 million for agricultural modernization and loans to industry;
- a marked reduction in income taxation in particular on higher salaries, the maximum rate being reduced from 77% to 60%, at a cost of £50 million;
- a fall of 5% in corporate taxation and an increase in exemption limits for smaller industries;
- a reduction in taxation on firms increasing their output and employment to a significant extent;
- an increase in agricultural taxation and an extension of its coverage to produce an additional £35 million;

- an extension of provisions for accelerated depreciation up to 31 March 1979 and a prolongation of stock relief;
- rises in postal and telephone charges of 13 and 25% respectively;
- a speeding up of the collection of taxation on independents;

As far as the *borrowing requirement* was concerned a reduction from 11 ½ to 11% of GNP was budgeted for.

February:

- The national pay agreement was ratified by the social partners.

March:

- Agricultural Ministers of the EEC decide on a devaluation of 6.25% in the Irish green pound.
- The Government agreed to establish a joint working committee with the trade unions to consider possible initiatives in regard to employment.

April:

— Agriculture Ministers of the EEC decide on an average increase of 3 ½% in Community agricultural prices for 1977/78.

— The Government decided to provide increased consumer subsidies of £10 million in a full year to offset the rise in food prices resulting from the increases in agricultural prices caused by changes in the green pound and the agricultural price review.

— The Finance Bill containing the detailed scheme for the reduction from 45% to 25% of corporate tax on companies increasing production and employment was published. The main conditions are that the value of sales in 1977 is at least 5% up on sales in 1976 and that the number of employees in 1977 is at least 3% higher than the level in 1976. Other conditions are that 95% of sales are sales of goods manufactured by the company itself, that 95% of its income comes from the specified trade and that the trade was in existence in 1976.

— In the case of farm taxation certain concessions have been allowed for wages of permanent employees in the Finance Bill. In addition, only half the tax payable for 1977/78 will now be due in September 1977; the balance will be payable in January 1978.

May:

— The Government approved the payment of the second phase of a pay deal for building workers, who had earlier threatened a national strike, following an adjudication by the Employer/Labour Conference that the deal conforms to the national pay agreement.

— Details of the scheme announced in the budget to encourage employers to take on more workers were finalized. The Employment Incentive Scheme offers a £20 tax-free payment per week for each new employee taken on in industry and agriculture from 24 February. It is hoped to make an extra 11 000 jobs available. The scheme applies to workers over 20 years of age who have received unemployment benefit or assistance and have been unemployed for at least four weeks, those under 20 receiving unemployment benefit and unemployed for at least four weeks and redundant apprentices who satisfy these conditions. A £10 a week premium for school leavers under 20 years left school for at least four months and with no previous permanent employment was also introduced. The scheme will operate to 24 February 1978 and premiums will be payable for about 24 weeks for each eligible worker.

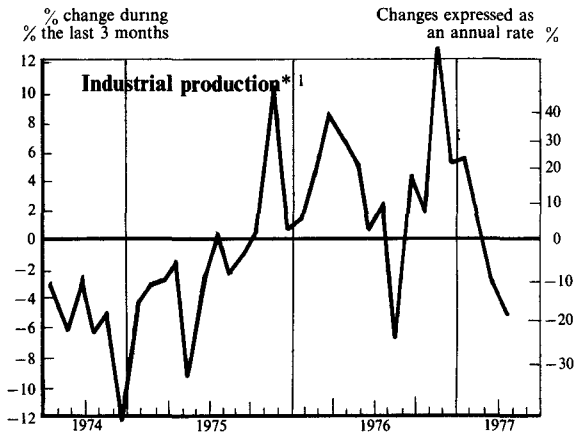
— The Central Bank announced steps to curb the inflow of foreign funds into the banking system. These involve the reimposition that banks deposit 50% of their foreign capital inflow with the Central Bank.

E – Italy

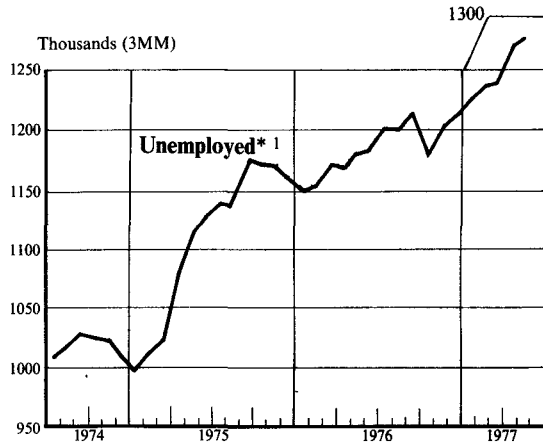
The economic upswing which began late in 1975 continued in the first quarter of this year. In the early months of 1977 it was sustained by domestic demand, and more particularly by investment. According to ISCO calculations, seasonally adjusted, industrial production was 2% up on the final quarter of 1976, when its growth had already been unusually rapid; in April, however, it fell again appreciably. At the same time prices continued to climb steeply, partly because of special factors. Overall, the balance of payments deteriorated significantly. The level of employment still tended to rise, but the number of unemployed also increased once again.

Economic activity is now likely to be affected by the restrictive economic policy in force particularly since last autumn. Even so, real gross domestic product is expected to grow by some 3% between 1976 and 1977 and employment to rise further. The upsurge in prices, though likely to ease distinctly, will still be very vigorous. The improvement in the balance of payments on current account will probably be considerable, but still insufficient.

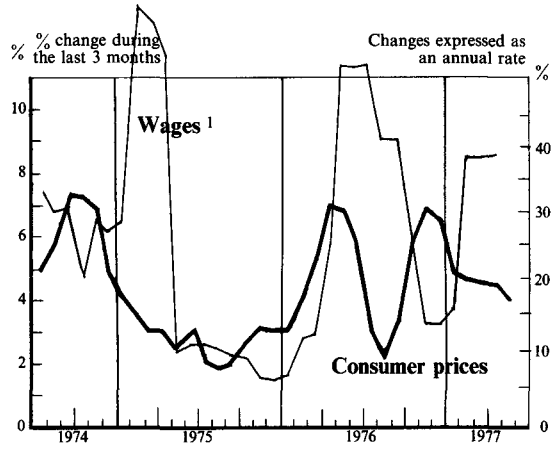
There would seem to be an urgent need to supplement short-term economic policy action by structural measures, in order to reestablish the basis for a rapid increase in production and employment.



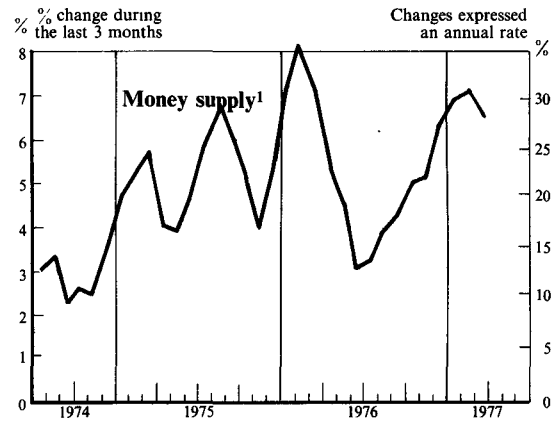
¹ Excl. construction.



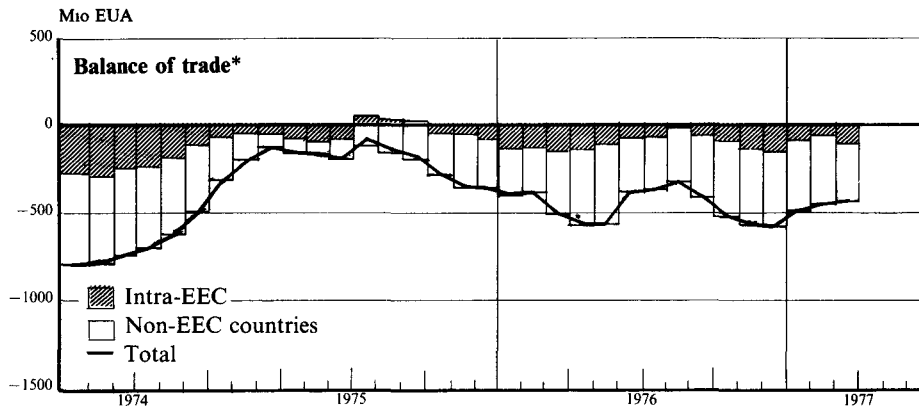
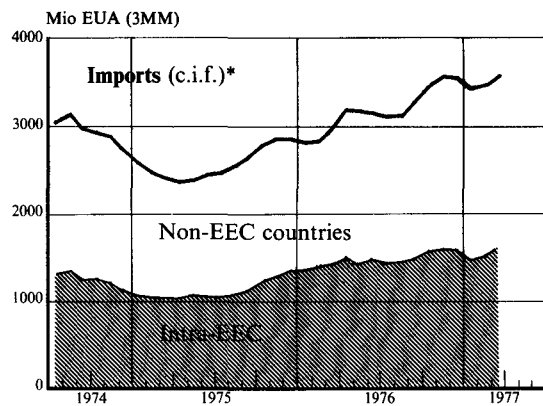
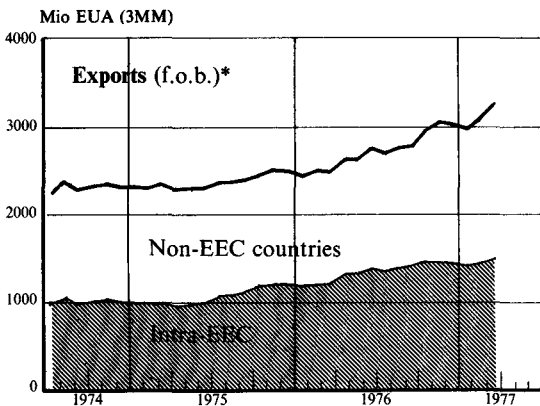
¹ Registered unemployed (seasonally adjusted by SOEC).
Source: Min. del Lavoro e della Previdenza Sociale



¹ Agreed minimum wages in industry (excl. family allowances)
Source: ISTAT

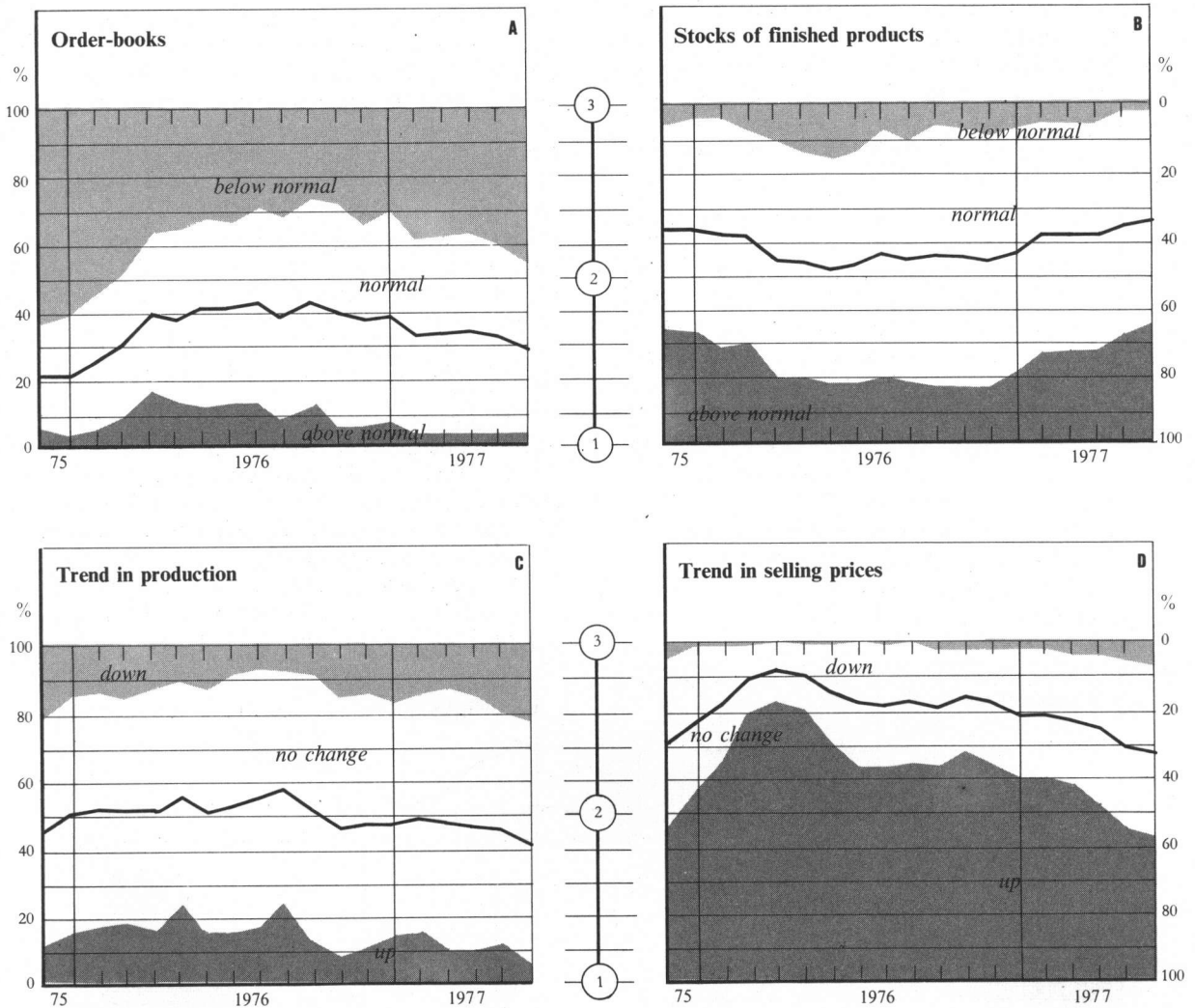


¹ Stock of money and near-money (M2).
Source: Banca d'Italia



*:Seasonally adjusted figures.
3MM: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

GRAPHS A, B, C and D: The three zones (grey, white and black) show the percentages of the three different answers.

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

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

1. Overall assessment and main policy issues

The rapid upsurge in costs and prices and the balance of payments difficulties which were experienced in 1976 and partly also in early 1977 and which last year led to repeated lira crises, showed once again how difficult it has become in Italy to reconcile rapid economic growth with satisfactory domestic and external equilibrium. The Italian authorities reacted to these difficulties mainly by taking a number of immediate measures, by tightening credit policy, by launching last autumn a phased programme with the emphasis on taxation policy and public service charges, and by introducing a scheme to curb the rise in labour costs, in which the two sides of industry cooperated.¹ Despite the restrictive economic policy stance, economic growth continued in the first quarter of 1977, though at a slower pace. At the same time the number of unemployed still tended to rise.

The stabilization efforts so far made by the government are clearly in line with the short-term economic policy need to restrain the growth of domestic demand and to improve Italy's international competitiveness. The economic policy conditions¹ laid down, in connection with the grant of further loans, by the International Monetary Fund and by the Council of the European Communities in the spring of this year are directed at the same objective. The Council's conditions include a ceiling on:

- central government expenditure in 1977 and 1978;
- (for the first time) the total public sector deficit (including that of ENEL, the state-controlled electricity undertaking) in 1977 and 1978;
- the combined deficit of the Treasury and local government in 1977;
- the Treasury deficit alone and its monetary financing in 1977;

— the growth in total domestic lending in 1977.

However, further economic policy efforts would seem to be necessary if these conditions are to be met. In addition, structural measures must be taken to reestablish the basis for a rapid and sustained increase in economic activity and employment.

2. Recent developments

After a sharp rise in the previous nine months, the value of merchandise *exports* in the first four months of 1977 ceased to rise, and according to the ISCO seasonally adjusted figures, actually declined. As was the case a year earlier, this was probably a phase of consolidation or simply a reflection of purely technical and statistical factors. In the first four months the value of exports was 38.5% and the volume some 7.5% up on a year earlier. Deliveries to oil-producing and state-trading countries seem to have been quite buoyant. Exports of services, particularly tourism, were still expanding: foreign exchange receipts from services generally were 25% and those from tourism no less than 84% up on a year earlier; however, the second figure was probably inflated by a reduction in some forms of the illegal export of capital.

According to the indicators (mostly qualitative) available so far, domestic demand was also higher in the first four months than in the preceding period. Despite last autumn's austerity measures, the expansion in the volume of *private consumption* continued, though at a slower rate: this seems to have been partly due to the massive increase in the cost-of-living supplements based on the sliding wage scale, but also to a decline in households' propensity to save, itself probably the result of fears of further sharp

¹ See the list of measures at the end of this chapter.

TABLE 1
Key indicators

Italy	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁵	1977 ⁶
Gross domestic product, volume	% change	4.1	— 3.5	5.6	3
of which: industry ¹		4.3	— 9.2	12.0	5
Gross domestic product in volume per person in employment	% change	3.8	— 3.6	4.8	2½
Total employment (number of persons) ²	% change	0.3	0.1	0.8	½
— Independent entrepreneurs		— 2.6	— 0.9	— 0.1	— ½
— Wage and salary earners in company sector		1.6	0.6	1.2	1
Unemployment	as % of labour force	3.3	3.3	3.7	3.9
Compensation of employees per wage and salary earner	% change	16.0	19.7	21.3	22
Price index of private consumption ³	% change	8.7	17.6	17.5	19
Current account balance ³	Lit. '000 million	— 744	— 368	— 2 380	— 750

¹ Excluding building and 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: ISTAT and *Relazione generale sulla situazione economica del Paese*, 1976

⁶ Estimates of Commission's Departments.

price increases. However, following the marked increase in late 1976, demand for new cars (seasonally adjusted) declined appreciably under the impact of several petrol price increases.

The growth of fixed *investment* was more rapid, particularly as regards plant and machinery. Contributory factors no doubt included last year's favourable profit position, the upturn in demand experienced for a year and a half, the increase — until recently — in the degree of capacity utilization, and the need to modernize the productive apparatus. Investment in stocks also showed a clear tendency to rise, at least where finished products are concerned.

On the supply side, *industrial production* in the first quarter went on growing, but at a considerably slower rate. According to the ISTAT indices — seasonally adjusted by ISCO — it was distinctly down on the high level reached last December, but over 2% up on the final quarter of 1976 and some 5% higher than before the start of the recession in mid-1974. In April, the trend of industrial production was distinctly downward. The growth rate for capital goods was higher than average. The unadjusted index of industrial production was 8.3% up on the level recorded in the first four months of 1976. According to ISCO's provisional calculations, real *gross domestic product* in the first quarter of 1977, on a seasonally adjusted basis, was 3% up on the average for 1976.

While the degree of utilization of industrial production *capacity* fell slightly for the first time in over a year (to 75.1%, the underlying trend in the *level of employment*¹ between the final quarter of 1976 and the first quarter of 1977 was probably again upward, owing to a further increase in the average hours worked per person employed. In the first quarter, in industrial firms with 500 or more employees employment was 8% up on a year earlier (fourth quarter 1976: up 6%); in April, however, it fell below the corresponding level of the previous year. In the first four months, the number of unemployed — which was stationary or declining at the end of last year — was again tending to rise (by 3% compared with the previous four-month period).² According to the latest sample survey of the labour market, the results of which were published by ISTAT at the end of May and which are not comparable with the earlier quarterly surveys, the number of unemployed in January totalled 1 459 000 or 6.8% of the labour force. 56% were women and 72% were persons between 14 and 29 years of age; over 42% were resident in Southern Italy and the islands.

According to the customs returns seasonally adjusted by ISCO, the value and volume of imports in the first four months of the year fell considerably, after soaring in the

¹ Number of persons employed multiplied by the average number of hours worked per employee.

² Ministry of Labour figures seasonally adjusted by EUROSTAT.

TABLE 2
Demand for and supply of goods and services

Italy	1974 ²	1975 ²			1976 ²			1977 ³		
	At curr. prices Lit. '000 million	% change on preceding year								
		Vol	Price	Value	Vol	Price	Value	Vol	Price	Value
Private consumption	66 437	- 1.4	17.6	16.0	3.2	17.5	21.3	2½	19	22
Public consumption	13 781	2.8	11.8	14.9	1.9	20.5	22.8	2	19½	22
Gross fixed asset formation	22 831	-13.0	19.5	4.0	2.3	18.6	21.3	2	17	19½
— Building and construction	12 745	- 8.3	19.8	9.9	- 1.2	19.9	18.5	0	17½	17½
— Plant and machinery	10 086	-18.9	19.2	- 3.3	7.2	17.0	25.3	5	16	22
Domestic final uses (excluding change in stocks)	103 049	- 3.2	16.9	13.2	2.9	18.1	21.5	2½	18½	21½
Domestic final uses (including change in stocks)	107 092	- 6.2	15.2	8.1	5.5	19.7	26.3	2	18½	20½
Exports ¹	22 871	3.5	11.1	15.0	12.6	18.9	33.9	9	16	26½
Imports ¹	29 052	- 9.9	6.3	- 4.2	13.1	24.7	41.0	4½	15	20
Gross domestic product at market prices	100 911	- 3.5	17.3	13.2	5.6	17.8	24.4	3	19	22½
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	103 049	- 3.1		13.5	2.8		22.0	2½		21½
Change in stocks	4 043	- 3.1		- 4.9	2.5		4.6	- ½		0
Balance of exports and imports ¹	- 6 181	2.7		4.6	0.3		-2.2	1		1

¹ Goods and services.

² Source: Relazione generale sulla situazione economica del Paese; 1976.

³ Estimates of Commission's Departments.

closing months of last year. Even if — as in the case of exports — the causes for this movement may be partly statistical and technical, it might already be heralding recessionary tendencies in the economy (see section 3 below). However, expressed in lire, *merchandise imports* were no less than 29% up on the figure for the first four months of 1976.

After slowing down distinctly last summer, *prices* have since started to rise again at a noticeably faster rate. There have been three main factors: the unexpectedly vigorous expansion of demand, the sharp rise in average wage costs per unit of output and the increases in indirect taxes, public service charges and administered prices which have taken place since the autumn. Wholesale prices rose by a monthly average of 1.2% in the period from January to April, i.e. at an annual rate of almost 15½%; in April they were 19.4% higher than a year earlier. The corresponding rates for consumer prices in the period from January to May were 1.4% and 18.2% respectively; the rise in May 1976 was 18.5%.

While the movement of merchandise imports and exports described above led in the first four months of the year to a tendency for the trade balance to improve (though remaining in heavy deficit) and while foreign exchange receipts from service transactions with abroad pointed upwards, the position on capital account deteriorated sharply. This was mainly because of a change in the pattern of leads and lags, which in turn was probably due to the phasing out of the non-interest bearing cash deposit and the special tax on purchases of foreign currency. In the event, the *overall balance of payments* closed with a heavy deficit (Lit 1 918 000 million) in the first four months of the year, after showing a surplus of Lit 746 000 million in the preceding quarter.¹ Nevertheless the (net) official gold and foreign exchange reserves again increased considerably (by Lit 878 000 million to Lit 11 759 000 million). This was firstly because the commercial banks were still importing money, thereby increasing their short-term external indebtedness (by Lit 1 898 000 million to no less than Lit 4 533 000 million). Secondly, in accordance with the rules laid down last December² the monetary authorities' gold reserves were once more revalued.³ The foreign exchange reserves proper, after rising in the final quarter of last year by Lit 1 397 000 million to Lit 2 276 000 million, fell slightly in the first four months of the year. In May, however, they rose by Lit 1 029 000 million; following the Community loan granted to Italy under the Council Decision of 17 May 1977, foreign exchange reserves also rose in June (by about Lit 950 000 million according to provisional information). Mainly as a result of the money imports by the commercial banks, the renewed depreciation of the *lira exchange* rate was kept within very narrow limits: on the official foreign exchange market a US dollar was worth Lit 872.20 at the beginning of January and Lit. 884.8 on 28 June, and the weighted exchange rate of the lira against all other currencies fell only slightly.

Cash disbursement under the *central government budget* rose very fast in the first four months. But since cash receipts increased even faster, the cash deficit was slightly lower than a year earlier. As a result of additional demands on the Cassa Depositi e Prestiti in connection with the financing of the central, regional and local authorities, other Treasury transactions produced a

rather high deficit whereas they had shown a considerable surplus in the first four months of 1976. Overall, the *Treasury's net borrowing requirement* amounted to Lit. 4 899 000 million in the period under review, compared with Lit. 3 063 000 million in the previous year.

The *monetary base*⁴ again expanded vigorously in the first four months of the year, mainly because of the rapid phasing out of the non-interest bearing cash deposit on purchases of foreign currency. This led to another sharp increase in *bank liquidity*, especially since there was still a ceiling on the expansion of bank lending. The banks therefore invested large amounts in short-term Treasury certificates. Partly as a result of the brisk economic growth, total *domestic lending* expanded far beyond the limit agreed when Italy was granted the new Community loan. Short-term *interest rates* showed a slight downward movement, while long-term interest rates tended if anything to edge up a little; the gap between them thus narrowed. Interest rates on interbank deposits fell from 16.76% last December to 15.16% in May; on the other hand, the yield on bonds issued by the institutions lending against goods and securities rose slightly over the same period, from 14.18% to 14.75%. In June, the discount rate and the rate for advances against securities were lowered from 15 to 13%;² however, for balance of payments reasons, the overall level of interest rates was kept above that prevailing abroad. The market in *long-term securities* was still decidedly unresponsive.

3. Outlook

Economic developments until the end of the year are likely to be determined by two main factors. First, the lively expansion in world trade is expected to continue. Secondly, it is probable that the restrictive short-term economic policy will damp down domestic demand until some time in early autumn. Overall demand is unlikely to recover again before late 1977.

Export demand, and in particular exports to non-member countries, will no doubt rise vigorously throughout the rest of the year. On the domestic demand side, real private consumption will be flat for a time or at best grow marginally, because of the steep rise in prices and the rapid increase in the tax burden. As regards fixed investment, inhibiting factors might outweigh the expansionary forces (described in section 2) in the second and third quarters, especially as a result of the restriction on lending. Stockbuilding, which last year increased unusually rapidly, will probably decline in volume.

In these circumstances it seems reasonable at present to expect real gross domestic product to grow by nearly 3% between 1976 and 1977; this rate implies that production will increase very little during 1977. Even though employment will again rise, the number of unemployed will probably climb further, since the increase in the

¹ According to provisional figures, the balance of payments deficit in May was Lit 140 000 million.

² See the list of measures at the end of this chapter.

³ by Lit 859 000 million; at the end of 1976 they had been revalued by Lit 6 351 000 million. Including a gold transfer from the IMF (Lit 21 000 million), the value of the gold reserves increased by Lit 880 000 million to Lit 9 035 000 million.

⁴ Recently the lira has actually increased slightly in value against the dollar.

TABLE 3
The Central Government Budget

Italy	1976			1977	
	Revised budget		Provisional outturn	Revised budget	
	Lit. '000 million	% change ⁴	Lit. '000 million	Lit. '000 million	% change ⁴
Expenditure ¹	47.7	47.2	47.3	48.8	2.3
of which:					
— current expenditure	37.0	40.7	36.8	38.5	4.1
— capital expenditure ²	10.7	75.4	10.5	10.3	— 3.7
Revenue ³	35.5	46.1	35.3	42.1	18.6
of which:					
— direct taxes	12.1	20.0	11.7	16.0	32.2
— indirect taxes	15.5	4.0	15.7	22.0	41.9
Net borrowing requirement ^{1 3}	— 12.1		12.0	— 6.7	

¹ Disregarding debt extinction

² Including participations, advances and loans.

³ Excluding loan proceeds.

⁴ On the preceding year's revised budget.

Notes:

a) The figures in this table are based on the national budgets and are recalculated on the basis of Community definitions.

b) Both in 1976 and 1977 the original budgets were later substantially altered. The figures given this time are therefore those for the revised budgets.

labour force is likely to exceed the increase in employment. Imports will probably expand much more slowly than exports, in terms of volume and value.

The upward movement of prices is likely to slacken perceptibly between now and the end of the year, but will still be quite steep. The balance of payments on current account will improve considerably, but the deficit for the year will still be heavy — over Lit 700 000 million, equivalent to 0.4% of gross domestic product.

1977 should thus see appreciable progress towards restoring more satisfactory domestic and external equilibrium; however, this progress might prove insufficient to achieve a current account surplus of at least Lit 500 000 million in the twelve-month period to the end of March and a surplus of approximately Lit 1 000 000 million in the 1978 calendar year as agreed with the IMF. The latter, is the main economic policy target — in addition to a lower rate of price increases — laid down for the Italian Government, in the context of the new Community loan at the Council meeting of 17 May. On the basis of the "instrumental" targets set by the Council at the same time, greater efforts will therefore need to be made to limit credit expansion, central government expenditure and public-sector deficits. One main problem is to destroy the increasingly clear association between economic upswing and balance of payments difficulties and so reestablish the basis for a faster and sustained growth of production and employment. To this end, short-term economic policy action must be supplemented by appropriate structural measures, particularly in agriculture, the energy sector, public administration, the distributive sector and also in the area of labour mobility and that of production, which must be adapted more closely to the changed structure of demand.

Major economic policy measures

December 1976:

— On 10 December the Government presented a draft law featuring a ten-year plan for residential construction, under which 120 000 new dwellings are to be built over the next three years. Total expenditure will be Lit. 2 600 000 million, of which Lit. 1 500 000 will be borne by the central government. For 1977, an extra Lit. 330 000 million will be made available from the central government budget.

— The Banca d'Italia repaid to the Bank of England the \$ 487 million loan which was granted by the United Kingdom at the end of 1974 under the Community's system of short-term monetary support and which had since been renewed several times.

— On 23 December the Government decided to phase out the 7% special tax on purchases of foreign currency introduced two months earlier. The rate of tax was to be reduced from 7 to 3.5% on 27 December, to 3% on 3 January 1977, to 2.5% on 10 January, to 2% on 27 January, to 1.5% on 24 January, to 1% on 31 January and to 0.5% on 7 February. It was to be abolished altogether on 18 February.

— The monetary authorities' gold reserves were revalued: previously these reserves had been valued at \$ 35 per fine ounce of gold and at Lit. 625 per dollar. In future, valuation will be based on 85% of the average dollar price of gold prevailing on the London gold market during the last 30 working days of each quarter, and on the lira/dollar market rate on the last working day of each quarter.

— The rent freeze was extended by three months from 31 December. (It was subsequently extended again until the end of June 1977 and again until the end of October 1977).

January 1977:

— The Ministerial Committee on Prices put up rail charges by 20% with effect from 1 March; they had already been raised by 10% on 1 December last year. Extra revenue from the latest increase is expected to total some Lit. 150 000 million or 15% of the railways' estimated deficit for the current year.

— The Government decided that short-term bank loans obtained by local authorities and provinces before 1 January 1977 (some Lit 5 000 000 million) should be converted into long-term debt to the Cassa Depositi e Prestiti, a department of the Treasury. This measure will mean a considerable saving in interest payments for the local authorities and

TABLE 4
Main economic indicators

	Year	Jan	Feb.	Mar	Apr.	May	June	July	Aug	Sept	Oct.	Nov.	Dec.
Industrial production (1970 = 100)	1975	109.3	112.9	108.8	107.7	102.5	106.3	108.0	100.2	107.3	108.2	110.8	108.1
	1976	109.5	115.9	117.7	116.9	122.8	119.9	121.2	114.3	125.2	123.6	129.0	132.0
	1977	130.8	130.8	128.5	124.3	.	.	.	.	.	.	.	.
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	1 151.4	1 156.2	1 172.2	1 171.2	1 182.7	1 184.2	1 201.6	1 200.1	1 216.0	1 179.6	1 203.5	1 215.4
	1977	1 226.6	1 234.3	1 243.8	1 273.1	1 282.9	.	.	.	.	.	.	.
Construction: Housing starts (000)	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	16 128	14 584	16 263	17 312
	1977	13 056	14 385	16 411	.	.	.	.	.	.	.	.	.
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	.	.	.	.	.	.	.	.
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	.	.	.	.	.	.	.
Visible imports (million EUA)	1975	2 527	2 271	2 539	2 328	2 239	2 584	2 441	2 269	2 811	2 724	2 807	3 126
	1976	2 682	2 671	3 182	3 095	3 305	3 140	3 011	3 146	3 256	3 371	3 843	3 579
	1977	3 352	3 484	3 789	3 681	.	.	.	.	.	.	.	.
Visible exports (million EUA)	1975	2 163	2 225	2 336	2 235	2 093	2 361	2 312	2 349	2 432	2 458	2 510	2 609
	1976	2 417	2 255	2 670	2 491	2 822	2 650	2 815	2 686	2 843	2 957	3 109	3 002
	1977	2 921	3 000	3 354	3 281	.	.	.	.	.	.	.	.
Balance of trade (million EUA)	1975	- 364	- 46	- 202	- 93	- 146	- 222	- 129	80	- 379	- 266	- 296	- 517
	1976	- 266	- 416	- 512	- 604	- 483	- 490	- 196	- 460	- 413	- 414	- 734	- 576
	1977	- 431	- 484	- 435	- 401	.	.	.	.	.	.	.	.
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	2 697	2 695	.	.	.	.	.	.	.	.	.
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	45 679	45 045	46 930	47 188	49 933
	1977	49 871	50 572	51 523	52 061	.	.	.	.	.	.	.	.

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.

provinces. It was also decided that local government should recruit no new officials in 1977 and contract no further short-term debt in 1977.

— To improve the balance of payments the Government proposed support measures for agriculture. In the next ten years a total of Lit. 5 650 000 million (of which Lit. 500 000 million in 1977) is to be made available mainly for cattle breeding, agricultural cooperatives and infrastructure schemes. Encouragement is also to be given to the sale of frozen meat in order to curb the consumption of expensive fresh meat.

— On 20 January the obligation on commercial banks to invest part of their assets in fixed interest securities was extended to the end of June 1977. However, for seasonal reasons, additional purchases of these securities

must only be equivalent to 30% of the increase in deposits (42% in the second half of 1976).

— On 26 January, employers and unions in industry signed an agreement designed to curb labour costs and increase productivity. Its main provisions are the following:

— From 31 January, the sliding wage scale will be disregarded in calculating redundancy pay and production bonuses.

— In 1977 seven holidays will be declared normal working days, and five of them will be paid as such. The other two days will be paid at the Sunday rate.

— To improve capacity utilization, employers and unions will arrange for annual leave to be staggered, will encourage shift-work, will increase overtime if necessary and will promote workers' mobility within firms.

— Tighter controls on absenteeism.

— On 31 January the Government provided, by Decree Law, that cost-of-living supplements based on the sliding wage scale would no longer be taken into account in calculating redundancy pay and that from 1 February the existing "privileged" sliding wage schemes were to be adapted to those in industry.

February:

— A Decree Law of 7 February shifted part (Lit. 1 420 000 million) of the burden of social security contributions from employers in industry (excluding construction) and small business to the central government (fiscalization). The extra expenditure will be financed by raising value added tax and certain other indirect taxes. The price rises induced by the tax increases will not be taken into account in calculating the cost-of-living supplements under the sliding wage scale arrangements. The latter provision was withdrawn during the parliamentary debate of 7 April, as was the provision according to which firms which granted wage increases higher than those agreed nationally would suffer tax disadvantages and would lose the advantages of "fiscalization". At the end of March, however, the Government instead managed to get a provision accepted under which increases in certain electricity charges, urban transport charges and the retail prices of daily newspapers would in future no longer affect the index on which the sliding wage scale was based.

March:

— On 29 March the ceiling on bank lending introduced on 15 October 1976 for the period to the end of March 1977 was extended to the end of March 1978. Lending by individual credit institutions to all domestic customers whose borrowings exceed Lit. 30 million may not grow, in comparison to the average level in the period from March to September 1976, by more than:

12% up to the end of May 1977

14% up to the end of July 1977

13% up to the end of September 1977

16% up to the end of November 1977

23% up to the end of January 1978

25% up to the end of March 1978.

April:

— On 6 April, after several months of negotiations, the Minister for the Treasury in a Letter of Intent officially applied to the IMF for a standby credit of SDR 450 million, with drawings to be completed by the end of 1978; the Letter contained a commitment to achieve a current account surplus of Lit. 500 000 million in the twelve-month period to 31 March 1978 and of Lit. 1 000 000 million in 1978 as a whole and to reduce the annual increase in the cost of living by March 1978 to 13% and by the end of 1978 to 8%. The following instrumental targets were set:

- The combined Treasury and local government deficit is to be limited to Lit. 13 100 000 million in 1977 and the total public sector deficit (Treasury, local government, social security institutions and ENEL) to Lit. 16 450 000 million in 1977 and to Lit. 14 450 000 million in 1978. In 1977 central government expenditure must not exceed Lit. 55 350 000 million on a cash basis; in 1978 it must not grow by more than 7% on the basis of commitment authorizations (budget on an appropriations basis).
- The growth in total domestic lending must not exceed Lit. 30 000 000 million in the twelve-month period to 31 March 1978, with the same limit applying for 1978 as a whole.
- Up to 15 April 1978 maximum quarterly levels were fixed for the special cost-of-living index on which the sliding wage scale is based.

The Government also undertook, for the duration of the agreement, to take no measures amounting to a system of split exchange rates, to impose no new restrictions on payments related to current transactions with abroad, and to introduce no new import restrictions in order to improve the balance of payments.

— On 7 April the Government decided to dissolve, by Decree, subsequently transformed into a Law on 6 June, the State holding company EGAM (Ente Autonomo di Gestione per le Aziende minerarie Metallurgiche) because of finance and management difficulties. The 50 or so enterprises of this holding company are to be transferred to the State-controlled undertaking ENI and IRI. The latter must, within the five months following the Decree, prepare programmes to restructure the profitable enterprises and to dissolve the unprofitable ones. Dissolving the

unprofitable enterprises must be initiated before 31 October 1977. Implementing the Law is to cost the Government some Lit. 850 000 million between 1977 and 1982, with some Lit. 200 000 million of this amount being incurred in 1977.

— Towards the end of the month newspaper prices were raised by one-third to Lit. 200 per copy. Pursuant to the agreement reached at the end of March between the unions and the Government, this increase will have no effect on the special sliding wage scale index.

May 1977:

— On 4 May the Government introduced, by Decree, a new method for calculating the prices of medicines and drugs. From 1 June, this will mean a reduction of some 20% in prices for a large number of medicines and drugs, especially sulfonamide and antibiotics. The resulting drop in earnings by pharmaceutical manufacturers will be compensated for by abolishing the discounts granted by manufacturers to the health insurance funds. This could mean an increase in health insurance funds' deficits, since the ending of discounts will apply to all medicines and drugs.

— On 17 May the Council of the European Communities took the final decision to grant Italy a Community loan of \$ 500 million. It also fixed the economic policy conditions to be observed by Italy. These conditions (ceilings), which also apply in respect of the medium-term financial assistance and the loan previously granted to Italy, are intended to help in attaining balance of payments and costs of living targets similar to those set by the IMF (see measures of 6 April). They may be summarized as follows:

- Total central government expenditure: ceiling of Lit. 55 350 000 million, on a cash basis, in 1977; maximum increase of 7%, on the basis of commitment authorizations, in 1978.
- Total public sector deficit (Treasury, local government, social security institutions and ENEL): maximum of Lit. 16 450 000 million in 1977 (Lit. 14 450 000 million in 1978), of which Lit. 13 100 000 for Treasury and local government together and Lit. 9 800 000 million for the Treasury alone.
- Financing of Treasury deficit by the monetary authorities: maximum of Lit. 4 000 000 million in 1977.
- Growth in total domestic lending: not to exceed Lit. 30 600 000 million in 1977.
- Public service charges and certain administered prices will have to be adjusted, with no effect on the sliding wage scale, to ensure compliance with the ceiling for the total public sector deficit mentioned at (b).

— On 27 May, the Government published a Law intended to improve coordination and strengthen policy in the field of export promotion, export credit financing and international cooperation. In future, policy in this area will come under the authority of a special Ministerial Committee (CIPES); a special department of the "Istituto Nazionale Assicurazioni" will deal with the insurance of risks connected with export credit. The extent of risks insured was extended; the ceiling for liabilities arising from the covering of risks (maximum period: 24 months) was raised to Lit. 5 000 000 million. These measures bring regulations in Italy more into line with those obtaining in its major trading partners.

June 1977:

— On 1 June, Parliament passed the draft law introduced at the end of October 1976, providing for measures to promote the employment of young people. The total amount which the central government is authorized to spend in 1977 and the following three years, was raised to Lit. 1 060 000 million (as against Lit. 400 000 million in the Government draft). The Law will enable some 600 000 young people to find permanent or temporary employment in industry or under the public authorities (for work of benefit to the community).

— On 8 June, the arrangements which have been in force since the beginning of October last year, requiring exporters granting short-term credit to foreign customers to procure immediately foreign currency to cover part (50%) of the credit, were eased (to 25%). This measure, which takes account of the favourable seasonal trend of the current balance of payments, is intended to bring about a gradual reduction in the very considerable short-term foreign indebtedness of banks.

— On 10 June, excise duties were raised on some petroleum products (except petrol). The estimated increase in revenue is about Lit. 90 000 million annually.

— On 11 June, the Minister for the Treasury announced that the discount rate and the rate for advances against securities were to be lowered from 15 to 13% with effect from 13 June. The maximum supplement which can be added in the event of certain limits being exceeded remains unchanged at

3%. The Minister stated that the lowering of rates was justified by the slight easing of inflation and by the favorable balance of payments trend which had been evident over the last two months.

— On the same date, the issue was announced of a new kind of government debt instrument, the Treasury credit certificate. Its attractive terms of issue should mean that it will be well received by the public, since it carries a two-year maturity, half-yearly interest coupons, and a variable interest rate (minimum interest rate or, if higher, yield of ordinary

Treasury certificates (BOT) during three months preceding the reference half year). The new debt instrument will probably gradually replace a proportion of the ordinary (three to twelve-month) BOT Treasury certificates. This would gradually reduce the very considerable liquidity potential which the BOT Treasury certificates held by banks represent.

— On 17 June, a Decree was passed raising the rate of VAT on milk not intended for direct consumption, and thus on almost all milk imports, from 6 to 14%.

F – Netherlands

The economic stagnation of early 1977 should be followed by some revival in the course of the year, although hardly at a fast enough rate to entail a reduction of unemployment. The slowdown of price inflation may in the coming months be only marginal. However, for the year 1977 as a whole the rate of inflation will be substantially lower than the year before. The external surplus on current account may remain high.

Prospects for 1977 generally suggest little progress towards realizing the medium-term objectives for employment. Indeed, economic policy can hardly in the longer run succeed in sustaining activity unless helped by a slowdown of the underlying increase in unit wage costs.

1. Overall assessment and main policy issues

The easing of cost and price inflation observed in 1976 has continued so far in 1977 helped by the appreciation of the guilder and the ensuing slowdown of the rise in import prices. Although some appreciation of the Dutch currency was expected, the effective rise of 7.6% (weighted by Dutch imports) as measured between April 1976 and April 1977 was larger than foreseen. This had led to a reappraisal of the 1977 outlook on certain points, and notably to a downward revision of earlier forecasts for the current external surplus as elaborated by the services of the Commission.

The strong position of the guilder in foreign exchange markets as from August 1976 was accompanied by a reversal of registered capital movements. Following the large deficits on non-monetary transactions in the second and third quarters of 1976, monetary conditions were indeed in the first months of 1977 influenced by a net inflow of funds from abroad (after elimination of seasonal fluctuations).

In order to prevent the emerging current account surplus from leading to an unwarranted appreciation of the guilder (and hence to too strong deterioration of the competitiveness for the Dutch industry) the Dutch

TABLE 1
Key indicators

Netherlands	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976	1977 ⁶
Gross domestic product, volume	% change	+ 4.7	- 1.1	+ 3.7	+ 4.2
of which: industry ¹	% change	+ 6.2	- 4.3	+ 6.3	+ 4.2
Gross domestic product in volume per person in employment	% change	+ 4.5	- 0.2	+ 4.2	+ 3.9
Total employment (man/year) ²	% change	+ 0.2	- 0.9	- 0.5	+ 0.3
— Independent entrepreneurs	% change	- 1.6	- 2.1	- 1.9	- 1.7
— Wage and salary earners in company sector	% change	+ 0.2	- 1.1	- 0.6	+ 0.5
— General Government	% change	+ 2.4	+ 1.6	+ 2.1	+ 1.6
Unemployment	as % of labour force	2.1	4.3	4.6	4.4
Compensation of employees per wage and salary earner	% change	+ 13.9	+ 13.5	+ 10.6	+ 8.0
Price index of private consumption ³	% change	+ 8.0	+ 10.5	+ 9.1	+ 7.1
Current account balance ³	in fl '000 million	+ 2.7	+ 4.4	+ 6.6	+ 7.0

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: Nationale Rekeningen 1975, CBS

⁶ Estimates of Commission's Departments

authorities have in recent years taken steps to facilitate capital exports, notably by providing better access to the Dutch capital market for foreign borrowers and to increase commercial banks' external lending operations. Apart from temporary disturbances (eg. in mid-1976) this policy has been accompanied by a lowering of long-term interest rates as well as of money market rates. However, despite these efforts, domestic liquidity has been expanding fast, from around 34% of national income in 1972 to around 40% in 1976. Although this high rate of liquidity is unlikely to have added to inflationary tendencies in the short run despite the existence of statutory liquidity reserves, it certainly increases the difficulties of controlling subsequent developments of incomes and demand. The authorities have therefore decided to aim at a lowering of the domestic liquidity ratio by around 1 percentage point per year over the next few years. In this context, the Central Bank, in May, after agreement with the commercial banks, decided to constrain domestic credit expansion through 1977 to 12½% of the level reached at the end of 1976. The main objective of this measure is, then, not to restrict the growth of demand but to stimulate capital exports and investment in long-term financial assets by the banks as well by the general public, thereby obtaining a relative decline of short-term financial assets.

In line with the medium-term policy to reduce the increase of the tax pressure, the stimulation of demand imparted

through general budgetary measures has not been stepped up in 1977. Also, partly due to the resignation of the government, an important stimulatory measure of a selective nature, the subsidy to business investment, has not been implemented within the delay foreseen. Consequently the existing fiscal allowances were kept in effect. The financial situation of the enterprise sector will, on the other hand, benefit from a recent decision to lower — as from 1 July — the social security premiums (corresponding to 0.35% of national income on an annual basis) and to utilize 625 million guilders — originally earmarked for transfers to social security in the central government budget — for supplementary support for construction activity and assistance to weak enterprises in all branches. These expenditure decisions are linked to an upward revision of revenue estimates for social security both for 1976 and for 1977 and do not entail a parallel expansion of the borrowing requirement. Indeed, according to most recent estimates, borrowing requirements of the public administration as a whole, is for both these years substantially lower than envisaged when the central government budget for 1977 was prepared.

2. Recent developments

The early months of 1977 appear to have been marked by sluggish growth in foreign demand coupled with a fairly brisk rise in the principal domestic demand components.

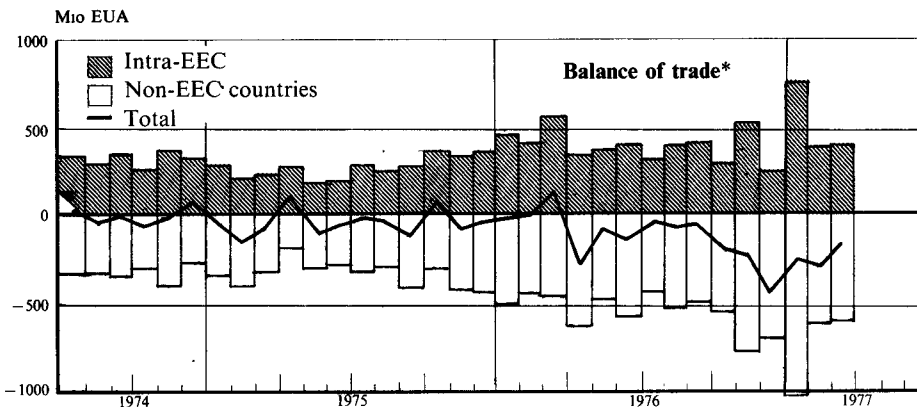
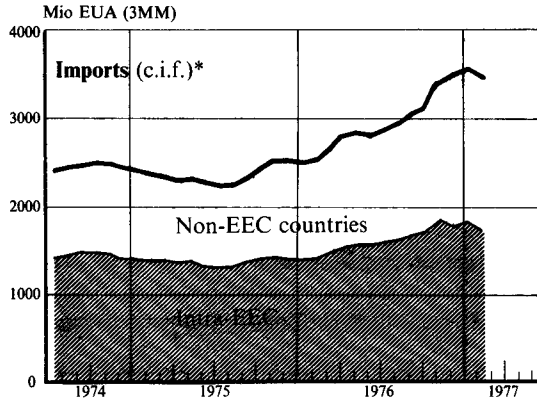
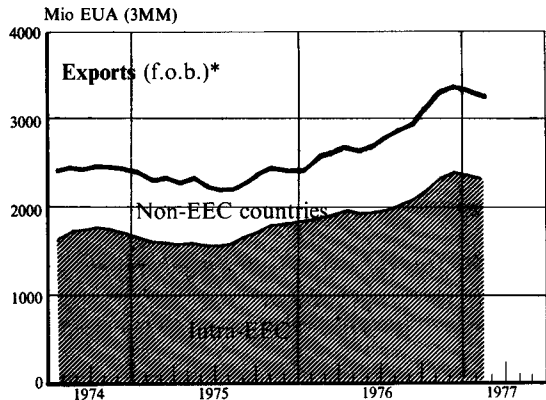
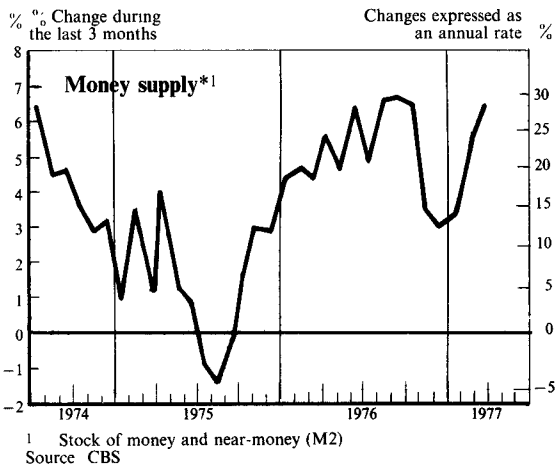
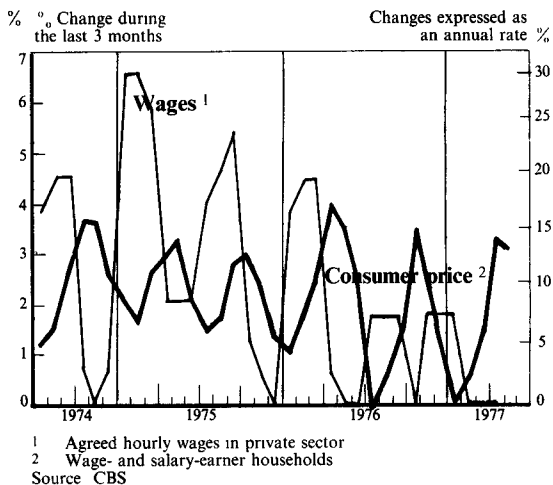
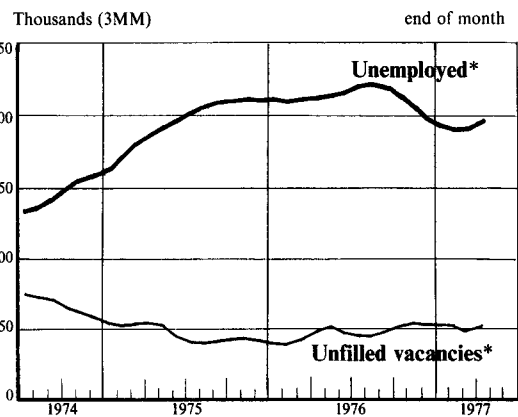
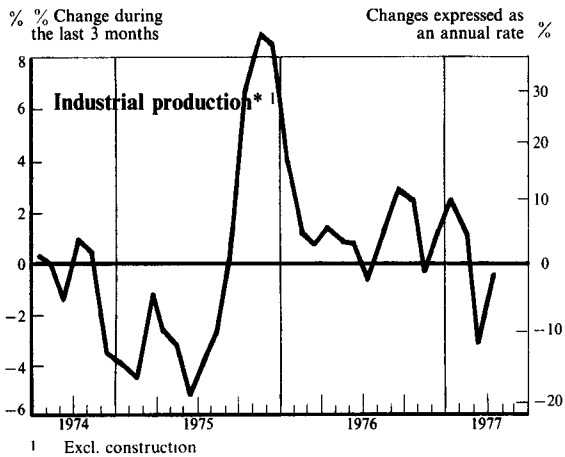
TABLE 2
Demand for and supply of goods and services

Netherlands	1974 ²	1975 ²			1976 ³			1977 ³		
	At current prices in Fl '000 million	% change on preceding year								
		Vol.	Price	Value	Vol.	Price	Value	Vol.	Price	Value
Private consumption	104.93	+ 3.0	+10.5	+13.9	+ 3.1	+ 9.1	+12.5	+ 3.2	+ 7.1	+10.6
Public consumption	32.18	+ 2.5	+12.3	+15.1	+ 4.1	+ 9.2	+13.7	+ 1.2	+ 7.3	+ 8.6
Gross fixed asset formation	41.14	- 3.9	+10.4	+ 6.1	- 1.7	+ 8.2	+ 6.3	+ 5.7	+ 6.9	+13.1
— Enterprises	23.86	- 6.8	+ 9.4	+ 2.0	- 4.9	+ 7.6	+ 2.3	+ 6.5	+ 5.8	+12.7
— Dwellings	10.45	- 4.8	+11.1	+ 5.8	+ 1.9	+ 9.0	+11.1	+11.0	+ 8.4	+20.3
— General Government	6.83	+ 4.1	+ 9.3	+13.8	+ 3.7	+ 9.0	+12.9	- 3.5	+ 8.2	+ 4.4
Domestic final uses (excluding change in stocks)	178.25	+ 1.4	+10.8	+12.3	+ 2.3	+ 8.9	+11.4	+ 3.4	+ 7.1	+10.7
Domestic final uses (including change in stocks)	181.75	- 1.4	+10.8	+ 9.3	+ 3.9	+ 8.9	+13.1	+ 4.0	+ 7.1	+11.4
Exports ¹	107.57	- 2.9	+ 4.6	+ 1.6	+10.5	+ 6.7	+17.9	+ 5.2	+ 3.6	+ 9.0
Imports ¹	102.21	- 3.9	+ 4.4	+ 0.3	+11.7	+ 6.2	+18.6	+ 5.3	+ 3.8	+ 9.4
Gross domestic product at market prices	187.11	- 0.9	+10.7	+ 9.8	+ 3.5	+ 9.1	+12.9	+ 4.0	+ 6.8	+11.1
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	178.25	+ 1.3	.	+11.7	+ 2.2	.	+11.1	+ 3.2	.	+10.3
Change in stocks	+ 3.50	- 2.6	.	- 2.7	+ 1.6	.	+ 1.6	+ 0.7	.	+ 0.7
Balance of exports and imports ¹	+ 5.36	+ 0.4	.	+ 0.2	- 0.3	.	+ 0.2	+ 0.1	.	+ 0.1

¹ Goods and services

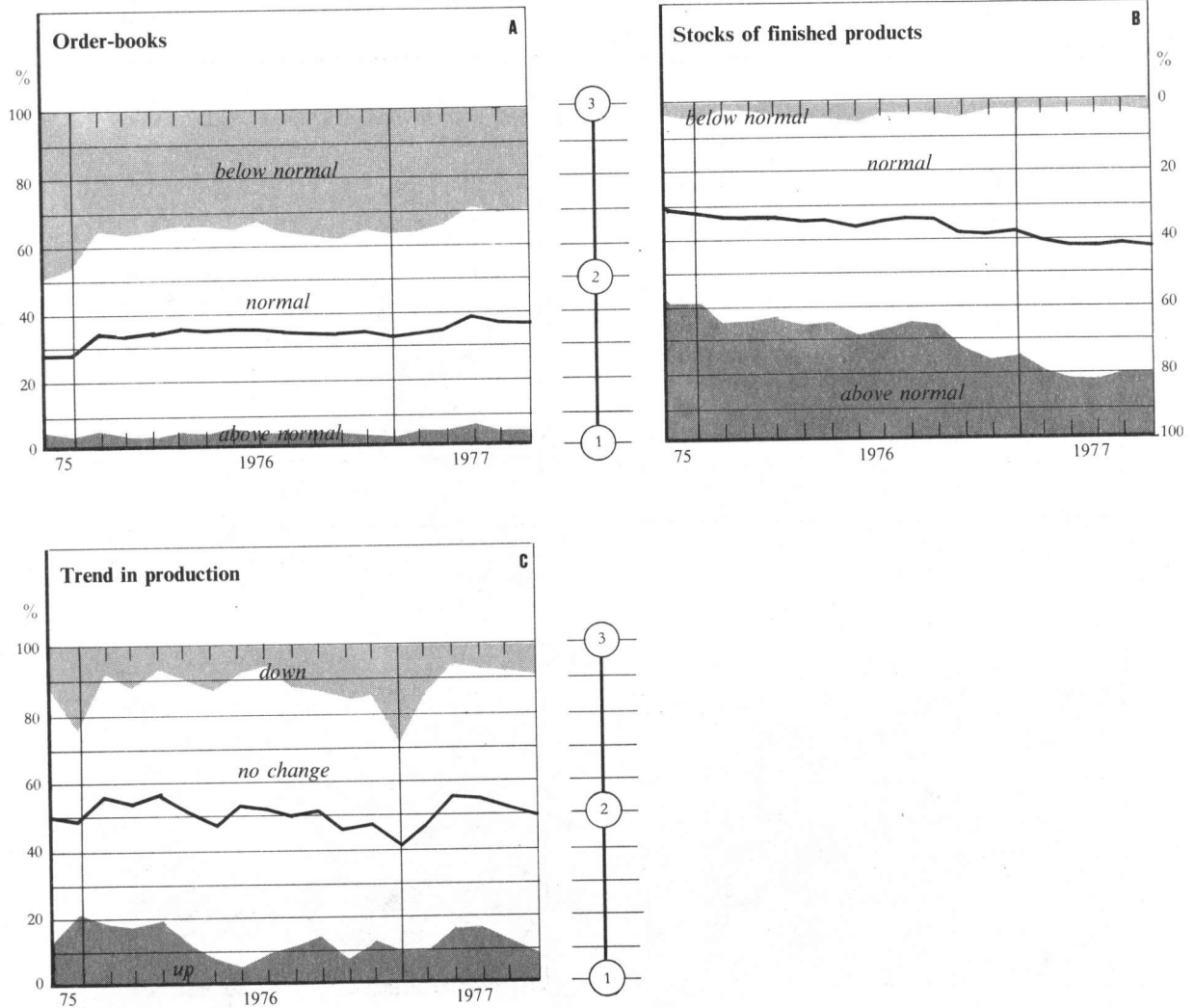
² Source: Nationale Rekeningen 1975, CBS.

³ Estimates of Commission's Departments



*: Seasonally adjusted figures.
3MM: Three month moving average.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

GRAPHS A, B and C: The three zones (grey, white and black) show the percentages of the three different answers.

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

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

Merchandise exports in volume terms in the first quarter dropped 5.3% below the fourth quarter level reflecting not only cyclical weakening of foreign demand and a "technical" decline in oil deliveries following high anticipatory exports in the fourth quarter, but also an appreciable decrease of exports of the shipbuilding industry. Together with a levelling off of industrial production, the slowdown of oil flows contributed to the decline by 5.6% in the volume of merchandise imports. The terms of trade having worsened by some 1%, the trade balance showed a further deterioration and the current external account dropped by some 2 000 million to some 260 million guilders.

Following a decline of 2.0% in the preceding quarter, *private consumption* in real terms rose by 3.5% in the first quarter of 1977. Growth of real disposable income showed a marked acceleration as the index of consumer prices remained relatively stable, whereas wage rates were raised by an estimated 2½%, the legal minimum wage by 4.6% and social security benefits by some 5½% as from January 1st.

The upward movement of *gross fixed asset formation* was probably maintained at about the same overall rate. The expansion of investment in dwellings — which started in late 1976 — is likely to have continued in the first quarter of 1977. Public investment, however, may have declined somewhat whereas some strengthening of fixed capital formation should have taken place in the business sector.

As a result, mainly, of the weak development of exports but also due to work stoppages related to sectoral wage negotiations, *industrial production* (excluding construction, adjusted for seasonal variations) fell by 0.8% between the fourth quarter 1976 and the first quarter of 1977. However, an upturn of 2.4% took place in April. In construction and notably in housebuilding production increased further and production of services rose quite strongly in the first quarter.

With only modest growth in economic activity since October 1976 the reduction of *unemployment* which had been observed for a time last year was brought to a halt. Indeed the number of unemployed, seasonally adjusted, rose from 191 100 at the end of February to 201 500 at the end of May, the latter figure corresponding to 4.2% of the labour force. The number of unfilled vacancies (seasonally adjusted), which had been stable over the 6 months up to March 1977, after a fall of some 9% in April rose again in May to a level of 8.4% above the year ago figure.

Month-to-month changes in *consumer prices*, following a series of very low figures in late 1976 and a decline in January this year, have accelerated in recent months and this in spite of a downward movement in the prices of potatoes, vegetables and fruit. The acceleration was, however, largely of a seasonal nature. On a twelve-month basis the slowdown continued: in May the general price index for wage and salary earners stood 7.0% above the level of April 1976. The special wage regulation index, which shows the price changes excluding the effect of the 2 points rise in the rate of VAT in October 1976, showed an increase of only 6.1% over the same period.

3. Outlook

Following stagnation in the first quarter, growth of economic activity is likely to have resumed, although at a modest rate only.

Merchandise exports should be more buoyant in the months ahead, as foreign demand improves somewhat and as agricultural exports will be boosted by the impact of a normal harvest. However, given a stabilization of natural gas exports, sharply reduced exports of ships and a slow growth of exports of other manufactured products, brought about by the deterioration in the competitive position of export industries, the volume increase for the

TABLE 3
The Central Government Budget

Netherlands	1976			1977	
	Original budget		Provisional outturn	Original budget	
	in Fl '000 million	% change ²	in Fl '000 million	in Fl '000 million	% change ²
Expenditure ¹	76.5	+ 23.8	75.5	84.8	+ 10.8
of which:					
— current expenditure	63.5	+ 26.2	63.0	72.8	+ 14.6
— capital expenditure	13.0	+ 13.0	12.5	12.0	— 7.7
Revenue	62.8	+ 7.9	66.1	72.0	+ 14.6
of which:					
— direct taxes	29.7	— 1.3	32.3	34.1	+ 14.8
— indirect taxes	20.7	+ 10.7	21.3	24.2	+ 16.9
Net borrowing requirement	— 13.7	—	— 9.4	— 12.8	—

¹ Disregarding debt extinction

² On the preceding year's original budget

Note. The figures in this table are based on the national budgets and are recalculated on the basis of Community definitions.

TABLE 4
Main economic indicators

	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	128	124	123	126	:	:	:	:	:	:	:	:
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	:	:	:	:	:	:	:
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	8.9	12.6	10.3	10.5	8.7	12.3
	1977	9.7	10.7	7.6	12.4	:	:	:	:	:	:	:	:
Retail turnover* (1970 = 100)	1975	160.1	159.1	161.2	164.6	171.7	161.5	166.5	165.5	173.1	180.0	174.3	183.3
	1976	180.6	178.1	177.4	188.5	180.8	186.2	189.3	186.5	201.6	186.4	187.8	203.9
	1977	192.5	192.3	:	:	:	:	:	:	:	:	:	:
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	:	:	:	:	:	:	:
Visible imports* (million Fl)	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	8 184	8 698	8 032	8 701	8 379	9 138	8 648	9 140	8 827	10 378
	1977	9 387	9 411	9 496	:	:	:	:	:	:	:	:	:
Visible exports* (million Fl)	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	8 830	8 632	8 104	8 670	8 743	8 619	9 099	8 968	10 010	9 672
	1977	8 677	8 776	:	:	:	:	:	:	:	:	:	:
Balance of trade (million Fl)	1975	+ 50	- 116	- 170	+ 820	- 415	+ 187	+ 320	- 41	- 316	+ 863	+ 41	+ 361
	1976	+ 189	+ 200	+ 646	- 66	+ 72	- 31	+ 364	- 519	+ 451	- 172	+ 1 183	- 706
	1977	- 710	- 635	- 183	:	:	:	:	:	:	:	:	:
Official gold and foreign exchange reserves (million Fl)	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	(18 750)	(20 770)	:	:	:	:	:	:	:
Money supply* (million Fl)	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	85 991	87 633	89 175	89 088	90 269
	1977	92 180	93 880	:	:	:	:	:	:	:	:	:	:

() Provisional figure

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 Source: CBS

year as a whole may be less than the expected growth of export markets (7%). However, given the likely trends in domestic demand, imports may also expand rather slowly, leading to some further shrinking of the trade deficit. With a practically unchanged net surplus on invisible trade account, the current external surplus will probably, therefore, increase a little from the 1976 level.

Over the coming months price increases may gradually catch up with the rise in nominal incomes, thus leading to a slowdown in the growth of real disposable income which in its turn may exert a dampening impact upon the rate of expansion of private consumption. Public

consumption and investment are not expected to provide an appreciable demand stimulus this year and house-building activity may lose some of its momentum. In spite of the still depressed overall profit situation, growth in fixed business investment will be appreciable this year, partly due to the stimulation of the government's fiscal allowances.

The growth of production should resume in the months ahead. Indeed, for the year 1977 as a whole, and assuming a marked recovery in the agricultural harvest, gross domestic product should expand by some 4%. This rate of expansion would hardly be high enough to create any

substantial inroads into unemployment, despite the fact that the labour force is unlikely to rise much in 1977. On average for the year, the number of unemployed is nevertheless expected to be down by some 8 000 to around 203 000 or 4.2% of the labour force.

On the assumption of a normal harvest in 1977 food prices should generally exert a dampening influence on consumer prices in the course of the year. Moreover, the decision to reduce social security premia from 1st July should help to keep down the rise in unit wage costs despite the forthcoming adjustment of wage rates at the same date. On the other hand, a renewed increase in import prices may from now on exert some upward pressure on domestic costs and prices. All in all, and including the impact of the rise in VAT rates on 1st October 1976, the index of consumer prices (wage and salary earners) is now expected to rise by 6.7% between 1976 and 1977.

As a whole, the 1977 forecasts suggest that progress toward the medium-term objectives outlined last year by the Dutch authorities may be slower than originally intended and that, in particular, the profitability of business investment may fail to improve as expected. The lesson to be drawn from this for macro-economic policy may indeed be one of modesty: there are narrow limits to the results which can be obtained through general or selective budgetary policies if the impact of such measures as are taken is absorbed by a deterioration of external competitiveness due to domestic cost increases or exchange rate appreciations. A major part of the responsibility for the Dutch economy in the medium-term thus remains in the hands of the social partners.

Major economic policy measures

October 1976:

— The Nederlandsche Bank halved the interest rates which commercial banks have to pay on borrowings in excess of their quotas.

November:

— From 1 November 1976 to 1 July 1977, a subsidy will be paid, under the programme to combat unemployment among the young, to firms that provide practical training to young unemployed persons, in notional jobs, for two days a week in accordance with the Apprenticeship Law.

— For the period from 1 November to 31 December 1976, workers may claim a flat-rate allowance of Fl 60.

— The Nederlandsche Bank decided to lower all its rates by 1% from 20 November 1977; this meant a reduction in the discount rate to 6%.

December:

— The institutions providing non-compulsory sickness insurance were authorized to raise their premiums for 1977 by up to 7%.

— Pursuant to Price Regulation 1976-II for goods and services and Regulation 1976-III on the notification of changes in the prices of goods and services, only increases in the prices of raw materials, auxiliary materials and semi-manufactures which occurred since the last reference date, i.e. 2 December 1976, may be passed on in selling prices.

— Under the new 1977 Price Regulation for goods and services, it will be possible to pass on in higher prices external costs (resulting from an increase in raw material prices for example), wage increases (only in the service industries, to the tune of 3.5%), costs such as electricity and cleaning charges (to the tune of 0.3%) and transport costs. The distributive trades are authorized to raise their margins by 3.5%. Manufacturing industry, by contrast, may not pass on wage increases, interest payments or depreciation. The reference prices are normally those prevailing on 3 December 1976.

— The scheme under which Dutch firms may obtain junior-ranking loans, with full State guarantee, totalling Fl 500 million was extended until 31 December 1977

January 1977:

— From 1 January 1977, the Nederlandsche Bank reintroduced the possibility for non-residents to contract loans by private agreement, within an overall ceiling of Fl 75 million. The loans must be for at least ten years, and are redeemable on a quinquennial basis. The issuing of borrowing authorizations to non-residents had been interrupted temporarily in May.

— In order to expand the opportunities for part-time work, Mr Boersma, the Minister responsible, introduced two measures with effect from 1 January 1977:

1. Employers providing part-time work to workers aged between 23 and 60 will receive a subsidy equivalent to 30% of the wage costs; this subsidy is available for six months in respect of workers of less than 30 years of age and for twelve months in respect of older workers.
2. The regulations concerning temporary work, under which public institutions and institutions ranking as such may take on workers on a part-time basis and claim a subsidy towards the wage costs, were extended to include part-time workers. Those aged less than 30 years must have been on the unemployment register for a continuous period of six months. They must work between twenty and thirty-five hours per week, and their annual pay, converted on the basis of a full week, must not exceed Fl 35 000.

— From 1 January, the statutory minimum wage was increased by 4.6% from its level on 1 July, bringing it to Fl 1 537.90 per month. Benefits under the general old-age insurance scheme and under the general survivor's insurance scheme went up by some 5.4%.

— The Nederlandsche Bank lowered its rates by 1% with effect from 7 January 1977. The new discount rate was 5%.

— Pursuant to a general administrative regulation no unemployment benefit will be paid to workers who, with interruptions, work for one and the same employer; workers without fixed jobs and seasonal workers are not affected.

— The Minister for Social Affairs announced details of the allocation of Fl 200 million made available by the Government for a limited supplementary employment programme for 1977. The funds will be divided in equal proportions between projects with a high employment content and projects with an average employment content and are then shared out by province. Projects will have to be carried out by registered unemployed.

February:

— A memorandum was presented to the Second Chamber on the implementation of the 1976 budget. The picture now differs appreciably from that outlined in the 1977 draft budget in September. Since then, the estimate of expenditure has fallen by Fl 781 million, while revenue has proved to be Fl 1 673 million higher. Expenditure is estimated at Fl 72 717 million and revenue totals Fl 68 515 million, giving a deficit of Fl 4 202 million instead of Fl 6 656 million in September, an improvement of Fl 2 454 million. When account is taken of the counter-cyclical items, expenditure is Fl 1 033 million lower. With expenditure totalling Fl 76 964 million and revenue Fl 66 150 million, the deficit, on this definition, is Fl 10 849 million as against Fl 13 555 million in September.

— In a letter to the Second Chamber, the Government announced that it intended to reduce, with effect from 1 July 1977, employers' contribution to the insurance scheme against incapacity for work (WAO) and to the special sickness insurance scheme in an effort to hold the increase in the wage and salary bill over 1976 to 0.5%. It also announced that the following sums had been set aside: Fl 400 million for combating excessive unemployment in certain provinces, Fl 225 million for assistance to individual enterprises and Fl 25 million for the reduction, ahead of schedule, of class sizes in primary schools; these measures are to be financed from surpluses or by the transfer of funds from the social security system.

— In a memorandum presented to the Second Chamber on economic and social policy for the years 1977 to 1980, it was announced, that an additional amount of Fl 136 million would be set aside to extend the regional investment premium schemes.

— Various measures were announced to assist Dutch exporters, notably by making available Fl 100 million for a Fund designed to help offset certain distortions of competition in export markets.

March:

— It was decided that the increase in telephone charges introduced on 1 January 1977 would be reduced by half with effect from 1 April and that the increase in postal charges would be postponed until 1 January 1978.

— The maximum rate by which public service charges may be raised in 1977 was fixed at 5%, compared with 7% previously.

— The salary limit up to which low-interest State loans may be obtained for the purchase of a dwelling in the "protected" housing market was raised from Fl 22 000 to Fl 24 000.

April:

— Under the price policy, firms may not pass on wage increases in prices. Only firms in the service industries may do so to the tune of 1% for the second half of the year, over and above the 3.5% permitted so far.

— The salary limit up to which rent subsidies are available was raised from Fl 33 000 to Fl 35 000. The range of rents covered was raised accordingly.

— Virtually all firms in the ready-made clothing industry were to be granted additional aid in the form of a lump-sum paid in respect of reduced working hours

— The Nederlandsche Bank lowered its discount rates by 0.5% (from 5 to 4½%) and the rate on advances by 1% with effect from 18 April 1977.

May:

— The Nederlandsche Bank reduced all its interest rates by 1%; the discount rate thus dropped to 3.5%.

— The Nederlandsche Bank, in agreement with the organizations representing the banks and the Post Office, decided that the growth in short-term lending to the private sector and in long-term loans not financed directly through the capital market must not exceed 12.5% in 1977

— A subsidy of 50% of costs, with a maximum of Fl 12 500 per worker and Fl 250 000 per project, will be available, under certain conditions, to employers who invest in order to improve the working environment.

— The wage cost subsidies hitherto granted to employers paying 10% or more of their wage and salary bill to workers on the minimum wage will in future also be available in respect of workers receiving up to 5% more than the minimum wage or equivalent compensation in kind.

G – Belgo-Luxembourg Economic Union

Belgium

With economic activity sluggish because of a slowdown in stockbuilding, some progress has been made in the fight against inflation. In addition, specific measures have been taken to improve the financial situation of the public sector and to reduce unemployment.

Activity is likely to gather momentum in the months ahead, although probably not sufficiently quickly to ensure a satisfactory level of capacity utilization or to permit any improvement in the labour market situation.

1. Overall assessment and main policy issues

The slackening of the rate of inflation noted last year has continued during the first few months of 1977. Thanks largely to the measures taken in 1976 to curb the growth of incomes, wage costs have increased less sharply. Since the parities were readjusted within the European "snake", all of the snake currencies have appreciated against other currencies. By May, the index of the trade-weighted exchange rate for the Belgian franc had increased by 5.2% over the level reached in September 1976. As result, the rise in import prices has been moderated, thus slowing down further the upward movement of domestic prices and costs. The rate of inflation in Belgium has therefore drawn closer to that in Germany.

The rate of expansion of economic activity has remained sluggish. At any rate, it has not been sufficiently rapid to allow any improvement on the labour market. A slowing-down in the growth both of domestic and export demand, partly due to increased international competition and structural problems in some industries, is now the major factor influencing current economic developments.

The firm trend of the Belgian franc following its realignment on 18 October has allowed a gradual relaxation of the restrictive monetary measures introduced during the months leading up to this decision. The "re-employment" ratios have therefore been discontinued and the rediscount ceilings raised. In the first half of 1977, the Banque Nationale has lowered its discount rate in stages from 9% to 6%. The financial intermediaries have followed this trend by lowering their rates for discount credits and overdrafts. But this movement has had little effect on capital market rates. Rates of interest on term deposits and on investment

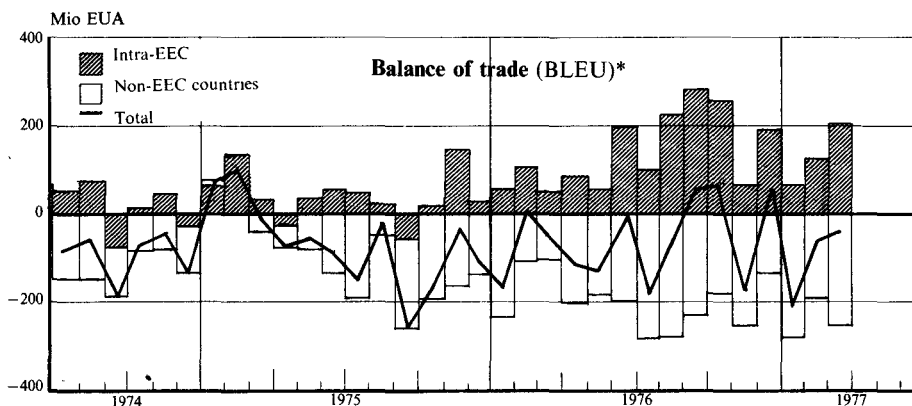
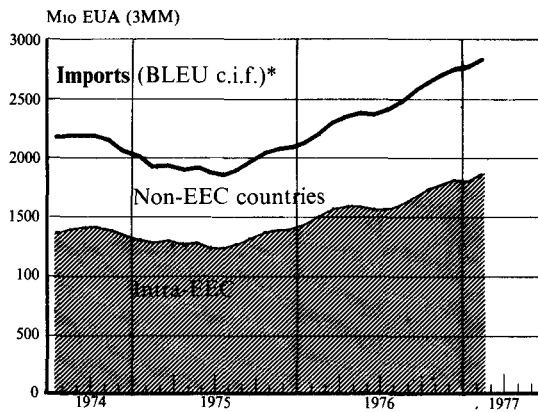
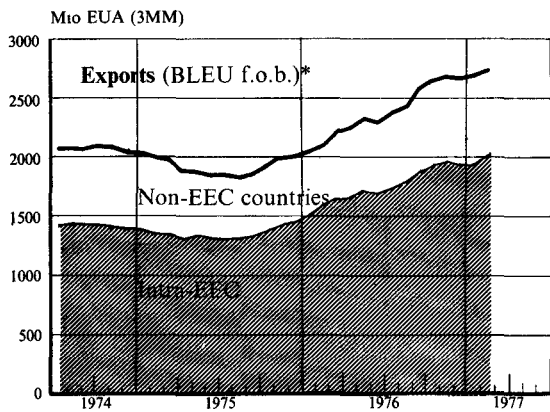
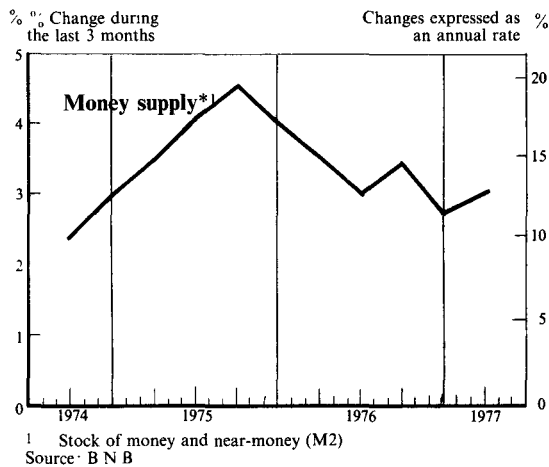
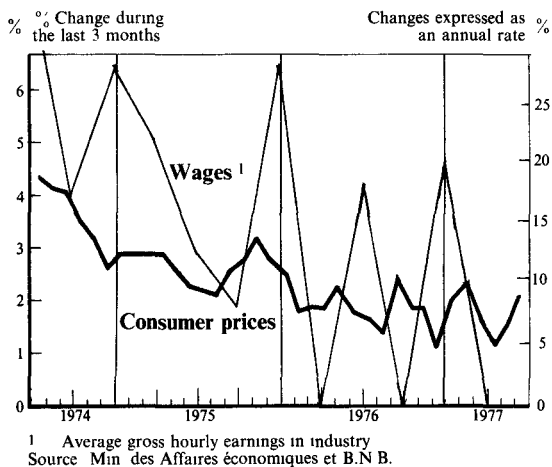
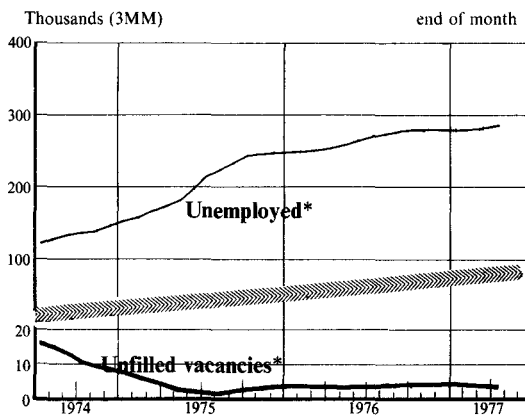
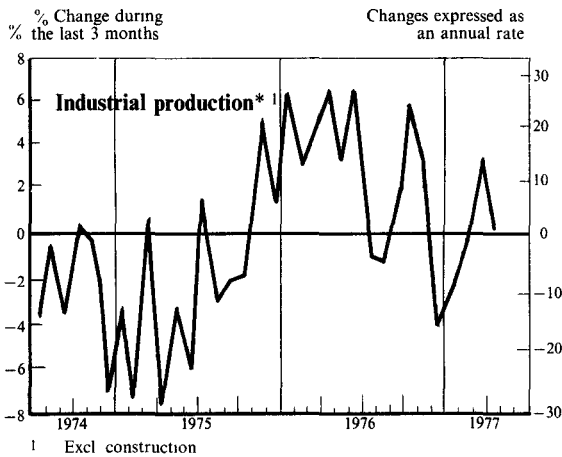
credits have been reduced only slightly by the financial institutions.

Since the difficult public finance situation has made global expansionary measures impracticable, the authorities have attempted, by means of a package of measures adopted in February (see the detailed account of the measures of 12-13 February below), to tackle the problem of unemployment along selective lines, to stimulate productive investment through tax incentives and to encourage exports. In order to improve the financial position of the Treasury and of the social security scheme, additional increases have also been made in indirect taxes and social security contributions (removal of upper limits). In spite of these tax measures, the general government net borrowing requirement in 1977 may well exceed that for 1976, even if economic growth gathers some momentum.

Owing to the early dissolution of Parliament in March, not all the measures announced were actually adopted. However, the Government implemented all those points in its programme that could be applied by decree or administrative instruments. For example, the increased VAT rates, applicable to certain items were introduced as planned on 1 April. According to the programme of the Government which was formed at the beginning of June, not all other proposed measures, which have remained in suspense, will not be adopted.

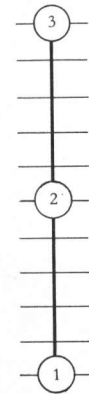
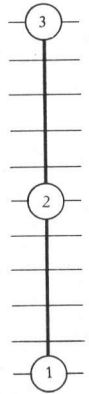
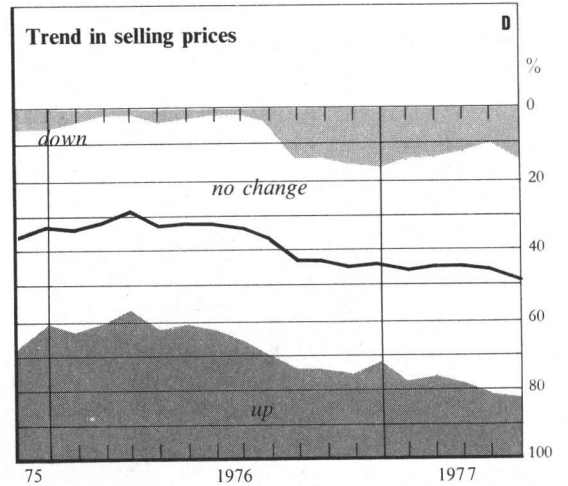
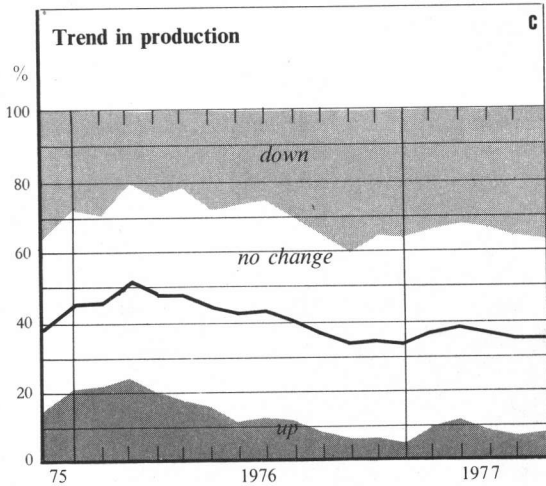
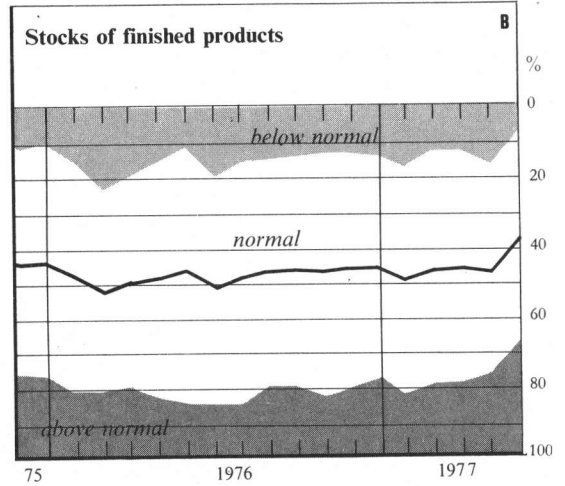
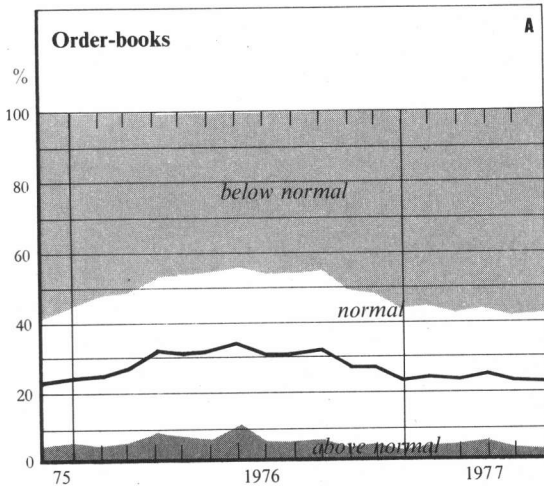
2. Recent developments

The process of reconstituting depleted stocks, which was a feature of economic developments in 1976 in Belgium as well as in its main trading partners, seems to have come to



*: Seasonally adjusted figures.
3MM: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

GRAPHS A, B, C and D: The three zones (grey, white and black) show the percentages of the three different answers.

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

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

TABLE 1
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	+ 3.2
of which: industry 1		6.7	- 6.4	+ 6.0	+ 4.0
Gross domestic product in volume per person in employment	% change	4.1	- 0.6	+ 4.6	+ 4.0
Total employment (number of persons) 2	% change	1.0	- 1.5	- 1.5	- 0.8
— Independent entrepreneurs		- 3.1	- 1.8	- 1.4	- 1.5
— Wage and salary earners in company sector		2.0	- 2.3	- 2.4	- 1.4
— General Government		2.4	+ 3.0	+ 2.2	+ 2.8
Unemployment	as % of labour force	2.3	4.5	6.1	6.9
Compensation of employees per wage and salary earner	% change	11.1	+ 15.6	+ 12.4	+ 11.2
Price index of private consumption 3	% change	6.3	+ 12.1	+ 8.8	+ 7.5
Current account balance 3	FB '000 million	38.9	+ 13.8	- 11.7	+ 1.5

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

an end at the beginning of 1977, at least as regards raw materials and semi-finished products.

For some months, the upward movement of BLEU exports has tended to level out (excluding seasonal variations). Sales to Community countries are apparently those which have slackened most while exports to non-member countries have remained fairly buoyant, probably as a result of a sharper expansion of domestic demand in these countries.

Final domestic demand (excluding changes in stocks) appears to have grown fairly steadily, although rather more slowly than at similar stages of previous economic cycles.

Owing to slackening inflation and increased welfare transfer payments, the rise of real private disposable income has generally been firm. *Private consumption* has been fairly well sustained, after some contraction of retail sales (in volume terms) had been recorded the fourth quarter of 1976. In the first five months of this year, sales of private cars were substantially up on last year. *Public consumption* has probably grown fairly sharply owing largely to an increase in the numbers employed.

Hopes of an upsurge in fixed *investment* have not been fulfilled. Only public investment has been buoyant. Activity in the residential construction industry has tended to mark time at a high level after a period of fairly brisk expansion in 1976.

Generally speaking, the growth of *output* has tended to match that of overall demand. In the first few months of 1977, the average industrial production index (excluding building and construction, not seasonally adjusted) was only slightly above the level for the fourth quarter of

1976. Nevertheless, it exceeded by 3.0% the level achieved in the corresponding period in 1976 and by 0.7% the average level in 1974 (a boom year, during which firms were operating much nearer full capacity than early in 1977).

There have been conflicting trends on the *labour market*. Although the number of wholly unemployed males of normal ability has tended to stabilize (probably because young persons have been given traineeships in firms and government offices), unemployment amongst women has again increased. The total number of unemployed (of all degrees of ability, not seasonally adjusted) increased from 278 000 at the end of December 1976 to 295 900 by the end of May. The unemployment rate (measured as a proportion of the working population) was 7.4% as against 2.7% in May 1974.

As a result of the marked deceleration in unit wage costs, the slow increase in import prices (expressed in Belgian francs) and a temporary reduction in the prices of some fruits and vegetables, the consumer *price* index rose by only 3.9% between December 1976 and June 1977, despite the increase in some VAT rates. In June the index showed a year-to-year increase of 7.7% as against 9.4% for June 1976. Wholesale prices have tended to stabilize during the period January to May after a strong rise in January. In May the index was 1.9% above the December 1976 level.

The *current account* of the balance of payments recorded a deficit in the first and third quarters of 1976 which were periods marked by intense pressures in the exchange markets, moved into surplus in the fourth quarter and was in balance in the first quarter of 1977. The improvement at the end of 1976 and in early 1977 can be attributed, not only to a reversal of leads and lags, but

TABLE 2
Demand for and supply of goods and services

Belgium	1974 ²	1975 ²			1976 ³			1977 ³		
	At current prices FB '000 million	% change on preceding year								
		Vol	Price	Value	Vol	Price	Value	Vol	Price	Value
Private consumption	1 244.5	0.8	12.1	13.0	3.3	8.8	12.4	3.0	7.5	10.7
Public consumption	312.9	7.2	16.9	25.3	4.5	10.0	15.0	3.3	9.2	12.8
Gross fixed asset formation	468.0	- 3.3	11.0	7.4	- 0.2	8.8	8.5	2.3	8.0	10.5
— Enterprises	273.8	- 4.2	9.8	5.2	- 3.5	7.2	3.4	1.3	6.8	8.2
— Dwellings	129.6	- 5.9	14.8	8.0	5.0	11.0	16.6	2.0	10.0	12.3
— General Government	64.5	6.2	8.9	15.7	3.1	10.5	13.9	6.3	8.5	15.3
Domestic final uses (excluding change in stocks)	2 025.4	0.8	12.6	13.6	2.8	9.0	12.0	2.9	7.9	11.0
Domestic final uses (including change in stocks)	2 073.1	- 2.2	13.0	10.4	4.2	9.0	13.6	2.9	7.9	11.0
Exports ¹	1 116.4	- 9.3	4.9	- 4.9	8.0	6.4	14.9	5.9	4.2	10.3
Imports ¹	1 109.2	- 9.9	6.2	- 4.4	10.6	7.2	18.6	5.3	3.7	9.2
Gross domestic product at market prices	2 080.3	- 2.0	12.4	10.1	3.0	8.6	11.9	3.2	8.2	11.6
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	2 025.4	0.8		13.2	2.8		12.0	3.0		11.1
Change in stocks	+ 47.7	- 3.1		- 2.8	1.4		1.5	0		0.1
Balance of exports and imports ¹	+ 7.2	0.3		- 0.3	- 1.2		- 1.6	0.2		0.4

¹ Goods and services

² Source: Institut national de Statistique, National accounts

³ Estimates of Commission's Departments

also to a real improvement of the balance of trade reflecting movements in the economy and, in particular, the end of a period of restocking. In the first quarter of 1977, the *overall balance of payments* was in surplus by FB 12.5 billion largely as a result of an inflow of direct foreign investment funds and of purchases by oil-producing countries of public sector debt.

3. Outlook

An examination of the various indicators of world trade prospects, and of the impact of present economic policies in Belgium and in its trading partners, does not suggest any significant change in current trends. Domestic demand (excluding stockbuilding) should continue to grow by about 3%. This growth should be accompanied by an improvement in the external balance, linked to the slowdown in stockbuilding. The propensity to invest should improve only slowly, but is not likely to give any appreciable boost to activity and employment in the near future. Taking 1977 as a whole, gross domestic product should increase by about 3 to 3½% compared with 1976. There is not expected to be any increase in employment except in the public sector and in some service industries. However, the measures introduced or announced concerning early retirement, traineeships for young people and special employment by public authorities, should

help to slow down the growth of unemployment. However, for 1977 as a whole, the average number of unemployed will, no doubt, be higher than in 1976.

Since the factors which helped to curb the upward movement in the consumer price index during the first four months of 1977 are either ceasing to have effect or are now having a contrary effect, the rate of increase is likely to accelerate a little in the months ahead. Taking 1977 as a whole, however, the index should rise less than in 1976, especially if the rise in import prices remains around 3.5% as currently expected. On this assumption, the balance on current account is likely to remain in surplus.

Amongst the various elements which go to make up the economic outlook for 1977, the imbalance in public finance can be seen to be the problem which, as time goes on, will prove to be the most intractable. As there is unlikely to be any spontaneous improvement during the years ahead, a further increase in the burden of taxation can be avoided only by severely limiting the growth of current expenditure and, more especially, of transfer payments. A reduction in unemployment must be achieved by continuing the present policy of selective measures and action at specific points rather than by further increasing public-sector employment and procurements, which would serve only to aggravate the budgetary position in the longer term.

TABLE 3
The Central Government Budget

Belgium	1976			1977	
	Original budget		Provisional outturn	Original budget	
	in FB '000 million	% change ²	in FB '000 million ³	in FB '000 million	% change ²
Expenditure ¹	851.0	+ 18.0	890.5	993.4	+ 16.7
of which:					
— current expenditure	732.7	+ 18.1	768.4	852.0	+ 16.3
— capital expenditure	118.3	+ 16.9	122.1	141.4	+ 19.5
Revenue	726.0	+ 12.8	734.9	863.2	+ 18.9
of which:					
— direct taxes	415.7	+ 19.3	410.0	504.5	+ 21.4
— indirect taxes	280.7	+ 4.9	294.4	326.2	+ 16.2
Net borrowing requirement	- 125.0	—	- 155.6	- 130.2	—

¹ Disregarding debt extinction

² On the preceding year's original budget

³ Provisional outturn

Note The figures in this table are based on the national budgets and are recalculated on the basis of Community definitions

Major economic policy measures

January 1977:

— The Banque Nationale decided to reduce, as from 6 January, its official discount rate and rate for advances in current account from 9% and 10% respectively to a uniform 8%. The discount rate had not been changed since 13 August 1976, whereas the advances rate had been raised substantially on 1 October. At the same time, the bank reduced its special rates to 8.5% and increased the rediscount ceilings for financial intermediaries by 10% (from FB 53 700 to 59 100 million).

— The commercial banks reduced their short-term lending rates, as from 7 January, by between 1% and 1.25%. The discount lending rate then stood at between 9.75% and 10% and the overdraft rate at between 10.5% and 10.75% (including margin).

— The Government decided to release 10% of the public investment credit for the first two months of 1977 (approximately FB 1 600 million for January and February). In 1976, 40% had been released for the first four months.

— As from 17 January, the financial intermediaries reduced their interest rates on short-term deposits by between 0.25% and 1% according to the term.

— On 19 January many banks decided to reduce their discount and acceptance credit rates by 0.50%. The base rates fell to 9.25%. The interest rates for overdrafts remained unchanged.

— The Government tabled a draft law adjusting the sickness insurance arrangements, including the abolition of the ceiling for calculating contributions relating to loss of earnings. This measure was to remain valid from 1 April 1977 to 31 March 1978; between 1 April and 31 December 1977, workers will be paying a "solidarity" social security contribution of 0.40% of wages and salaries (on which no ceiling was imposed), the solidarity contribution to be suspended if the number of wholly unemployed falls below 200 000 (the additional revenue is estimated at FB 3 500 million); the income ceilings used to calculate the social security contributions of self-employed persons were raised from FB 700 000 to FB 840 000 for the last nine months of 1977.

— On 27 January the banks reduced the interest rate charges on overdrafts by 0.50% to 10.25%.

— A royal decree implementing the economic recovery act of 30 March 1976 specified that private firms employing less than 100 workers may take on a single trainee, for whom they receive a flat-rate grant of FB 30 000 when the trainee has completed six months or twenty-six weeks with a firm.

— The supplementary regional aid scheme (a 2% reduction in interest rates) laid down in the act on economic expansion was extended until 30 June 1977.

— A draft bill, designed to create jobs by temporarily reducing employers' social security contributions, stipulated that such contributions would not be payable by certain employers for two consecutive quarters in respect of workers newly taken on, provided such workers represented a net increase in their number of employees.

February:

— The Government extended from 1 to 28 February the decree restricting maximum mortgage lending ratios issued in May 1976 to curb the sharply rising trend in prices in the building industry

— On 9 February the banks decided to reduce their discount and acceptance credit rates by 1 point to 8.75% and their overdraft rates by 0.25 point to 10.0%.

— At its "conclave" on 12 and 13 February, the Government decided to take the following measures:

— To stimulate the economy: tax relief on supplementary investments by firms, partial tax immunity under certain circumstances for the reinvestment of capital gains realized, encouragement to self-financing by private firms, easier depreciation rules and special investment aid within the framework of the economic expansion acts; it was also decided to implement in the first six months of this year more than half of the public investment programme for 1977.

— To create jobs and reduce unemployment, measures were proposed for increasing employment in small and medium-sized enterprises, particularly by extending the use of employment grants and by encouraging exports. Provision was also made for increasing the number of trainees and the number of unemployed taken on by the public authorities, for introducing early retirement for those wholly unemployed for more than a year, for extending the school-leaving age from 14 to 16 and for improving vocational training arrangements.

— Finally, to strengthen the Treasury's financial position supplementary credits were cut from FB 30 000 million to FB 10 000 million. Additional revenue amounting to some FB 16 000 million was expected from an increase in VAT on cigarettes, petrol, wines, apéritifs, hotel accommodation and catering, leather goods, etc. and some other direct taxes.

— The Banque Nationale reduced its discount rate from 8% to 7% and the acceptance credit from 8.5 to 7.25% as from 17 February.

— The rules restricting the lending ratios on the market value of property pledged against mortgage loans were extended until 31 May 1977.

— On 22 February the banks lowered their lending rates by 0.50%, thus reducing their base rate for overdrafts to 9.50% (including margin) and that for discount and acceptance credit to 8.25%.

TABLE 4
Main economic indicators

	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	119.0	117.8	117.0	121.4	124.8	121.0	116.7
	1977	122.3	120.8	120.7	122.5	.	.	.	.	.	.	.	.
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	.	.	.	.	.	.	.
Construction: Permits for residential construction*	1974	7 992	7 476	7 330	8 416	8 937	7 491	9 721	7 472	7 328	5 738	5 579	5 809
	1975	5 855	6 142	5 726	6 061	4 842	6 301	5 231	6 096	6 888	6 301	7 143	8 168
	1976	7 676	8 182	8 138	7 192	7 886	8 227	6 610	8 484	7 611	8 360	7 663	9 747
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	135.2	132.7	135.2	131.2	132.7	136.2
	1977	137.2	136.5	.	.	.	.	.	.	.	.	.	.
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	.	.	.	.	.	.	.
Visible imports* (billion FB)	1975	89.73	90.33	89.82	89.89	84.31	91.43	94.59	88.10	99.33	99.98	102.80	109.23
	1976	104.16	103.10	107.07	112.32	107.10	115.52	113.43	116.00	121.44	113.57	118.33	109.01
	1977	117.04	116.29	118.98	.	.	.	.	.	.	.	.	.
Visible exports* (billion FB)	1975	91.46	90.96	85.35	83.40	80.86	85.12	85.19	84.86	83.39	88.01	98.14	91.00
	1976	91.30	99.60	98.59	98.76	97.92	108.71	97.12	111.98	113.52	112.81	102.78	110.72
	1977	106.16	108.48	117.33	.	.	.	.	.	.	.	.	.
Balance of trade (billion FB)	1975	+ 1.73	+ 0.63	- 4.47	- 6.49	- 3.45	- 6.31	- 9.40	- 3.24	- 15.93	- 11.98	- 4.65	- 9.23
	1976	- 12.86	- 3.51	- 8.48	- 13.56	- 9.18	- 6.80	- 16.31	- 4.02	- 7.92	- 0.76	- 19.55	+ 1.71
	1977	- 10.87	- 7.31	- 1.65	.	.	.	.	.	.	.	.	.
Official gold and foreign exchange reserves (billion FB)	1975	217.4	223.1	224.9	226.6	230.9	234.1	236.2	238.2	234.6	235.9	- 4.65	- 9.23
	1976	223.0	218.4	216.0	208.2	207.8	207.2	200.5	199.4	185.7	185.5	- 15.55	+ 1.71
	1977	208.3	211.9	215.1	(219.0)	(222.5)	.	.	.	.	.	.	.
Money supply* (billion FB)	1974	.	.	1 312.7	.	.	1 337.6	.	.	1 368.9	.	.	1 408.0
	1975	.	.	1 456.7	.	.	1 515.7	.	.	1 584.9	.	.	1 650.0
	1976	.	.	1 708.5	.	.	1 759.9	.	.	1 819.9	.	.	1 869.4

Not available

() Provisional figure

* 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

— The financial intermediaries reduced their interest rates on time deposits by between 0.50% and 1% according to the term. The rate for six-month deposits was cut from 7% to 6.5%, while rates for savings accounts and for sums deposited for more than twelve months remained unchanged.

April:

— As a result of the dissolution of Parliament, a number of measures provided for in the Egmont Plan could not be implemented. This applied also to other proposals which had still to be approved by Parliament (mainly measures relating to sickness insurance, such as the "solidarity" contribution). However, the Government decided to implement as many measures in the Plan as possible by means of royal decree or ministerial directive. This covered the following: the exemption from the withholding

tax chargeable on interest payments made in respect of certain loans raised abroad, price control measures, the special employment of unemployed persons by public authorities, the employment of a larger number of trainees, rules against "moonlighting", the extension of early pension rights, aid to intangible investments and the speeding up of the public authority investment programme.

— The VAT charged on a number of so-called luxury products was increased with effect from 1 April. The Minister for Finance estimated that this would provide additional revenue of FB 13 500 million.

— The CMCES (Comité Ministériel de Coordination Economique et Sociale) decided to grant the textile industry employment credit. This credit amounted to FB 20 000 per person employed by firms with a labour force of more than fourteen. Employment in the firms must be maintained up to at least 90% for a year. The interest charged by the banks granting this credit will be borne by central government.

— The CMCES approved an increase in the ceilings for market values and borrowable amounts for middle-range subsidized housing (by from FB 150 000 and FB 300 000 according to the type of housing).

— The Government approved royal decrees relating to taxation, notably those concerning easier declining balance depreciation rules for investments made in 1977, exemption in some cases from the withholding tax applicable to interest payments on loans raised abroad, tax immunity for capital gains from 1 March 1977 onwards, subject to their reinvestment within a specified period, and new investment.

— At the end of April, the banks reduced their base rates for discount credit by 0.50% and that for cash advances by 0.25%.

May:

— With effect from 5 May, the Banque Nationale lowered its interest rates by 0.5%. The discount and acceptance rates were cut from 7% to

6.5% and the special rates from 7.25% to 6.75%. The last change occurred on 17 February.

— On 5 May, the banks again decided to reduce their rates for discount credit by 0.50% and those for overdrafts by 0.25%. The respective rates now ranged from 7% to 8% and from 8.50% to 9.50%.

June:

— The ceilings for market value and borrowable amounts for middle-range are increased by 10% from the 1st of June. Thus the borrower can obtain credit equal to 70% (previously 60%) of the market value of his mortgage, with a maximum of 3 million francs.

— The financial intermediaries reduced the interest rates on short-term bonds by 0.25%.

— On 23 June the Banque Nationale reduced its discount rate from 6.5 to 6%. The special rates were lowered from 6.75% to 6.25%.

Luxembourg

With the economic situation dominated by continuing crisis in the steel industry, offset in part only by the progress made in other branches of manufacturing industry and in the services sector, the Luxembourg authorities are still faced with the unfamiliar problem of creating jobs and reducing unemployment.

Although the available indicators offer little prospect of any really rapid improvement in the months ahead, the somewhat sporadic recovery already under way and the accompanying slow improvement in the economic climate should ensure continued expansion of activity in 1977, though at a less rapid pace than in 1976.

1. Overall assessment and main policy issues

The sluggish period following a short-lived spurt at the end of 1975 and at the beginning of 1976 has continued into 1977, mainly owing to the slackness of world demand for steel products and the lack of investment buoyancy.

As a result, Luxembourg — a country which had enjoyed full employment for many years — now has a number of

problems to contend with in this area. The departure of foreign workers has not prevented the appearance of unemployment which — in addition to its cyclical aspect — has, in common with other Community countries, a structural component which is reflected in the imbalance between the skills possessed by job applicants and those required by potential employers. The structural problem is particularly acute for young people.

TABLE 1
Key indicators

Luxembourg	Unit	1970-1974 average ^{4 5}	1975 ⁵	1976 ⁶	1977 ⁶
Gross domestic product, volume of which: industry ¹	% change	4.1 :	— 8.4 — 18.3 ⁶	3 7.1	2 3.3
Gross domestic product in volume per person in employment	% change	1.7	— 8.6	4.6	2.8
Total employment (number of persons) ²	% change	2.4	0.2	— 1.5	— 0.8
— Independent entrepreneurs		— 3.6	— 2.6	— 1.8	— 2.3
— Wage and salary earners in company sector		3.9	0.4	— 1.7	— 0.8
— General Government		2.2	2.9	0.7	1.4
Unemployment	as % of labour force	0	0.2	0.3	0.5
Compensation of employees per wage and salary earner	% change	12.9	12.5	10	10
Price index of private consumption ³	% change	6	10.7	9.8	7.5
Current account balance ³	Mio Flux	:	— 2 400 ⁶	— 3 600	— 3 200

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 Departements.

· No data available

When the crisis began, the authorities immediately acted to combat unemployment and — with the exception of special government-sponsored work schemes for workers in danger of redundancy which were terminated in April — have continued to rely on the schemes adopted for this purpose, namely short-time working and budgetary measures designed to give a direct boost to activity in the building and construction industry.

In order to examine the problems of employment more closely, the Government organized a tripartite conference in April. In addition to its own representatives, the conference was attended by delegates from both sides of industry. One of the tasks set was to study medium-term employment in the light of population trends and the likelihood of a substantial reduction in jobs in the steel industry between now and 1980.

As regards the 1977 financial year, the authorities have laid stress on promoting investment by increasing appreciably the appropriations of the extra-budgetary funds. The financing of this policy has been helped by the growth in tax revenue accruing from local financial activities.

However, in an open economy such as that of Luxembourg, where exports are almost as important as domestic demand, there are strict limits to stimulatory action by the central government and even less than in other countries

can such action alone get the economy overall moving again.

2. Recent developments

Although some industries, such as chemicals, have been buoyant, economic activity generally has again been deeply affected by the crisis in the steel industry.

In spite of some recovery in March and April, new orders for steel products, in the first five months of the year were 3% down on the same period last year. Deliveries also fell markedly over the same period. Even though other industries continue to benefit from a high level of demand, *exports* are unlikely to have increased either in volume or value terms.

There has again been no uniform pattern in the trends of the various demand components. *Private consumption*, probably helped by a reduction in the saving ratio, has again been buoyant. The emphasis, in the purchases by households, was mainly on durable goods: for example, purchases of cars in the first four months of 1977 were 17.3% up on the same period last year. However, although credit demand from households increased throughout the whole of 1976, *investment* in property has continued to decline and the apparent increase in building permits at the beginning of the year cannot lead to an upturn in demand beyond a few months at most.

TABLE 2

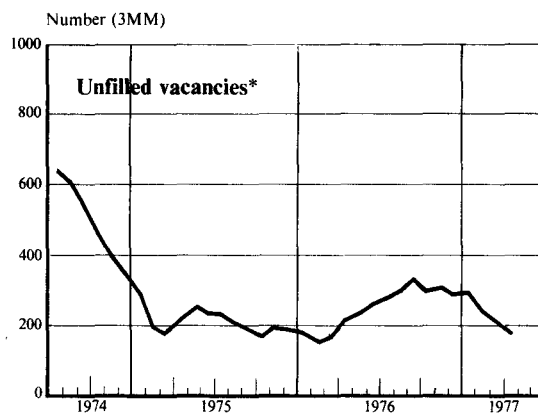
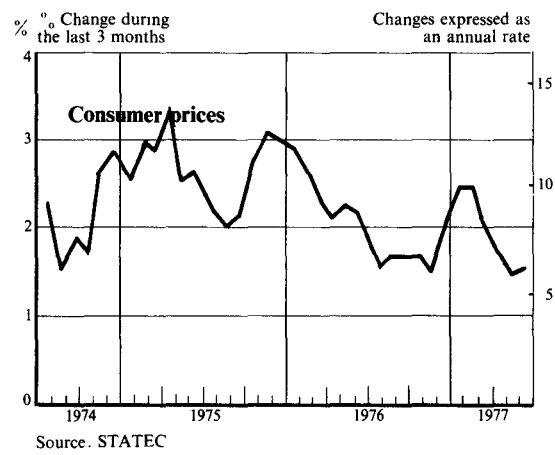
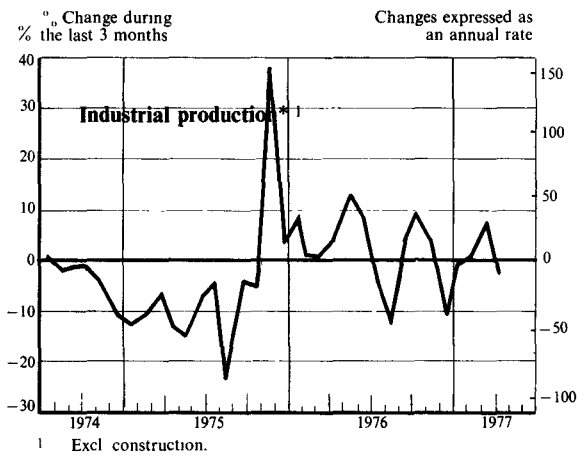
Demand for and supply of goods and services

Luxembourg	1974 ²	1975 ²			1976 ³			1977 ³		
	At current prices mio Flux	% change on preceding year								
		Vol	Price	Value	Vol	Price	Value	Vol	Price	Value
Private consumption	42 861	2	10.7	12.9	3	9.8	13.1	2.5	7.5	10.2
Public consumption	10 037	3.4	17.2	21.2	2	9.9	12.1	2	10	12.2
Gross fixed asset formation	22 802	- 8.6	13	3.3	- 4.5	7.2	2.4	4.3	8.5	13.2
— Enterprises	:	:	:	:	- 9.9	6.3	- 4.2	6.8	9.4	16.9
— Dwellings	:	:	:	:	-10	8	- 2.8	0	8.2	8.2
— General Government	:	:	:	:	10.7	8	19.6	4	7.3	11.6
Domestic final uses (excluding change in stocks)	75 700	- 1	12.2	11.1	0.8	9.1	10	2.9	8.1	11.3
Domestic final uses (including change in stocks)	77 011	- 0.2	11.9	11.7	0.8	8.9	9.8	2.3	8	10.5
Exports ¹	82 087	-13.5	- 8.3	-20.7	3.2	0.9	4.1	3	3	6.1
Imports ¹	69 927	- 5.3	5	- 0.6	0.5	7.1	7.6	3.3	3	6.5
Gross domestic product at market prices	89 171	- 8.4	0	- 8.4	3	4	7.1	2	8.4	10.6
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	75 700	- 0.9	:	9.4	0.8	:	10.3	3	:	11.9
Change in stocks	1 311	0.7	:	0.7	0	:	0	- 0.5	:	- 0.5
Balance of exports and imports ¹	12 160	- 8.2	:	-18.5	2.2	:	- 3.2	- 0.5	:	- 0.8

¹ Goods and services.

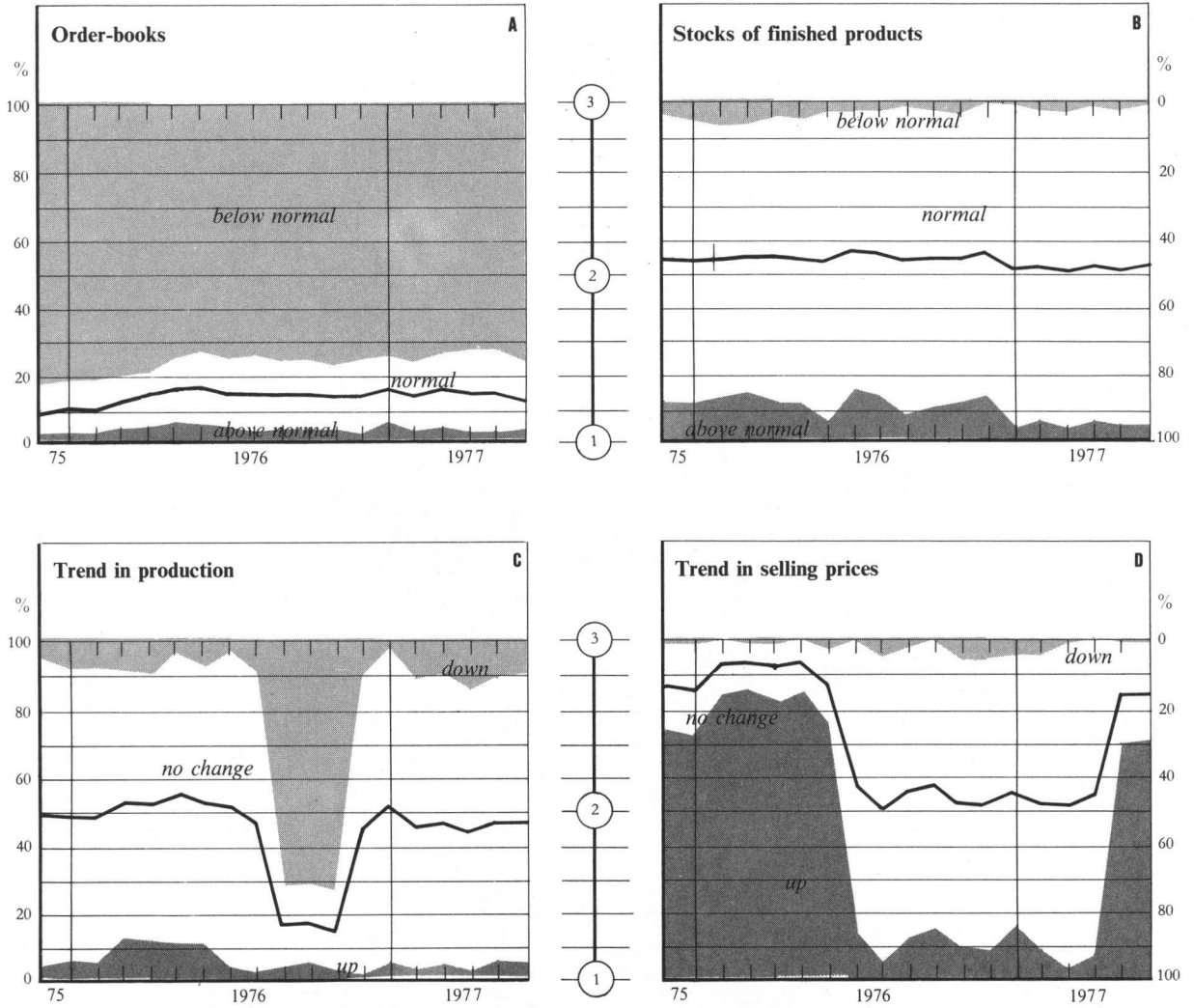
² Source: Stacc, completed for 1976 by estimates of Commission's Departments

³ Estimates of Commission's Departments
No data available



*: Seasonally adjusted figures.
 3MM: three month moving average.
 Source: EUROSTAT, except where otherwise indicated.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

GRAPHS A, B, C and D: The three zones (grey, white and black) show the percentages of the three different answers.

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

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

Investment by firms has remained depressed pending the implementation of the investment plans announced by the steel industry. Only general government investment has remained steady.

For the first four months of 1977, the seasonally-adjusted industrial *production* index showed about a 2% increase over the corresponding period in 1976. According to the more detailed STATEC index, this percentage conceals divergent trends amongst the different industries, ranging from a slight decrease in the steel industry (-1.1%) to a 5.6% increase in other industries. In the building and construction industry, there was a 5.4% fall during the period in question compared with the same period last year. Although the index does not cover all activity in the industry, it is clear that the crisis, particularly in the building sector, remains severe.

The low level of capacity utilization has caused a continuing fall in *employment* in industry, without other sectors, such as the services industry, being able to absorb the surplus manpower released. The number of workers in the steel industry has fallen by some 400 in five months and by some 800 in twelve months. By the end of March, the number of workers in industry had fallen by 2.4% compared with a year ago, while the corresponding rate of decrease for foreign workers was 2.2%.

Inflation has continued to slacken. The year-to-year rate of increase fell from 7.9% in January to 7.6% in June, the lowest rate recorded since January 1974. Foodstuffs seem to have been least affected (up 4.4% in May compared with a year before) and beverages and tobacco the worst hit (up 20.9% over the same period).

As imports must have increased more rapidly than exports, the heavy trade balance is probably continuing, although this should have been offset in part by an appreciable external surplus on factor income owing to the increase in financial activities in the country.

3. Outlook

In the short term, there is unlikely to be any appreciable strengthening of the external or internal stimuli from which the economy might benefit. However, the implementation by the Commission of an "emergency plan" for the steel industry of the Community could bring about an improvement of climate in this sector and, in particular, a slight rise of export prices in the course of the second half of 1977.

Given the present state of order books and the outlook for export demand, the growth in merchandise exports seems unlikely to accelerate appreciably during the remainder of the year. Only exports of services should prove to be buoyant. However, thanks to rationalization investment in the steel industry and to a steady expansion of general government investment, gross fixed asset formation should stage a modest recovery. Consequently, despite a slightly slower rate of increase of private consumption in volume terms, final domestic demand (excluding changes in stocks) should increase overall by around 3% compared with less than 1% last year. As investment in stocks will now probably mark time and as the external balance seems unlikely to improve in the short term, gross domestic product in real terms should increase by about 2% in 1977.

The rate of consumer price rises is unlikely to exceed the levels recorded early in 1977. Taking the year as a whole, therefore, the index should increase by only a good 7% compared with 9.8% in 1976.

The general government net borrowing requirement, which last year turned out to be a little lower than initially expected, may well — on the basis of present estimates and forecasts — increase from Flux 500 million in 1976 to some Flux 1 000 million in 1977. As a deficit of this order is unlikely to pose any problems, the main economic policy preoccupations relate to the longer-term outlook, the key to which is demand in the steel industry.

TABLE 3

The Central Government Budget ¹

Luxembourg	1976			1977	
	Original budget		Provisional outturn	Original budget	
	Flux '000 million	% change ²	Flux '000 million ³	Flux '000 million	% change
Expenditure ⁴	30.3	+ 17.4	31.7	35.6	+ 17.5
Revenue ⁵	29.6	+ 12.5	32.1	34.6	+ 16.9
of which:					
— direct taxes	15.7	+ 15.4	—	19.6	+ 18.5
— indirect taxes	9.4	+ 9.3	—	10.7	+ 13.8
Net borrowing requirement	- 0.7	—	+ 0.4	- 1.0	—

¹ Ordinary and extraordinary budget

² On the preceding year's original budget.

³ Estimates.

⁴ Disregarding debt extinction.

⁵ Without borrowing.

TABLE 4
Main economic indicators

	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	.	.	.	.	.	.	.	.
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	181	191	.	.	.	.	.	.	.	.
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	.	.	.	.	.	.	.

() Provisional figure

Not available

* Seasonally adjusted

Source: EUROSTAT (except as otherwise indicated).

Industrial production, excluding construction

Unfilled vacancies, end-of-month figures

- Consumer prices, all households

Major economic policy measures

November 1976.

— An agreement was concluded with France to build up reserve stocks of crude oil and/or petroleum products on French territory for firms established in Luxembourg.

— With a view to providing resources for the unemployment fund, adjustments were made to the basis of tax assessment and to tax rates applicable to supplementary pay.

— A maximum price was fixed for the sale to the consumer of solid mineral fuels for domestic use.

December:

— The central government budget for 1977 was adopted by Parliament. It provides for ordinary revenue totalling Flux 34 600 million and extraordinary revenue totalling Flux 1 000 million, the corresponding figures for expenditure being Flux 31 500 million and Flux 4 600 million respectively. With expenditure at Flux 36 100 million and revenue at

Flux 35 600 million, the deficit is in the region of Flux 500 million (or about Flux 1 000 million if the Community system is applied).

— Family allowances were increased.

— The salaries of Government civil servants were increased by 2%.

January 1977:

— The minimum wage was increased and extended to cover persons in domestic service, persons working at home and persons employed by family undertakings.

— Pay scales for bank employees were restructured, family allowances were increased and measures to help young people in this service industry were also adopted.

February:

— An indexed savings contract scheme was introduced. Under this scheme, a saver must undertake to pay in over a period of five years a sum agreed in advance (up to a maximum of Flux 6 000 per month). The interest rate will be the average rate of inflation calculated at the end of the year (plus a bonus of 0.50% per annum), but subject to a lower limit of 7% and an upper limit of 9% per annum.

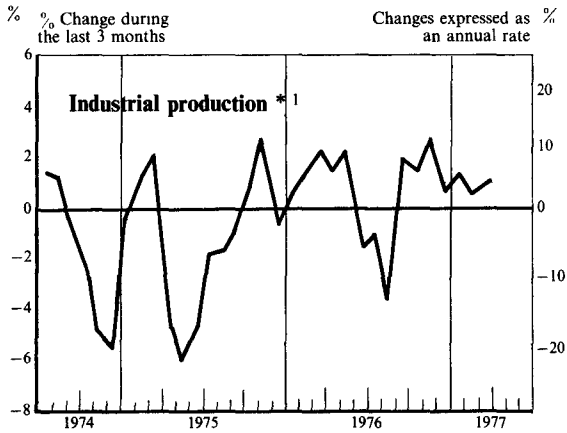
H – United Kingdom

Confidence in the financial situation of the United Kingdom has improved markedly since the turn of the year.

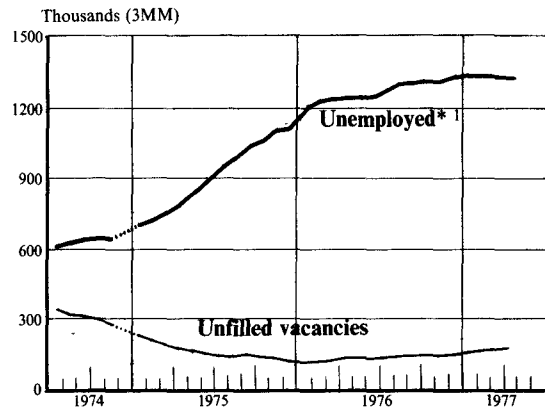
The fiscal measures announced in December 1976, the granting of the IMF loan facilities, the sterling balances arrangement and the new Euro-currency loan have brought stability to the foreign exchange markets, strengthened the reserves and enabled domestic interest rates to fall rapidly from their crisis levels. At the same time, strong growth of North Sea oil production has helped to produce a marked turn round in the current account of the balance of payments.

However, the growth in output has remained sluggish, high unemployment has persisted and some increase in the rate of inflation has been recorded.

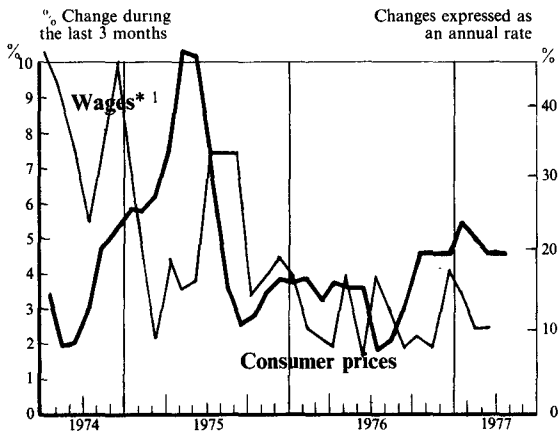
Uncertainties persist about the outlook for incomes policy but, provided a satisfactory agreement can be found that does not undermine domestic or overseas confidence, the outlook is for a modest recovery in domestic demand in the second half of 1977, together with strong export growth. The current account of the balance of payments should have moved firmly into surplus before the end of the year and a marked fall in the rate of inflation should have occurred. Unemployment, however, is likely to increase.



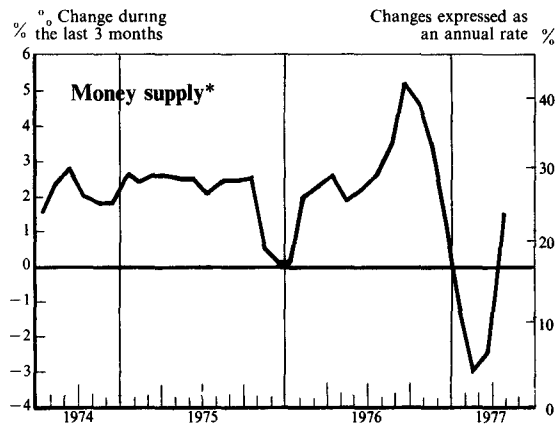
1) All industries
Source: C.S.O.



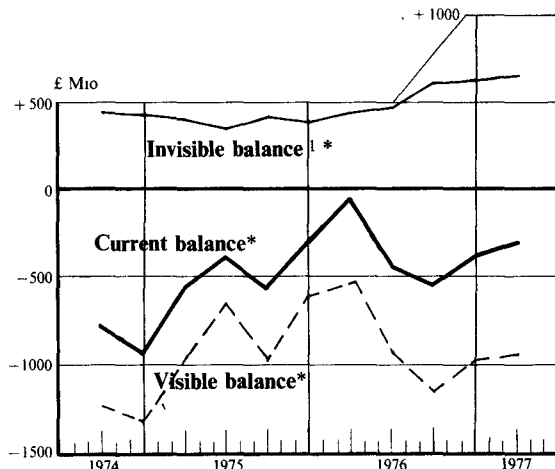
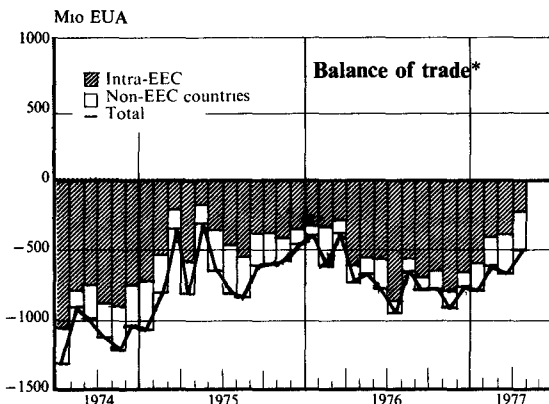
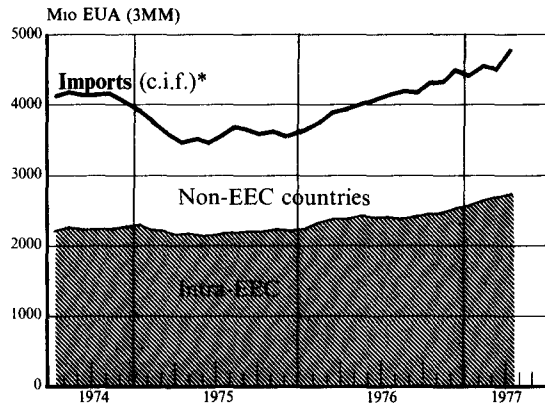
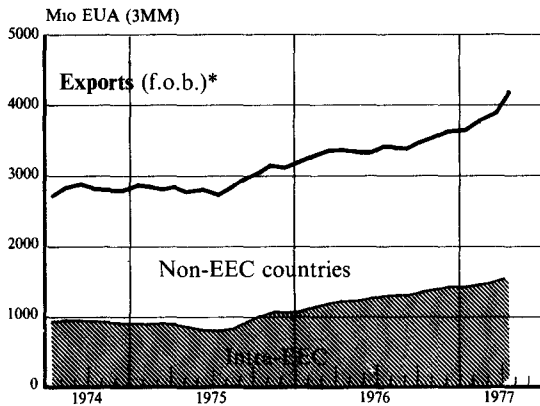
1 Excl. school-leavers and adult students
Source: Dept. of Employment



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.
3MM: three month moving average.
Source: EUROSTAT, except where otherwise indicated.

1. Overall assessment and main policy issues

The first half of 1977 was marked by a restoration of financial stability and confidence in the United Kingdom economy, resulting from a series of major policy decisions.

On 15 December 1976, the UK Government announced a set of measures designed to reduce inflation, to strengthen the balance of payments and to promote a lasting recovery in output and employment. In particular, these measures included:

- reductions in the planned levels of public expenditure for the financial years 1977/78 and 1978/79;
- specific targets for the Public Sector Borrowing Requirement (PSBR) and Domestic Credit Expansion (DCE) for 1977/78 and 1977/79.

Subsequent to these policy measures, the International Monetary Fund (IMF) agreed to make available the UK's remaining credit tranches with the Fund which would allow the UK to draw up to SDR 3 360 million in stages over a two-year period. In addition, the Bank of International Settlements, with the support of the central banks of eleven countries, established a \$3 billion safety net for sterling, to protect the UK foreign exchange reserves against possible withdrawals of official sterling balances. Furthermore, on 24 January 1977, the Government announced the arrangement made by a group of UK and foreign banks to raise a medium-term loan of \$1.5 billion on behalf of the Government.

These measures, together with the tight monetary policy established in the latter part of 1976, led to a marked recovery in domestic and overseas confidence at the turn of the year. This was reflected, in particular, in the strong

and sustained downward trend in interest rates, and in the large swing in the overall balance of payments. Despite a massive inflow of capital, the authorities maintained a steady exchange rate. Apart from speculative capital movements, the official reserves increased in the opening months of 1977 to record levels as a result of:

- drawings on the IMF standby facility (\$1 200 million) and on the Eurocurrency loan (\$1 000 million);
- the unwinding of leads and lags established during 1976;
- the phasing-out of the use of sterling for financing third-country trade.

In addition, the current account of the balance of payments has clearly been improving in recent months, largely because of increased North Sea oil production and a more favourable development of the non-oil trade balance.

Helped by the rapid fall in domestic interest rates from the very high level (15%) established in the autumn of 1976, there were unprecedentedly large sales of public sector debt to the non-bank private sector which, together with the lower than expected outturn for the PSBR for the financial year 1976/77, caused the growth of the money supply as broadly defined (M3) to cease in the early months of 1977; indeed some contraction in M3 took place in the first quarter of the year, followed by resumed growth in April.

Despite the return of financial stability, other aspects of the economic situation continued to give cause for concern. In particular:

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	+ 1.8	+ 0.8
of which: industry ¹		+ 1.7	+ 1.6	+ 1.6	+ 2.3
Gross domestic product in volume per person in employment	% change	+ 2.2	- 1.0	+ 2.6	+ 1.1
Total employment (number of persons) ²	% change	+ 0.3	- 0.7	- 0.8	- 0.3
— Independent entrepreneurs		+ 0.8	0.0	0.0 ⁶	:
— Wage and salary earners in company sector		+ 0.1	- 0.7	- 1.2 ⁶	:
— General Government		+ 1.7	+ 3.7	+ 2.6 ⁶	:
Unemployment	as % of labour force	2.8	3.7	5.2	5.9
Compensation of employees per wage and salary earner	% change	+ 13.9	+ 30.6	+ 14.9	+ 11.1
Price index of private consumption ³	% change	+ 7.5	+ 23.4	+ 15.2	+ 15.0
Current account balance ³	£ mio	- 436	- 1 650	1 476	+ 250

¹ Manufacturing industries.

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

- only very slow growth in industrial production has been recorded in recent months;
- unemployment, falling slightly for a few months, rose sharply in June and remains disturbingly high;
- the underlying rate of inflation has increased, touching 20% in April;
- the implications for the growth in earnings of the present talks on incomes policy are not yet clear.

On 29 March 1977, the Chancellor of the Exchequer announced his Budget. The estimated outturn for the PSBR in 1976/77 (\$ 8 800 million) which was well below earlier official forecasts, together with the projection of a marked fall in 1977/78 (to £7 400 million), enabled the Chancellor to reduce the burden of personal taxation without breaching the ceilings for PSBR as indicated in the Letter of Intent to the IMF. Direct taxes were reduced (by £2 300 million in a full year) to offset fiscal drag, part of the consequent loss in Government revenue being met by increases in indirect taxation (£810 million¹ in a full year). Certain of the direct tax adjustments (£960 million in a full year), however, were made conditional upon a satisfactory agreement being reached between the Government and the Trades Union Congress (TUC) on the next stage of incomes policy. The Budget also included the extension of special measures designed to support employment.

Overall, the United Kingdom Government's present policy stance is in line with recent recommendations of the Commission. The firm grip on monetary expansion established by the end of 1976, the fiscal policies announced on 15 December 1976, and the shift in the burden of taxation introduced in the March Budget, provide the basis for a longer-term strategy designed to limit the absorption of resources by the public sector and permit the sustained expansion of net exports and investment, and thereby of employment; at the same time, reducing the rate of inflation is to be achieved by firm control of the monetary aggregates together with agreement on a voluntary incomes policy.

2. Recent developments²

Compared with the previous half year, there is likely to have been little increase in the level of real output or demand in the first half of 1977. When measured on the basis of output data, Gross Domestic Product (GDP) rose by just under 1/2% between the fourth quarter of

¹ This figure excludes the loss of revenue resulting from the intended rescinding of the increase in petrol tax. No decision has yet been made as to whether it will be offset by alternative increases in taxation.

² 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.

TABLE 2
Demand for and supply of goods and services

United Kingdom	1974 ²	1975 ²			1976 ²			1977 ³		
	At current prices £ mio	% change on preceding year								
		Vol.	Price	Value	Vol.	Price	Value	Vol.	Price	Value
Private consumption	51 811	- 1.0	+23.4	+22.2	+ 0.2	+15.2	+15.5	- 1.1	+15.0	+13.7
Public consumption	16 637	+ 4.5	+31.4	+37.3	+ 2.8	+12.2	+15.4	- 0.4	+10.8	+10.4
Gross fixed asset formation	16 690	- 1.3	+24.5	+22.9	- 4.3	+17.4	+12.4	- 3.4	+11.5	+ 7.7
— Enterprises	10 662	- 0.2	+25.6	+25.3	- 3.7	+19.7	+15.3	:	:	:
— Dwellings	3 149	+ 6.8	+19.6	+27.7	- 0.3	+14.8	+14.5	:	:	:
— General Government	2 879	- 8.1	+18.4	+ 8.8	-14.5	+13.8	- 2.7	:	:	:
Domestic final uses (excluding change in stocks)	85 138	0.0	+25.3	+25.3	- 0.1	+15.0	+14.9	- 1.4	+13.4	+11.9
Domestic final uses (including change in stocks)	86 285	- 2.3	+25.0	+22.1	+ 1.1	+15.0	+16.3	- 1.2	+13.4	+12.1
Exports ¹	22 963	- 4.0	+21.3	+16.5	+ 6.6	+21.5	+29.3	+ 7.4	+15.3	+23.8
Imports ¹	27 270	- 6.5	+13.2	+ 5.8	+ 4.0	+21.0	+25.9	+ 0.2	+17.4	+17.7
Gross domestic product at market prices	81 978	- 1.7	+28.2	+26.0	+ 1.8	+15.0	+17.1	+ 0.8	+12.8	+13.7
		Contribution to % change in gross domestic product								
Domestic final uses (excluding change in stocks)	85 138	0.0	—	+26.3	- 0.1	—	+15.3	- 1.4	—	+12.0
Change in stocks	+ 1 147	- 2.0	—	- 3.0	+ 1.3	—	+ 1.3	+ 0.2	—	+ 0.2
Balance of exports and imports ¹	- 4 307	+ 0.3	—	+ 2.7	+ 0.6	—	+ 0.5	+ 2.1	—	+ 1.5

¹ Goods and services.

² Source: Central Statistical Office

³ Estimates of Commission's Departments
No data available.

1976 and the first quarter of 1977. For the first half of 1977, total domestic demand (excluding stocks) will have fallen, largely because of a drop of almost 2% in the volume of *private consumption*.

In contrast, the volume of *exports* of goods will have advanced strongly in the first half of 1977, by about 4%, whereas the volume of imports has changed very little. These movements, together with little change in the terms of trade and a large and growing surplus on the invisibles account, point to a deficit on *current account* of about £200 million in the first half of the year, as against a deficit of £ 950 million during the last six months of 1976.

North Sea oil will make a major contribution to the current account of the *balance of payments* in 1977. Output could well reach 45 million tons (compared with 12 million tons in 1976) with an estimated value of about £2 500 million. If account is taken of imports of capital equipment related to the oil operations (which are expected to fall slightly from 1976 levels), as well as of oil-related debits on the invisibles account, the net contribution of North Sea oil to the current account of the balance of payments could be in the region of £1 500 million, as against an estimated negative effect of £250 million in 1976.

Although the fall in private manufacturing investment has now ceased — indeed between the second half of 1976 and the first half of 1977 a very modest increase may have occurred — *gross domestic capital formation* as a whole will have shown a decline because of the falls in public sector investment and a considerable reduction in investment in private sector dwellings.

Industrial production has apparently shown only modest growth in the first six months of 1977 compared with the previous half year. Indeed the output index covering all production industries increased only by 0.1% in the period January to March 1977, compared with the previous three months, whereas the manufacturing output index rose by nearly 1%. Although a decline in

*unemployment*¹ in the early months of the year was recorded, partly because of employment support measures, a sharp rise occurred in June to 1 350 thousand, the equivalent of 5.7% of the labour force.

The underlying rate of *inflation* has increased;² indeed, when measured on the basis of the index of retail prices which excludes seasonal food items, annual rates close to 20% were recorded during the second quarter of the year. The main factors behind this deterioration are the delayed effects of the depreciation of sterling in 1976 and the direct effects of specific fiscal measures taken by the Government including increases in indirect taxation and the phasing-out of certain subsidies to nationalized industries.

The growth of average earnings (at an estimated annual rate of just below 10% for the twelve months since August 1976) has been somewhat faster than the terms of the present stage II incomes policy originally implied. *Real personal disposable income*, however, has been severely squeezed because of the much higher rate of price inflation.

As a result of the improvement in confidence in sterling since the end of 1976, the *foreign exchange markets* were marked, in the first four months of 1977, by substantial inward capital movements which, given the Government's policy of holding the exchange rate stable, led to a massive increase in the foreign exchange reserves. These reached a level of \$ 9 900 million at the end of May, compared with \$ 4.1 billion at end-1976. These inward capital movements do not appear to have been maintained through the second quarter of the year.

As a result of the Government's tight monetary policy, the *money stock* as broadly defined (sterling M3), which had been rising very rapidly in the autumn of 1976, fell

¹ Wholly unemployed — excluding school leavers and adult students.

² Based on the change over a six-month period, expressed as an annual rate

TABLE 3
The Central Government Budget

United Kingdom	1976-1977			1977-1978	
	Budget forecast		Provisional outturn	Budget forecast	
	£ mo	% change ¹	£ mo	£ mo	% change ¹
Expenditure	54 544	+ 24.9	50 525	56 916	+ 4.3
of which:					
— current expenditure	45 817	+ 20.8	45 107	50 776	+ 10.8
— capital expenditure	8 727	+ 50.9	5 418	6 125	- 29.8
Revenue	44 118	+ 23.1	44 695	50 057	+ 13.5
of which:					
— direct taxes	19 543	+ 21.6	19 556	20 480	+ 4.8
— indirect taxes	11 955	+ 14.0	12 507	16 018	+ 34.0
Net borrowing requirement	10 426	+ 33.2	5 830	6 859	- 34.2

¹ On previous year's Budget forecast

Note. The figures in this table are based on the national budgets

during the opening months of the year to the extent that the growth of sterling M3 in the financial year 1976/77 (about 7½%) was below the target growth range (9-13%) announced at the time of the December measures. Since April, bank lending to the public and private sectors has increased markedly causing sterling M3 to expand significantly. The strong downward pressure on interest rates has been reflected in the movements of the minimum lending rate, which has been reduced fifteen times since last October from 15% to 8% in May.

3. Outlook

Assuming that the current discussions within the TUC and the Government lead to an agreement on incomes policy that does not cause any dramatic change in the rate of increase of average earnings during the second half of 1977, there is likely to be a relatively marked recovery in domestic demand. This recovery will be based on a resumption of growth in private consumption (largely offsetting the decline in the first half of the year) as the squeeze on disposable income comes to an end, helped by the tax rebates announced in the March Budget which are assumed to be granted in full. The decline in fixed capital formation should cease and some modest rebuilding of stocks could well occur.

On the external side, the steady growth in exports of manufactured goods should continue and further increases in North Sea oil production should help to improve the overall balance of trade. For the second half of the year, a current account surplus of about £500 million is foreseen.

The increase in the level of GDP between the two years will be of the order of one per cent. Unemployment is likely to increase in the second half of the year.

The present outlook is for a marked fall in the rate of retail price inflation in the second half of the year to about 11% (at an annual rate).

Present forecasts for the PSBR for 1977/78 point to an outturn within the figure indicated in the Letter of Intent to the IMF, without increasing the tax pressure significantly. However, the outlook for a new round of incomes policy is by no means clear and any reflationary moves should be on the cautious side and should take into account the continuing need to give priority to reducing the rate of inflation.

Major economic policy measures

— On 3 January, the International Monetary Fund (IMF) approved the United Kingdom's application for a loan of SDR 3.36 billion.

— At a meeting in Basle, on 10 January, the Bank for International Settlements, backed by the central banks of Austria, Belgium, Canada, Denmark, the Federal Republic of Germany, Japan, the Netherlands, Norway, Sweden, Switzerland and the United States, agreed to make available to the Bank of England a medium-term credit facility of \$3 billion as a "safety net" against withdrawals of official sterling balances. The availability of the credit depends on Britain's adherence to the conditions in the UK's Letter of Intent of 15 December 1976 to the IMF. In addition, the United Kingdom will offer official holders of sterling the possibility of investing in foreign currency bonds.

— Also on 10 January, the United Kingdom drew the first tranche, of the equivalent of SDR 1 000 million, of the IMF loan.

— On 13 January the Bank of England released about £1.1 billion of special deposits, in order to overcome the exceptional shortage of funds in the London money markets.

— On 24 January, the Chancellor of the Exchequer announced that the Bank of England had negotiated a new loan of \$1 500 million from the Euromarket for a period of seven years.

— On 27 January, the Bank of England released a further £360 million of special deposits as a temporary aid to liquidity.

February:

— In a move designed to re-assert its control over the level of short-term interest rates, the Bank of England announced, on 3 February, that it was abandoning, *pro tem*, the normal market-related formula for determining the minimum lending rate. This followed a period in which the rate had fallen faster than was considered appropriate to the situation (i.e. from 14% on 7 January to 12¼% on 29 January).

— The \$3 000 million standby credit arranged on 10 January with the Bank for International Settlements came into operation on 8 February.

March:

— On 3 March, measures to alleviate unemployment amongst young people were announced, including:

— an extension until 31 August 1977 of the Youth Employment Subsidy, the Work Experience Programme and the Job Creation Programme expected to provide, in total, an additional 41 500 places;

— a proposal to extend training courses for young people under the Training Opportunities Scheme by 5 000 places to a total of 17 000.

— On 11 March, the Bank of England reactivated the market-related formula for determining the minimum lending rate but reserved the right, exceptionally, either not to change the rate or to change it by less than would result from the operation of the formula.

— On 18 March, the Bank of England allowed the minimum lending rate to fall by ½ per cent to 10½% and introduced measures designed to slow the decline in interest rates and to discourage inflows of foreign "hot" money. The measures were:

— an issue of Government stock of £800 million; payment for the new issue to be in instalments to avoid excessively depressing the money supply;

— the removal of tax exemption for foreign holders of the new stock and future issues.

— On 29 March, the Chancellor of the Exchequer presented his Budget proposals for the fiscal year 1977/78.

Compared with the previous financial year, and taking account of the tax reductions conditional on a satisfactory wage increase figure, the rise of total central government receipts in 1977/78 was forecast to be 13.5% compared with 4.3% for expenditure. The public sector borrowing requirement (covering general government and public corporations) was estimated to be £8 471 million compared with an estimated outturn for 1976/77 of £8 820 million.

The measures included:

— reductions in direct personal taxation of £1 300 million in a full year by means of raising tax thresholds, increasing tax-free personal allowances and introducing tax relief for employees working abroad. The Chancellor also proposed a reduction in the basic rate of income tax from 35% to 33% (costing £960 million in a full year) but conditional on a satisfactory agreement on pay policy for the twelve months from August 1977;

— corporation tax rates to remain unchanged but the profit limit below which a preferential rate of 42% is payable was raised from £30 000 to £40 000. The interim scheme of relief for stock appreciation is to continue for two more years.

— changes in indirect taxation (yielding £810 million in a full year) including increases in the price of cigarettes, petrol and heavy oil and in the annual excise duty for private cars and commercial vehicles;

— the Temporary Employment Subsidy to be extended until 31 March 1978 and be payable for eighteen months instead of twelve months;

— a new Small Firms Employment Subsidy is to be introduced and will be payable for each new employee taken on by small firms in special development areas;

— a short-term subsidy is to be paid to employers taking on a disabled person;

— a special programme to be started to train extra teachers of mathematics and science;

— £100 million to be made available over the next two years for construction work in certain inner areas of cities

TABLE 4

Main economic indicators

	Year	Jan	Feb.	Mar	Apr	May	June	July	Aug.	Sept	Oct	Nov.	Dec
Industrial production (1970 = 100)	1975	105.5	105.0	103.3	101.5	99.8	99.7	100.0	98.4	100.3	100.6	100.7	99.8
	1976	101.2	102.5	102.0	102.3	104.4	100.4	101.4	100.6	102.4	102.8	103.5	103.3
	1977	103.4	103.3	103.1	103.2								
Unemployment (000)	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	1 352.8						
Construction Housing starts (000)	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	18.8
	1977	21.4	16.8	20.9									
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	282.8								
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								
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							
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	349.8	348.1							
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	259.6							
Exports (million EUA)	1975	2 912	2 733	2 806	2 915	3 147	2 759	3 123	2 433	2 867	3 450	2 924	3 280
	1976	3 106	3 109	3 892	3 370	3 387	3 692	3 435	3 187	3 443	3 408	3 682	3 781
	1977	3 573	3 648	4 490	3 919	4 513							
Imports (million EUA)	1975	4062	3 466	3 234	3 750	3 343	3 422	3 852	3 321	3 515	4 032	3 487	3 567
	1976	3 726	3 742	4 395	4 226	4 019	4 530	4 436	3 848	4 296	4 177	4 602	4 347
	1977	4 539	4 138	5 091	4 455	5 032							
Balance of trade (million EUA)	1975	-1 151	- 733	- 427	- 835	- 196	- 663	- 728	- 888	- 648	- 582	- 563	- 378
	1976	- 620	- 633	- 504	- 856	- 632	- 838	- 1 001	- 662	- 853	- 769	- 919	- 565
	1977	- 960	- 489	- 602	- 537	- 519							
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	80.5	80.0	80.3	79.8	81.0	80.7	79.6	78.7	79.6
	1977	81.4	80.8	80.4	79.7	78.1							
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	61.3						
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							
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	28 782	29 011							

Not available

Seasonally adjusted unless otherwise stated

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 (all industries) (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 payment 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 (c + g).

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

April:

- On 4 April, the Chancellor announced the terms of the foreign currency bonds, agreed at Basle on 10 January, which will be available to official holders of sterling.
- Also on 4 April, the Prices Secretary published a new Price Commission Bill giving details of proposed legislation for controlling prices. Under the new legislation, the Price Commission will have wider investigative powers and the authority to refuse price increases even when companies face higher costs.
- On 22 April, controls were introduced on imports of stainless steel from Spain and clothing and textiles from India.
- At a meeting on 26 April the Agriculture Ministers agreed a rise in common EEC farm prices of 3½%. The United Kingdom is to devalue the Green Pound by 2.9% as from 1 May.

May:

- On 4 May, it was announced that, with effect from 5 August, the Government would withdraw the petrol price increase of 5½ pence per gallon introduced at the time of the Budget.
- On 13 May, the Bank of England announced that the 'corset controls', imposed on 18 November to restrict the growth of interest bearing eligible liabilities, would continue for a further six months.
- On 24 May, the Secretary of State for Price and Consumer Protection accepted an amendment to the Price Commission Bill which will limit the Commission's powers to control company profit margins and dividend payments to one year from 1 August 1977.
- On 27 May, a variable interest rate Government bond was issued, with the rate of interest linked to the yield on Treasury Bills.

Trends in industrial labour costs

After increasing momentum between 1972 and 1975, the upward movement of labour costs¹ slackened in 1976 in all Community countries. Indeed, costs actually declined in the Federal Republic of Germany, as in the United States. The upturn in production and the slower rate of growth of wages and salaries are the main reasons for the change.

The calculation in national currencies gives a slowdown varying appreciably in intensity from one country to the next. As in 1975, labour costs rose most sharply in Ireland (6%), in Italy (11½%) and above all in the United Kingdom (14%). Elsewhere the rise was a good deal slower, ranging between 1.5% and 4.8%. In the Federal Republic of Germany, where the increase had been the slowest in the Community over the two preceding years, costs fell by about 2% in 1976. There was also a slight fall in the United States, where the increase had been fairly sharp in 1974 and 1975.

For the 1970-76 period (see Table 1), there were marked divergences between Member States. The rate of increase was roughly three times higher in Ireland, Italy and the United Kingdom (between 112% and 137½%) than the lowest rate recorded — 38½% in the Federal Republic of Germany. Increases in the other countries ranged from 56% to 75½%. In the period from 1973 to 1976, the rate of growth accelerated in all countries, with the exception of the Federal Republic of Germany, compared with the preceding three-year period, and the divergences between countries also became more acute. This was mainly because of the recession, during which wage costs had increased sharply under the joint impact of a very vigorous upsurge in the gross compensation of employees

and the slowdown in production; the increase had been accentuated in several countries by the effect of legal requirements governing redundancies. In addition in the Federal Republic of Germany, the cumulative variation between 1973 and 1976 shows a relatively smaller increase than in other countries, as well as a fall in labour costs in 1976.

In 1976, gross value added at constant prices in industry began to rise again at an appreciable pace in all Community countries except the United Kingdom. With many firms running well below capacity, the upturn generated an appreciable increase in productivity per person employed. Except for the United Kingdom, the increase in gross value added per person employed varied between 80% (Denmark, Netherlands) and 11% (Italy), whereas in 1975 there had been an almost general fall, in most cases ranging between 1% and 2%, but reaching some 9% in Italy. The number of wage and salary earners continued to fall in 1976 in the Federal Republic of Germany, France and Italy (by about 1½% in all three countries); this fall was more marked in Ireland, the United Kingdom (2½% in both cases), the Netherlands (3%) and Belgium (4%); in Denmark, however, employment increased slightly. In the United States, on the other hand, the upturn brought substantial increases in productivity — gross value added per person employed increased by 8½% compared with 1½% in 1975 — and a 2½% increase in employment, which fell by 8½% in 1975.

¹ Labour costs per unit of gross value added in industry, including construction.

TABLE 1
Labour costs in industry per unit of gross value added at constant prices
(Including construction)

Countries	Percentage change on preceding year						1970-1976 Cumulative change	
	In national currency			In dollars ¹			In national currency	In dollars ¹
	1974	1975	1976	1974	1975	1976		
Denmark	17.7	16.4	3.7	16.8	23.5	— 1.4	75.5	117.7
FR of Germany	8.0	7.8	— 2	11.5	13.4	— 4.6	38.5	100.5
France	15.7	16.9	4.3	7.3	31.0	— 6.5	75.6	104.0
Ireland	18.9	25.8	6	13.7	19.1	— 13.2	112.2	59.9
Italy	20.3	32.3	11.5	7.9	31.8	— 12.0	137.5	79.5
Netherlands	11.2	14.2	2.5	15.6	21.3	— 1.9	56	113.6
Belgium	16.2	13.9	1.5	16.3	20.7	— 4.0	59	104.3
United Kingdom	23.5	33.7	14	18.0	26.5	— 7.5	136	76.7
United States	15.0	9.3	— 1	15.0	9.3	— 1	34	34

¹ Calculated on the basis of figures in national currencies adjusted for exchange rate changes in relation to the dollar.

Source: Departments of the Commission

The growth of gross compensation per employee, which had slackened in 1975, again slackened fairly appreciably in 1976, except in the Federal Republic of Germany. Nevertheless, the latter country again recorded the lowest rise (8% as in 1975). The rise was again sharpest in Italy (23½%), Ireland (19½%) and the United Kingdom (approximately 18½%); in the last two countries, however, there was a marked slowdown compared with 1975, when the increase had been 27½% and 32½% respectively. In Italy, on the other hand, the rate of growth was rather higher than the rate of approximately 21% recorded in 1975. In the other countries, the rise in compensation per employee varied between 11% in the Netherlands and Belgium and 14½% in France, whereas in 1975 it had ranged from 12% to 15½% in the same countries. All in all, the divergences in trend between Member States have narrowed somewhat, but remain excessive. In the United States, where the rise had been about 11% in 1975, compensation per employee only increased by about 7½% in 1976.

Changes in exchange rates have brought trends in the various Member States closer together. These series, be they adjusted for exchange rate variations in relation to the Eur or the dollar or adjusted for changes in effective exchange rates (see Table 2), show, for countries which between 1970 and 1976 had the sharpest growth of unit wage costs calculated in national currency, a marked deceleration owing to the depreciation of their currencies. For countries whose currencies have tended to appreciate, on the other hand, the figures show a sharper cumulative increase in unit costs. This increase has been slowest in the Federal Republic of Germany — despite the fact that its currency has appreciated most — and in Italy; the rate of increase in these two countries is similar to that in the United States. In the other Member States, the figures show substantial rates of increase, which do not differ widely from country to country. Of all the Community countries, the cumulative rise has been sharpest in Denmark, owing to the appreciation of its currency.

TABLE 2
Cumulative change in industrial labour costs (including construction) —
adjusted for variations in exchange rates

Countries	1971-1973 (Cumulative change)				1974-1976 (Cumulative change)			
	In national currency	In dollars ¹	In Eur ²	Effective exchange rates ³	In national currency	In dollars ¹	In Eur ²	Effective exchange rates ³
Denmark	23.4	53.1	22.2	30.1	42.2	42.2	40.9	51.4
FR of Germany	21.4	66.3	35.5	43.3	14.1	20.6	16.6	30.4
France	24.6	55.4	24.6	29.4	40.9	31.3	29.2	39.6
Ireland	33.5	36.1	8.8	21.2	59.0	17.5	15.1	31.5
Italy	33.7	43.4	14.6	18.4	77.6	25.2	23.1	27.9
Netherlands	19.8	55.2	24.8	28.1	30.2	37.6	34.9	44.8
Belgium	18.2	51.6	21.5	24.5	34.5	34.8	34.6	42.1
United Kingdom	25.5	28.0	2.3	7.5	88.0	38.0	36.1	42.8
United States	7.4	7.4	- 14.1	- 11.1	24.8	24.8	22.8	33.1

¹ Calculated on the basis of figures in national currencies adjusted for variations in exchange rates against the dollar

² Calculated on the basis of figures in national currencies adjusted for variations in exchange rates against the Eur

³ Calculated on the basis of figures in national currencies adjusted on the basis of exchange rates weighted in accordance with the external trade of the different countries in 1974
Source: Departments of the Commission.

Notes on methods

The definitions and methods of calculation used are as follows:

Compensation per employee covers wages, salaries and social security contributions. However, no breakdown of the compensation of employees as defined above by economic sector is as yet available for Belgium; in this case, therefore, the index provided by the Banque nationale de Belgique for average gross earnings per hour worked has been used, corrected in aggregate by the index of hours worked.

The series for *gross value added* are calculated in market prices. However, as Ireland publishes no market-price

figures for gross value added at constant prices, broken down by economic sector, data available at factor cost have been used for this country. For the calculation of gross value added at constant prices, 1970 has been used as reference year. Although it would have been preferable to take as base changes in gross compensation of employees and gross value added at constant prices per hour worked, this proved impossible because the statistics on the number of hours worked in the Community countries are not complete. Consequently, these two items could only be calculated per employee.

Labour costs per unit of gross value added at constant prices have been calculated by dividing the index for gross

compensation of employees by gross value added at constant prices. These figures can also be obtained by dividing per capita compensation of employees by gross value added per person employed.

The Annex gives figures showing *labour costs adjusted for changes in exchange rates*. Until 1971, these were calculated to the International Monetary Fund. From 1971 onwards, the data were converted into dollars on the basis of market rates; the conversion into Eur carried out according to a method established by EUROSTAT has been maintained this year prior to the more general use of the EUA (European unit of account — for definition see EUROSTAT Monthly General Statistics Bulletin n° 3-1977, table 753-annex.

The *implicit price index* is obtained by dividing gross value added at current prices by gross value added at constant prices.

The figures for 1976 are based wholly or partly on estimates.

As to the *significance of the series* used, the following comments will be helpful:

The statistics have, as far as possible, been drawn from the publication 'National Accounts ESA (1970-1975)' of the Statistical Office of the European Communities. However, comparability is established only in respect of changes in the indices within each country.

Use of national accounts has meant that only annual figures could be referred to. Changes in the course of the year are reflected only in part in the corresponding annual

figures and also influence the results for the following year. This makes assessment of a short-term change particularly difficult.

As for wage- and salary-earners in industry, in the case of Ireland the results of annual surveys on paid employment by sector have been used.

The notion of *value added* differs from that of 'industrial production' as generally applied in calculating monthly indices of industrial production.

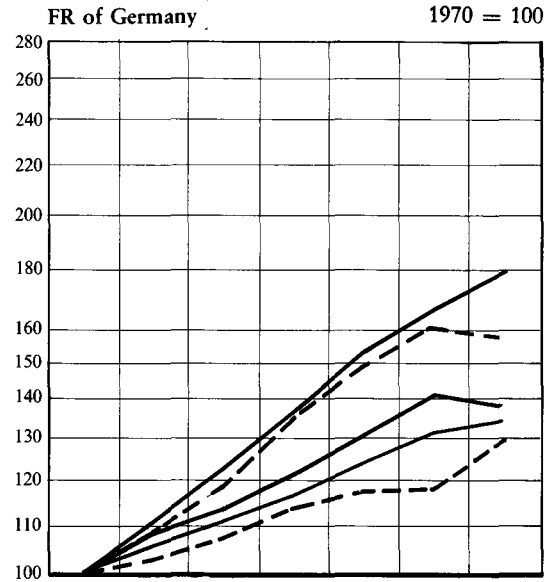
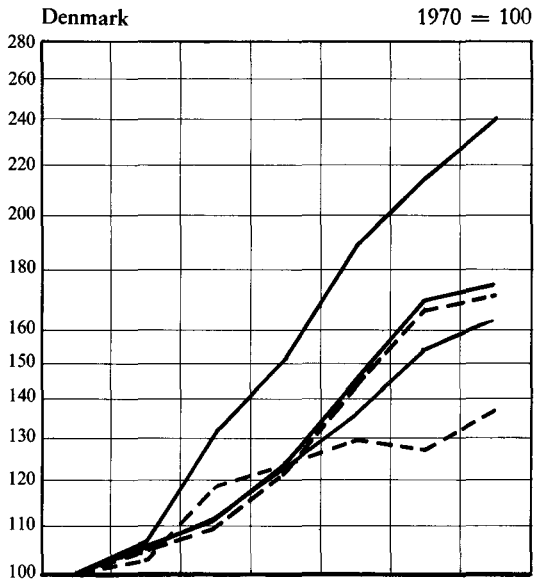
The difference between value added and industrial production (as defined for production indices) appears most clearly in the *implicit price index for gross value added*. In respect of effective market prices, this index neglects two important factors, namely firm-to-firm supplies within an industry and supplies from other industries, including abroad. The implicit price index is therefore not in line with market price index; the discrepancy varies from one country to another as a function of the relative share of value added in the gross production of industry.

The concept of *compensation of employees in industry* does not cover all wages included in deliveries of industry at market prices: it does not cover wages included in the value of goods and services supplied to industry by other sectors of the domestic economy.

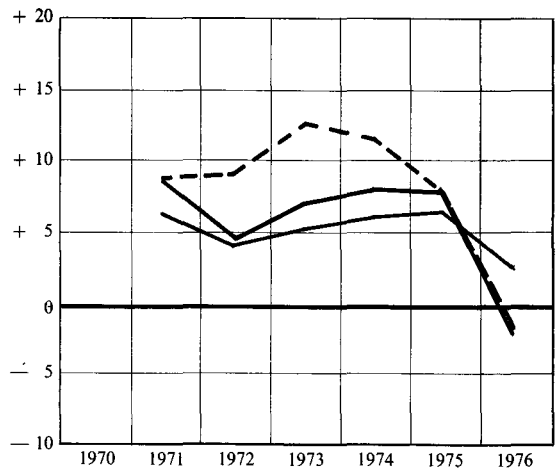
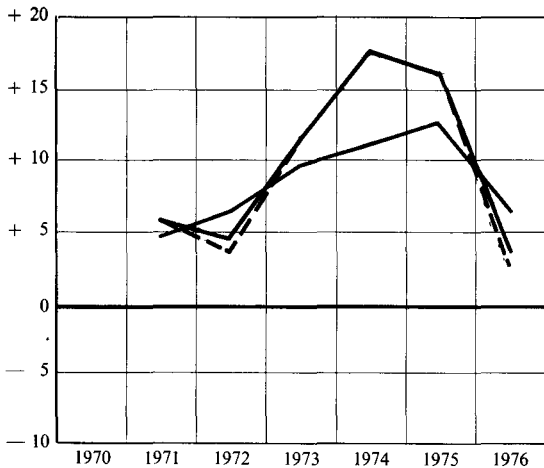
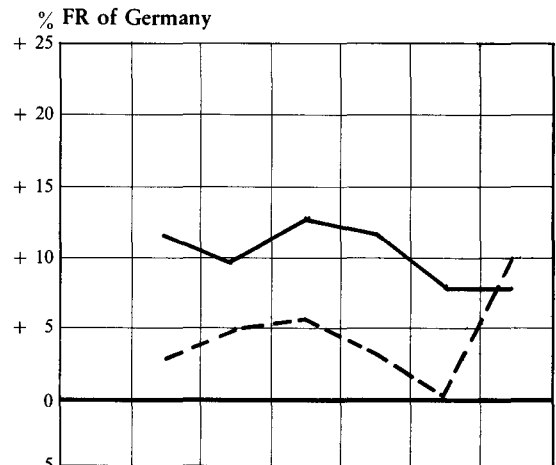
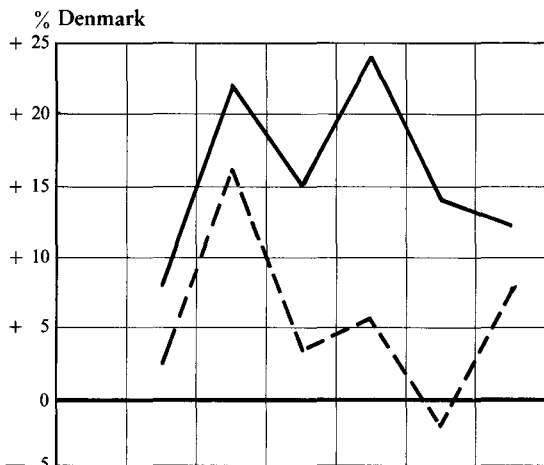
These remarks show that the series which follow must be used cautiously. They are not automatically comparable from country to country, and their development in time is different from that of series the data of which are based not on value added but on gross output.

Graphs

LABOUR COSTS IN INDUSTRY

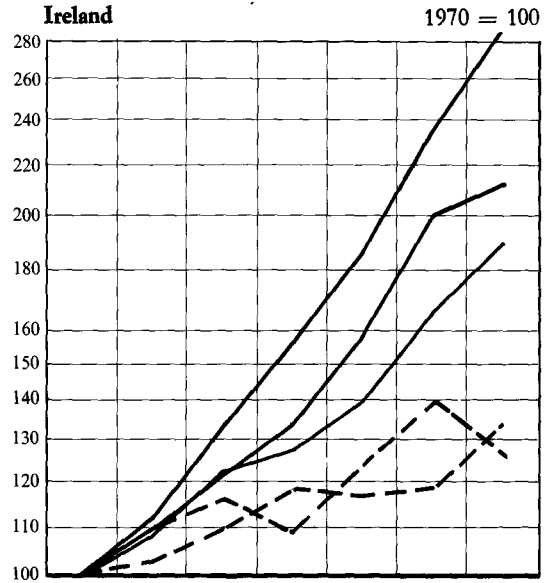
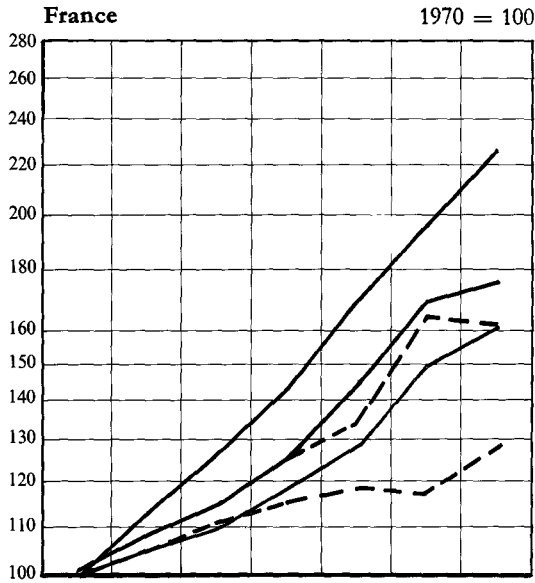


% change on preceding year

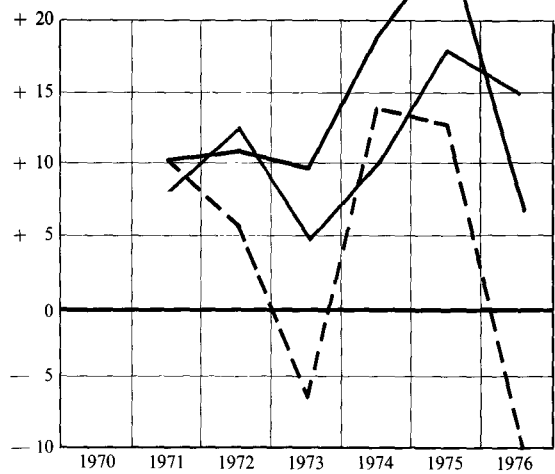
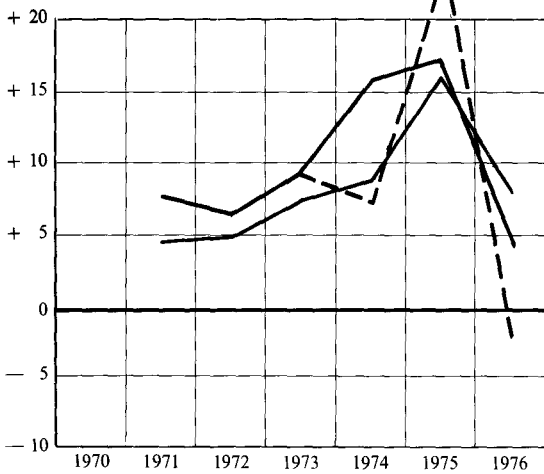
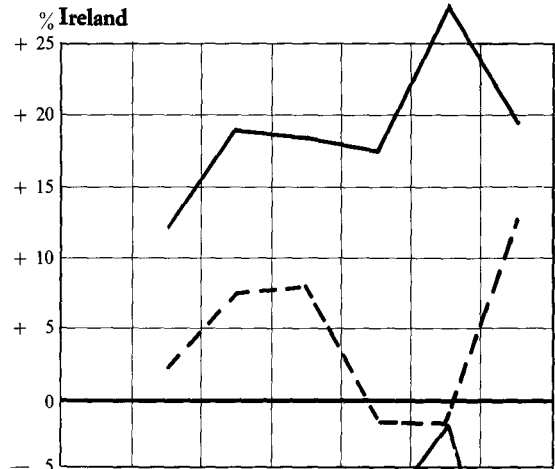
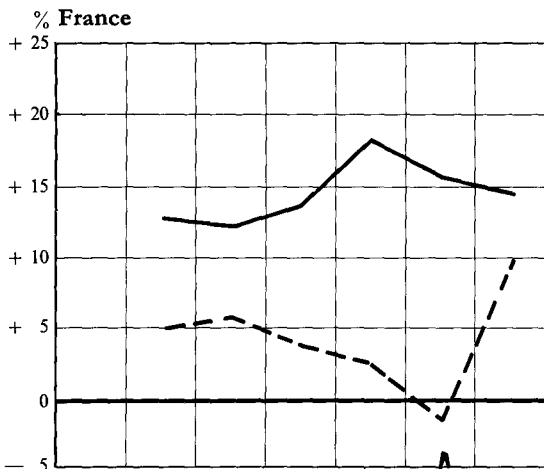


- *Income from employment per head*
- - - - - *Gross value added (at constant prices) per employee*
- *Labour costs per unit of gross value added (at constant prices)*
- - - - - *Labour costs per unit of gross value added (at constant prices) corrected to account for changes in exchange rates in relation to Eur*
- *Implicit price index of gross value added*

LABOUR COSTS IN INDUSTRY

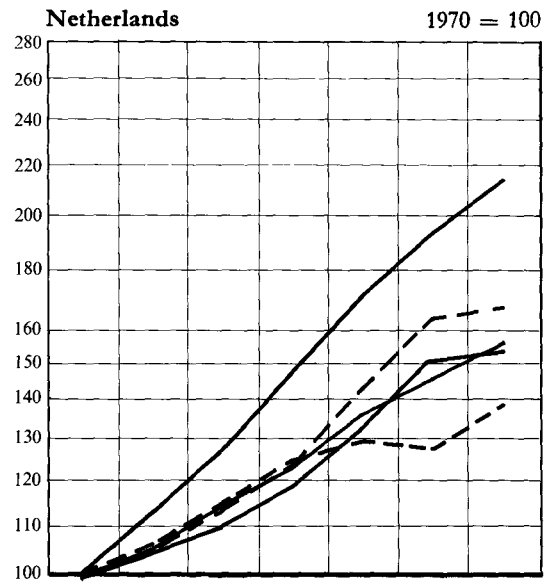
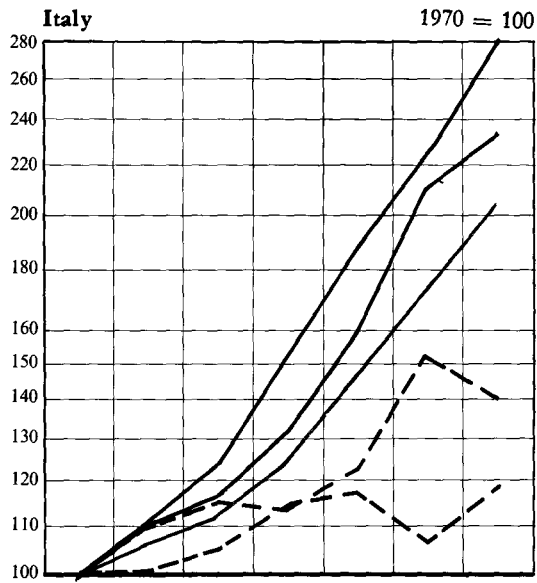


% change on preceding year

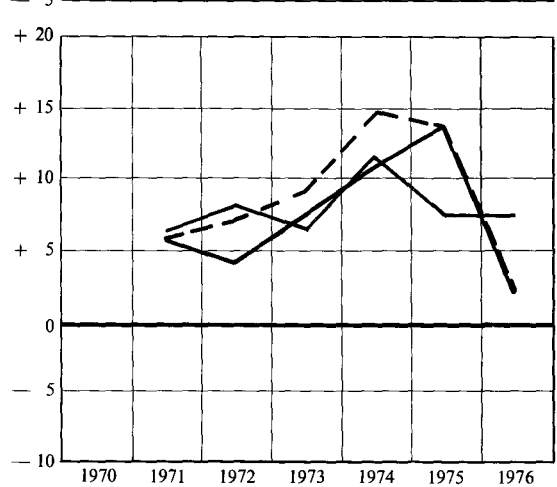
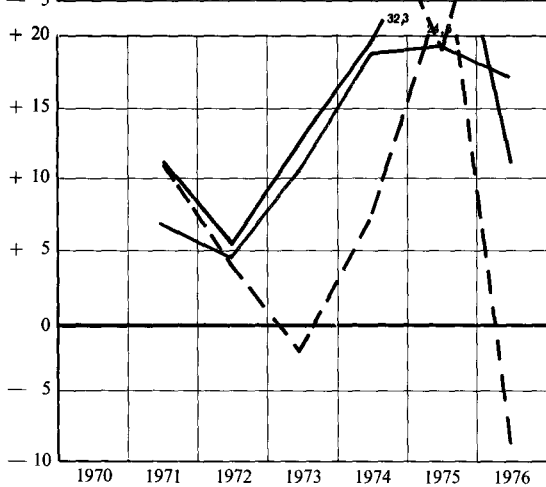
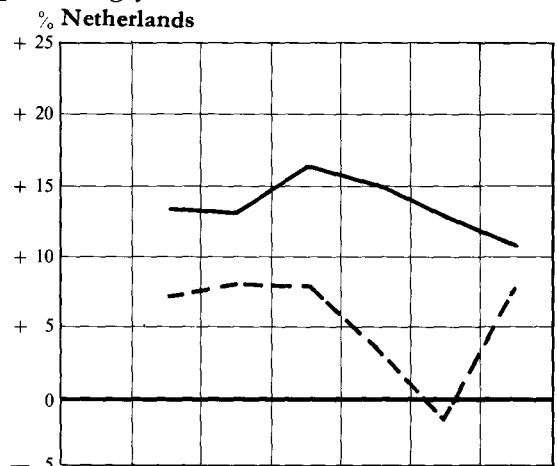
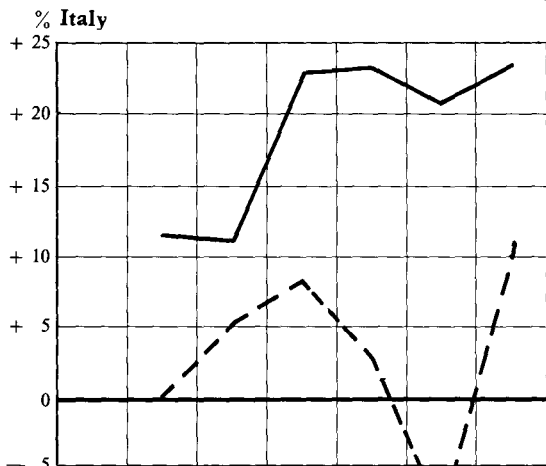


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LABOUR COSTS IN INDUSTRY

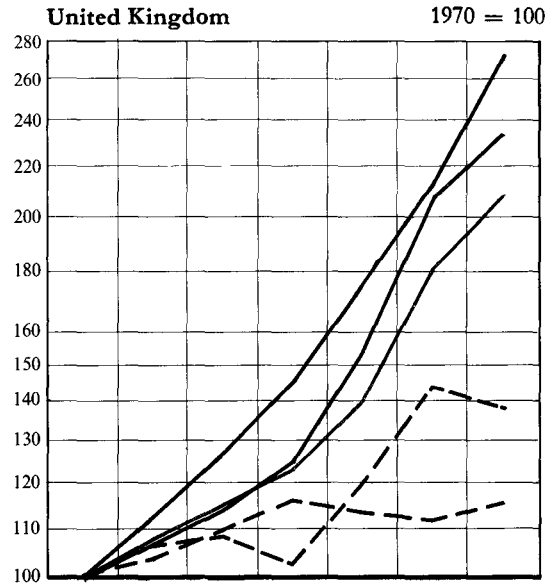
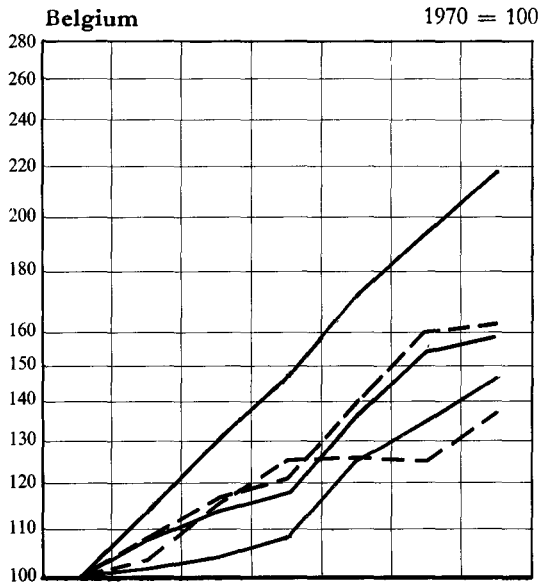


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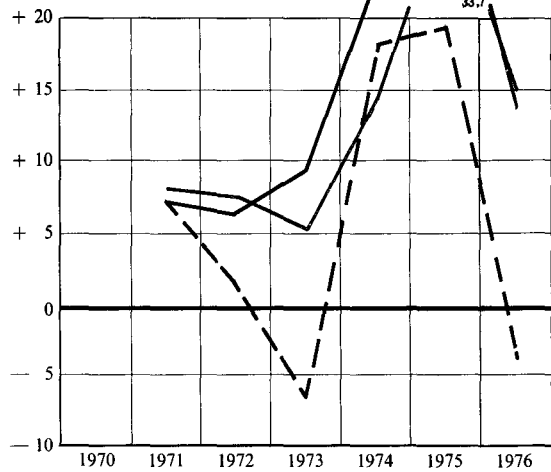
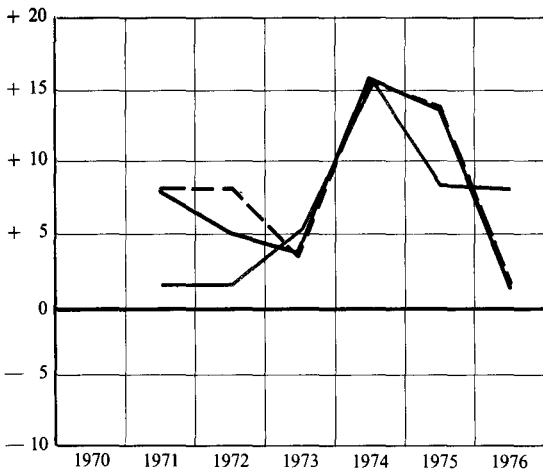
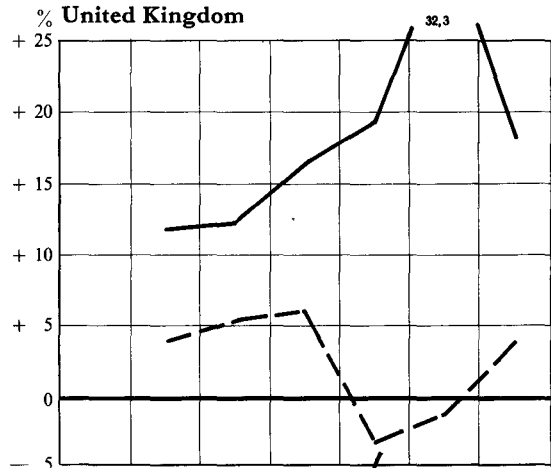
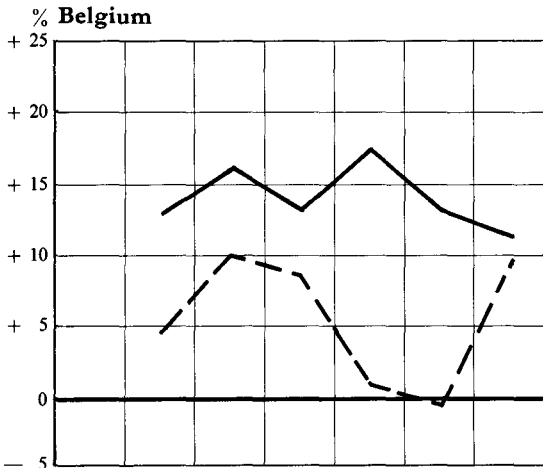


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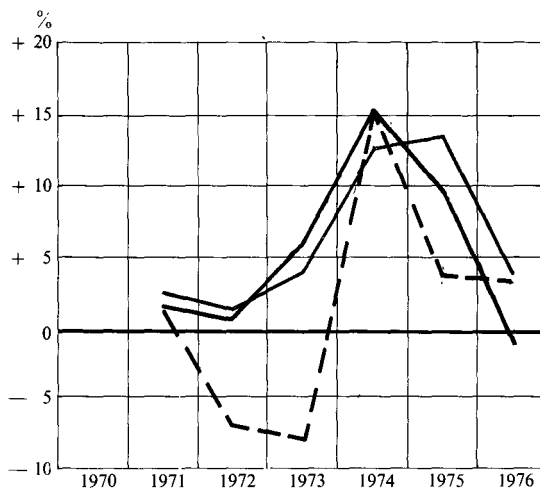
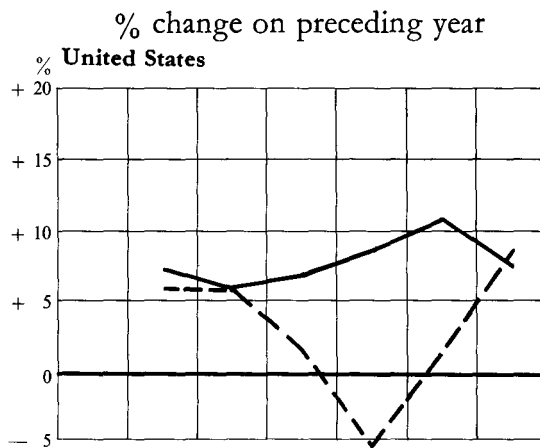
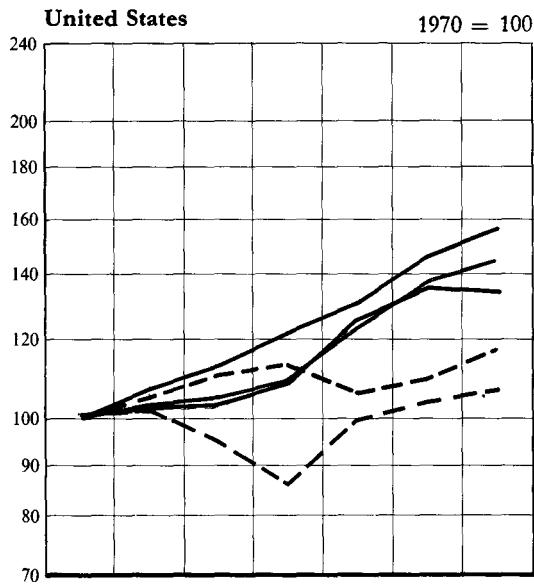


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