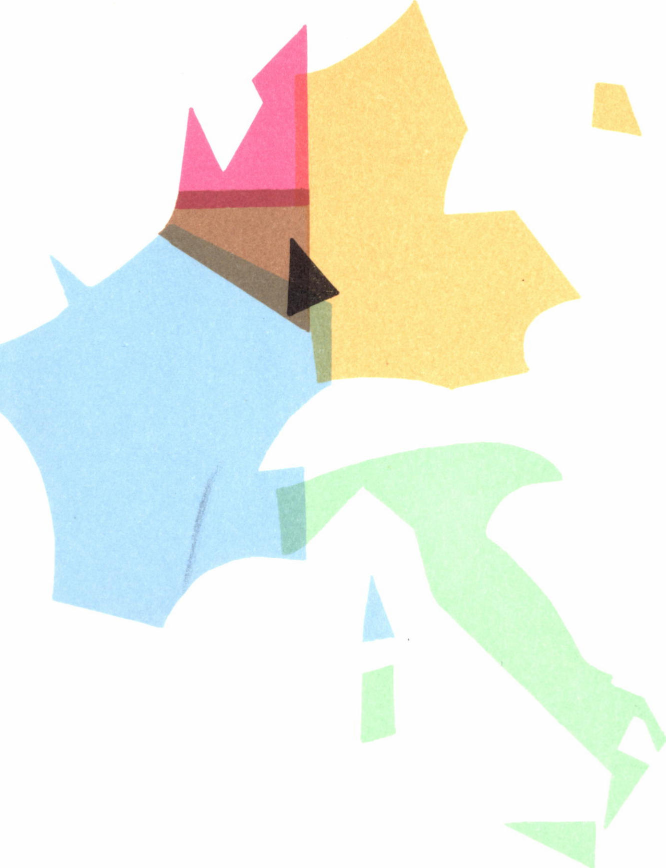

European Communities

Commission

Directorate-General for Economic and Financial Affairs

The economic situation in the Community

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1970

Quarterly survey

Commission of the European Communities
Directorate-General for Economic and Financial Affairs
Directorate for National Economies and Economic Trends
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EUROPEAN COMMUNITIES

COMMISSION

The Economic Situation in the Community

MARCH 1970

Contents

Note :
This survey was completed around mid-March 1970. As regards the most recent developments and where it has not been possible to take them into account because of the pace at which national statistics are prepared and the time it takes to publish the Survey in five languages, the latest issue of the "Graphs and Notes on the Economic Situation in the Community" can usefully complete the information supplied here.

I. THE OVERALL SITUATION

Around the turn of the year business was decidedly booming in the Community. At the end of 1969 and the beginning of 1970, the very rapid rise in aggregate demand did, it is true, slow down a little as demand from major non-member countries slackened and the expansion of private consumption weakened temporarily, but the relationship between supply and demand was still under the severe strain caused by the appreciably slower pace at which production has been advancing. This in turn was due to the unusually high degree of technical capacity utilization and the very acute labour shortage, to bad weather and to industrial disputes—the latter being particularly sharp in Italy. Seasonally adjusted, the level of unemployment was very low.

The imbalance on the markets for goods and services and the increase in internal and external costs led to an appreciable rise in the level of prices. The Community's balance of trade with non-member countries has been deteriorating since October 1969; at the same time, the capital account has been showing heavy deficits, due mainly to massive outflows of money and capital from Germany following the revaluation of the German mark; official gross gold and foreign exchange reserves have therefore dropped sharply.

The outlook for the remainder of 1970 is still much as set out in Quarterly Survey 3/4-1969. The growth of external demand is likely to slacken further as the world business climate continues to cool down. Internal demand by contrast may—especially in the first half of the year—expand somewhat more vigorously than had previously been expected. Private consumers' expenditure in particular should rise very appreciably, and investment activity can be expected to remain at a high level. For the time being, then, the expansion of demand will on the whole *appreciably outstrip the possibilities for an increase in production, but in the second half of the year the gap between supply and demand may narrow.*

Given this outlook, the growth of real gross Community product from 1969 to 1970 is at 5 ½% likely to be higher than had been assumed in the last Quarterly Survey. Imports from non-member countries will at the same time be soaring. With exports expected to rise only modestly, the deficit on the Community's balance of trade will probably grow appreciably, despite an improvement in the terms of trade. There is all the more reason to fear a persistence of the upward thrust of prices as in 1970 the rise in cost per unit of output may tend, if anything, to gather additional momentum in most member countries.

A. The economic situation: problems and short-term policy

As the following analysis of the economic trends in the Community will show, the business situation is today characterized by the persistence of heavy inflationary strains. Although the expansion of domestic demand has slowed down somewhat in certain countries, this is mainly attributable to special factors, and in many industries it may well be that the coming months will see still heavier calls being made on capacity. Given the already very high degree of utilization of the factors of production in the Community and the resultant slowing of output, the gap between supply and demand has in general not narrowed but, in some countries, even widened.

A particularly worrying element in the present situation is the increasingly steep climb in unit costs caused by the slowdown in productivity gains and the faster rise in wages. This rise in costs is at present occurring against a background of very heavy strains in the business situation; should it continue to do so, the upward thrust of prices, already considerable, could gain further momentum and subsequently continue at a rapid pace even if the trend of demand calms down quite substantially.

With the backlog of orders still very considerable, the tendency observed in various countries and industries for the flow of new orders to flatten out will not lead to a rapid reduction in the margin of excess demand, and consequently of the inflationary pressures, unless it continues over a fairly long period and broadens further.

At present it is mainly the relative weakness of actual exports from the Community to non-member countries that contributes to an easing of pressures in the Community. With imports expanding sharply, this weakness has led to deficits on the Community's trade account and consequently to a deterioration in the current account. Since the German mark was revalued, there has in addition been a reversal in capital movements, so that the Community's gold and foreign exchange reserves have fallen very considerably. The external financial position of the Community as a whole has therefore been developing along distinctly less favourable lines.

The effect of the balance-of-payments trend has been to reduce internal liquidity and so to force up the cost of credit. Short-term interest rates have adjusted to the international level even in countries like Germany and Italy, where until a few months ago they had been appreciably lower than elsewhere. The rise in long-term interest rates has at the same time continued and broadened.

In the months ahead there is still little likelihood of the severe strains on the markets for goods and services easing significantly. The restrictive influence of the expected slowdown in exports to non-member countries will certainly gain in strength, and the flow of new orders for plant and machinery may be less dynamic. On the other hand, everything suggests that almost all countries will experience a pronounced consumer boom. This may cause the trend of investment to diverge unduly from that of consumption, and in the longer term could well raise problems for the maintenance of rapid and steady economic growth.

Following a period when economic trends in the member countries were moving along remarkably parallel lines, the situation in the Community has changed in that there are now signs of developments in various countries getting out of line. In France, especially, expansion may be less dynamic than in the other countries, while in Italy the forces of expansion can be expected to gain in strength and strains are likely to mount further, heavy though they already are.

The Commission memorandum of 22 December 1969,[1] whose conclusions the Council adopted at its session of 26 January 1970, stressed the need for rapid action if an early process of disinflation were to be started. Such action should concentrate on the first half of 1970, so as to ensure that in the longer term there is no slowdown of growth accompanied by persistent increases in costs and prices against a precarious international background. Em-

[1] The text of the Commission memorandum to the Council on the Community's short-term economic policy for 1970, dated 22 December 1969, is given in the Annex.

phasis should be placed on instruments to dampen the expansion of internal demand. Endeavours should in particular be made to practise greater austerity in budgetary matters, maintain the restrictive line on credit, stimulate private saving with a view to dampening private consumption and stemming the outflow of capital, and encourage competition on the markets for goods and services.

Given the current outlook, the guidelines of the memorandum remain fully valid. There are indeed many grounds for an even stricter application of the restrictive policy. Several countries might be well advised to make still greater efforts in the budgetary field; for one thing, public finance policy is more suitable than most other economic policy instruments for bringing direct and rapid influence to bear on incomes and consequently on the expansion of internal demand; for another, it may well be that as the year advances the world economic climate and the trend of interest rates on the major money and capital markets will modify the background against which monetary and credit policy operates in the Community countries. Although there is still much uncertainty about this point, the chances are that with the economic climate in the United States cooling down increasingly, demand for bank loans in that country will calm down, entailing a fall in interest rates. This would touch off a corresponding trend on the Euro-currency market, which would presumably spread to the money and credit markets in the Community. From a long-term angle such a development is no doubt to be welcomed, particularly if it is part of a concerted effort; the impact of credit policy, however, would then be less restrictive.

In the circumstances, and given the expected persistence of strains within the Community, budget policy should be primarily counter-cyclical in character. While in France the budget is being handled in a way that appears to fit the business situation, the same may not be true in all other countries. It would seem that handling of the budget should be stricter, particularly in Italy, where the economic situation at home will have to be consolidated rapidly if external economic equilibrium is to be restored and the real purchasing power of personal incomes maintained at as high a level as possible. In the Benelux countries, too, the pressures discernible appear to make it advisable to reduce the stimuli provided by the operation of the budget. Although in Germany the various budgets are already removing a substantial amount of liquidity from the internal money stream, here too it must be asked whether the efforts currently being made in the field of public finance will suffice to restore a reasonable measure of price stability.

In all these countries, then, there will have to be stricter handling of the budget and of the public finances, and more particularly a cut in the rate at which public expenditure is rising. Should these measures, together with the restrictive credit policy and steps to promote saving, prove insufficient to ensure the necessary moderation in the expansion of domestic demand, an additional increase in current revenue, particularly direct taxes, would have to be contemplated. Such an increase would have to be conceived along lines which enable it to be offset comparatively fast through appropriate tax cuts once economic expansion begins to lose momentum. To this end, appropriate contingency reserves for public spending should be set aside now, as these would permit a rapid adaptation of spending policy to any change in the business situation, and so endow budget policy with the flexibility and reversibility which is very necessary if stability is to be restored and lasting and rapid economic growth safeguarded.

B. Recent developments

1. Demand

The expansion of overall demand in the Community slowed down a little in the closing months of 1969 and early 1970. There was in particular a weakening in the dynamism of external demand in terms of actual exports of goods and services to non-member countries.

From November to January, the value of the Community's visible exports (foreign trade statistics, adjusted for seasonal and fortuitous variations) was only 3% higher than from August to October; it is even probable that in terms of volume there was no further rise at all, as export prices have stiffened considerably.

This trend in Community exports is mainly attributable to the tendency for sales to the United States and the United Kingdom to level out, if not to decline slightly.

In the United States, economic activity has entered a phase of stagnation; in the fourth quarter of 1969, real GNP declined slightly; the index of industrial production fell by 2.8% from July to January. The pressure on costs and prices has nevertheless not yet eased. In February, consumer prices were 6.3% up on a year earlier. The level of American imports has remained virtually unchanged in the past few months.

In the United Kingdom, too, the economic trend lacked dynamism. The index of industrial production, however, which had been declining until October has since been showing signs of moving slightly upwards. While investment activity continued to gain in strength, the volume of private consumption stagnated. Imports showed no more than a very modest rise.

While, then, the trend of Community sales to the United States and the United Kingdom, sales which account for more than one fourth of the Community's total exports to non-member countries, was sluggish and exports to the countries of the Eastern bloc were climbing less steeply, deliveries to other major trading partners continued to expand appreciably. Exports to the continental EFTA countries, including in particular Sweden and Switzerland, maintained their vigorous upward movement. Sales to Spain and Japan likewise continued to rise distinctly. The value of deliveries to the developing countries also remained at a high level.

In the early part of 1970 gross fixed asset formation was still growing at a very lively pace, especially in the form of investment in plant and machinery: in the past few months there has been a very vigorous expansion in deliveries by the Community's capital goods industries to the internal markets, as well as greatly increased imports of capital goods from non-member countries.

Investment in building and construction, particularly industrial building, again moved distinctly upwards, while in residential construction the level of orders in the third quarter of 1969 and the more recent figures for building starts point to a slowdown of expansion. In most member countries the growth of building investment by the public authorities was curbed by the more rigorous budget policy.

Stockbuilding probably made a more vigorous contribution to the expansion of overall demand than previously. Import statistics show that purchases of raw materials and semi-manufactures accelerated sharply. In addition, there has in the past few months been an increasing tendency for industry and the distributive trades to pay more attention to the build-up of their stocks; the business surveys show at any rate that fewer managements than before report their stocks of finished products as below normal.

In the fourth quarter of 1969, private consumers' expenditure in the Community as a whole rose less vigorously than in the previous quarter. In Italy, the loss of income suffered by workers during the strikes unmistakably affected spending. In France, expenditure by households on consumption has been expanding much more slowly since September, as hire purchase regulations were tightened at the end of August and the propensity to save of households was returning more and more to normal, after having dropped sharply during a bout of speculative buying. In Belgium, the expansion of private consumption probably eased for a time during the final quarter, credit

Visible exports to non-member countries

(Values and % changes on preceding year)

	1968		1969				
	million u.a. [1]	Full year	1st quarter	2nd quarter	3rd quarter [2]	4th quarter [2]	Full year [2]
All non-member countries	35 290	+ 11.5	+ 3.5	+ 21	+ 9.5	+ 10	+ 11
of which :							
Industrialized countries [3]	22 873	+ 11.5	+ 2.5	+ 21	+ 11	+ 13	+ 12
including :							
United States	5 768	+ 30.5	— 15.5	+ 19	+ 1.5	+ 8	+ 3
EFTA	11 217	+ 7.5	+ 7.5	+ 17.5	+ 13	+ 15	+ 13
United Kingdom	3 127	+ 10	+ 2.5	+ 14	+ 7	+ 7	+ 7
Developing countries [4]	9 309	+ 12	+ 7	+ 19.5	+ 8	+ 6	+ 10
including :							
Associated overseas countries and territories	2 064	+ 15.5	+ 12	+ 39.5	+ 2	0	+ 11
Other countries [5]	3 108	+ 8.5	+ 3.5	+ 28	+ 5	+ 2	+ 9

Source : Statistical Office of the European Communities (SOEC).

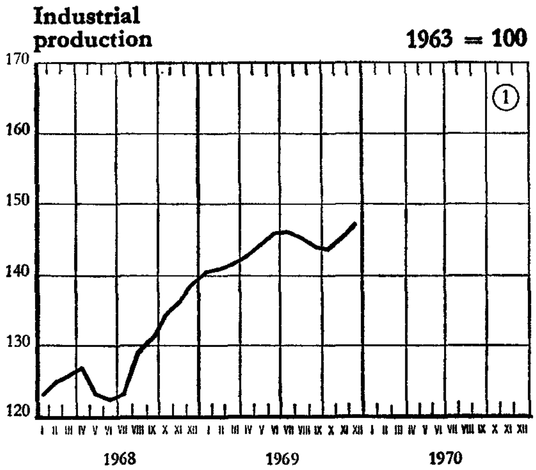
[1] 1 u.a. = 1 unit of account = 0.888671 g of fine gold = US $1 at the official exchange rate.
[2] Commission estimates.
[3] Class 1 of the Standard Country Classification for Foreign Trade Statistics of the EEC.
[4] Class 2 of the Standard Country Classification for Foreign Trade Statistics of the EEC.
[4] Class 3 of the Standard Country Classification for Foreign Trade Statistics of the EEC and other destinations.

restrictions having been tightened up in the middle of 1969 and the introduction of TVA having been postponed to 1 January 1971. In Germany, by contrast, private consumers' expenditure, supported by a spate of wage awards, continued to surge ahead in the fourth quarter.

2. Production

Around the turn of the year internal supply in the Community was still expanding, though more slowly than before.

From the third to the fourth quarter of 1969, industrial production as reflected in the seasonally adjusted index of the Statistical Office of the European Communities, which excludes construction and food, beverages and tobacco, went up by a good 2%; preliminary and incomplete information on the trend obtaining at the beginning of 1970 suggests that expansion has since gathered little if any momentum. In the past few months, however, there have also been special factors that depressed the level of production, especially in Italy, where there were unusually sharp labour disputes in the fourth quarter, and in Belgium, where at the beginning of 1970 labour disputes at the collieries entailed difficulties in the supply of energy to individual sectors. The exceptionally bad weather of this winter has probably also helped to depress the level of production generally.



Thanks to the substantial backlog of orders, production has not been affected by the slow-down in the expansion of new orders reaching certain industries in a number of member countries since the autumn of 1969; the difficulties hampering the advance of production have on the contrary been almost exclusively the result of shortages of manpower and technical capacities.

In the services sector there has been no easing in the pace of expansion. Early in 1970, turnover in the distributive and tourist trades was still being stimulated by a further rapid expansion in the incomes of households. In the other services sectors, such as banking and transport, the rapid expansion of general economic activity was reflected in an appreciable rise in real value added.

The strains on the labour markets of the Community continued unabated and in some member countries they even grew more acute. Taken overall, the manpower requirements of firms continued to rise unmistakably. Unemployment

Industrial production in the Community

(% change on preceding year)[1]

	1968	1969				
		1st quarter	2nd quarter	3rd quarter	4th quarter	Full year
Industry as a whole [3]	+ 8.8	+ 13.0	+ 18.2	+ 9.7	+ 6.1	+ 11.7
of which :						
Germany	+ 13.1	+ 17.5	+ 14.8	+ 11.9	+ 11.2	+ 13.8
France	+ 4.0	+ 10.8	+ 33.0	+ 9.0	+ 4.6	+ 13.6
Italy	+ 6,3	+ 9.0	+ 7.9	+ 3.1	— 8.7	+ 2.7
Netherlands	+ 12.0	+ 14.5	+ 12.9	+ 13.6	+ 12.5	+ 13.4
Belgium	+ 6.4	+ 11.8	+ 12.7	+ 7.7	+ 10.8	+ 10.8
Luxembourg	+ 5.5	+ 17.2	+ 12.9	+ 12.6	+ 11.1	+ 13.4
of which :						
Mining and quarrying	+ 4.3	+ 3.5	+ 8.1	+ 2.6	+ 2.2	+ 4.2
Textiles	+ 9.2	+ 10.8	+ 15.4	+ 5.2	+ 6.3	+ 9.4
Paper and paperboard	+ 7.6	+ 10.9	+ 14,1	+ 9.5	+ 8.4	+ 10.7
Leather	+ 9.9	+ 12.1	+ 11.4	— 0.3	— 2.5([2])	+ 5 ([2])
Metalworking	+ 7.3	+ 15.5	+ 23.3	+ 11.8	+ 8 ([2])	+ 14 ([2])
Iron and steel	+ 9.7	+ 8.5	+ 17.0	+ 6.9	+ 3.6	+ 9.0
Electricity	+ 8.4	+ 9.2	+ 14.7	+ 9.3	+ 8.3	+ 10.2

[1] Calculated on the basis of the unadjusted indices of the Statistical Office of the European Communities.
[2] Estimates.
[3] Excluding construction and food, beverages and tabacco.

was down to a very low level, and the recruitment of foreign labour was stepped up.

3. Balance of the markets

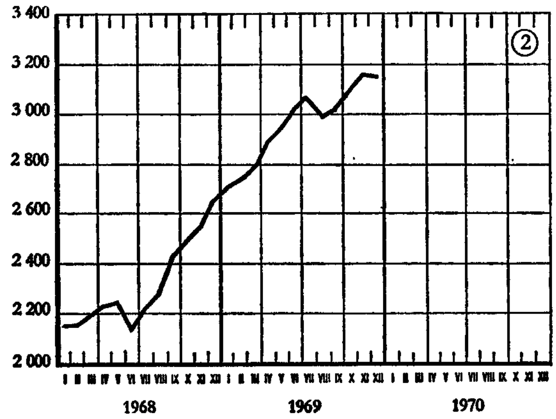
At the end of 1969 and the beginning of 1970, the Community's imports from non-member countries were still expanding rapidly. From November to January, the value of visible imports (foreign trade statistics, seasonally adjusted) was 6% higher than from August to October.

The advance of industrial production, the replenishment of stocks and the price increases on the raw material markets caused a lively rise in imports of basic materials. Vigorous investment demand led at the same time to a further expansion of purchases of plant and machinery. Lastly, the marked expansion of consumption was also reflected in a faster growth of consumer goods imports. Imports of agricultural products, by contrast, rose only slightly in most member countries.

Deliveries by the EFTA countries, especially Sweden and Switzerland, showed a particularly vigorous increase. The sharp expansion of sales by the developing countries was attributable not only to the rise in raw material prices but also to the vigorous growth of Community imports measured in terms of volume. In the past few months, there has also been a vigorous expansion of imports from the state-trading countries.

The persistent boom throughout the Community is reflected in a rapid expansion of visible trade between the member countries. But the pace of advance has slowed down a little, partly because of special factors such as the parity changes in France and Germany and the strikes in Italy, partly, too, because the expansion of expenditure on consumption has calmed down in France. The vigorous expansion of French imports, which until the autumn had exerted a strong influence on intra-Community trade, gave way to a decline after the devaluation. The continuing rise in purchases by Germany and the Benelux countries did not fully offset this development; at the same time demand from France's major trading partners was still very lively, so the expansion of French sales abroad was gathering momentum again round the turn of the year, after having slackened for a time after the devaluation.

Trade between member countries **million u.a.**



Prices continued to display a strong upward tendency throughout the Community. The reasons for this are many: they include the persistence of very heavy strains on the markets for goods and services, a rise in import costs, an increase in the charges for public services in some countries and, increasingly, a rise in wage costs. To judge by incomplete information on the trend of production, wage incomes and employment, the rise in industrial labour costs per unit of gross value added at constant prices, for instance, which had already amounted to 2 ½ to 3% in 1969 (see Annex), was in most countries gathering additional momentum at the beginning of 1970.

In France there was the additional factor that the difference between the French and the common agricultural prices caused by devaluation and authorized through a Council decision in August has been partly reduced. Authorization was also granted for increases in the prices for industrial raw materials and semi-manufactures, some of which were considerably lower than the corresponding world market prices. In addition, the charges for various public services were put up.

In Germany, the rise in the level of consumer prices has gathered momentum in the past few months, despite the moderating influence exerted by revaluation.

In the Benelux countries, prices have been forced up not only by general upward tendencies inherent in the business situation, but also by the revaluation of the D-mark. In Luxembourg, *Visible imports from non-member countries*

(Imports 1968 and % year-to-year changes)

	1968		1969				
	million u.a. [1]	Full year	1st quarter	2nd quarter	3rd quarter	4th quarter [2]	Full year [2]
All non-member countries	33 542	+ 8.5	+ 12	+ 22.5	+ 15	+ 17	+ 17
of which :							
Industrialized countries [3]	18 626	+ 9.5	+ 11.5	+ 26	+ 17	+ 20	+ 18
including :							
United States	6 386	+ 8.5	— 2.5	+ 25	+ 13	+ 20	+ 14
EFTA	7 840	+ 10.5	+ 16.5	+ 25	+ 18	+ 20	+ 20
United Kingdom	2 994	+ 11	+ 15	+ 24	+ 17.5	+ 20	+ 20
Developing countries [4]	12 506	+ 8	+ 13	+ 18.5	+ 11	+ 10	+ 13
including :							
Associated overseas countries and territories	2 498	+ 9.5	+ 9	+ 23	+ 7	+ 19	+ 12
Central and South America	2 679	— 4.5	+ 14	+ 18	+ 21.5	+ 18	+ 18
Other countries [5]	2 410	+ 5	+ 9	+ 18	+ 18.5	+ 12	+ 14

Source : Statistical Office of the European Communities (SOEC).

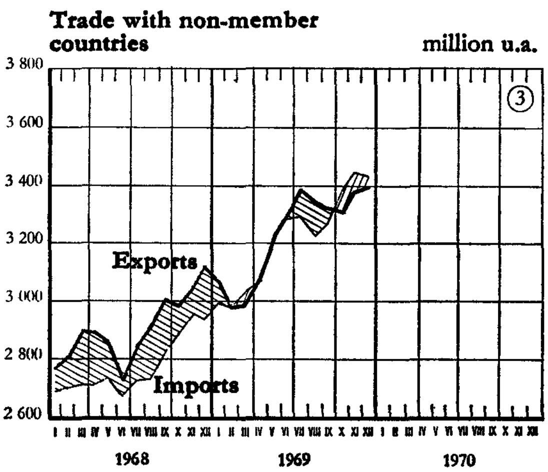
[1] 1 u.a. = 1 unit of account = 0.888671 g of fine gold = US $ 1 at the official exchange rate.

[2] Commission estimates.

[3] Class 1 of the Standard Country Classification for Foreign Trade Statistics of the EEC.

[4] Class 2 of the Standard Country Classification for Foreign Trade Statistics of the EEC.

[5] Class 3 of the Standard Country Classification for Foreign Trade Statistics of the EEC and other sources.

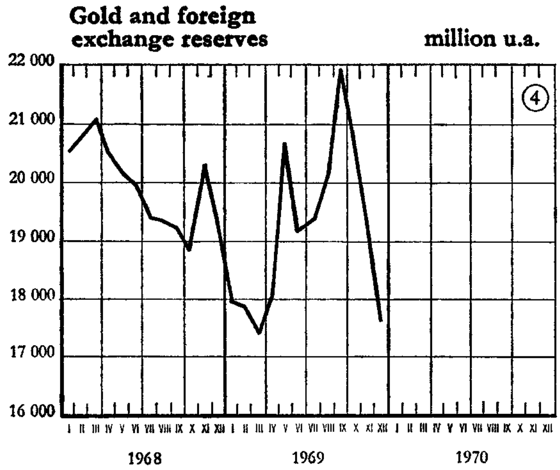


the introduction of TVA on 1 January 1970 has not yet had any very significant effect on consumer prices, but it must be borne in mind that profit margins were frozen.

The Community's balance of visible trade with non-member countries has tended to deteriorate since the third quarter.

The Community's capital account closed with a very heavy deficit, mainly owing to massive outflows of money and capital from Germany in the wake of D-mark revaluation. But Italy, too, experienced heavy exports of capital, which in February prompted the Italian Government to take special measures to supervise money transfers across the frontiers. In the fourth quarter, the official gross gold and foreign exchange reserves of the Community fell by some $4 300 million, reaching at the end of December the comparatively low level of $17 700 million. In Germany alone, reserves fell by some $4 000 million.

In some member countries the cash transactions of the public authorities also acted as a drain on liquidity. The cash surplus of the Italian Treasury, for instance, was much heavier in the fourth quarter than a year earlier. In France, the cash surplus was of the same order of magnitude as in the corresponding quarter of



Demand for and supply of goods and services

	1967 [1]	1968 [1]		1969 [2 4]		1970 [3 4]
	At current prices in '000 million u.a.[5]	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Gross fixed asset formation	80.4	+ 6.5	+ 8.6	+ 10	+ 16½	+ 7½
Public current expenditure on goods and services	50.0	+ 3.0	+ 8.0	+ 4	+ 11½	+ 4
Private consumers' expenditure	211.3	+ 4.4	+ 7.3	+ 7	+ 11½	+ 6½
Gross Community product	350.0	+ 5.8	+ 8.7	+ 7½	+ 12½	+ 5½
Balance exports less imports (at current prices, in '000 million units of account) [5]	+ 5.9		+ 7.1		+ 5.5	+ 4

[1] *Source :* Statistical Office of the European Communites.
[2] Commission estimates.
[3] Commission forecasts.
[4] Based on Community totals of the aggregates of the individual member countries at official exchange rates 1963.
[5] 1 u.a. = 1 unit of account = 0.888671 g of fine gold = US $1 at the official exchange rate.

Note :
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks and differences in treatment of the balance of exports less imports.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts of the member countries but are established and published on the sole responsibility of the Commission.

the previous year, when it had already been very high. Germany, the Netherlands and Belgium registered the usual seasonal deficits. In Germany, however, the deficit was low compared with a year earlier; it was mainly financed from existing credit balances and short-term loans, while in Belgium the authorities made considerably more use than before of long-term financing. In the Netherlands, the budget deficit was comparatively low—as it had been in 1968.

The expansion of bank lending to business and private customers slowed down a little in some member countries. This is in part due to a tightening of the restrictive credit policy but in part also, as in the Benelux countries, to return flows of foreign exchange after the revaluation of the German mark. In Germany, by contrast, the credit requirements of trade and industry went up sharply after revaluation, because much of the money which had flowed in from abroad was repatriated and enterprises were increasingly forced to borrow from their banks.

As a result of the restrictive credit policy pursued in all member countries, and even more because of the persistent rise in interest rates on the Eurodollar market and in major non-member countries, the situation on the Community's money markets had grown tighter by the end of the year. Only in January-February, when short-term interest rates eased both in the United States and on the Eurocurrency market, did call money rates adjust downwards, particularly in the Benelux countries. In Germany and Italy, however, the central banks put up the cost of credit again at the beginning of March. In Germany, the discount rate and the rate for loans against securities were raised from 6% to 7.5% and from 9% to 9.5% respectively, mainly in view of the domestic business situation. Italy at the same time put up the discount rate from 4% to 5.5%, which brings the cost of rediscount credit up to 7 % if the relevant supplements are taken into account.

On the capital markets of the Community, yields from fixed-interest-bearing securities continued to rise distinctly until the beginning of 1970. On the equity markets of the member countries, prices have been more or less static or have even declined since October. The weakness of the New York Stock Exchange and the effects of the restrictive measures were probably major contributing factors; at the end of January, the Dow-Jones index of industrial stock prices touched its lowest point since November 1963. Only on the Paris Stock Exchange was the price trend still fairly firm at the beginning of the year.

C. Outlook

The outlook for the months ahead is largely identical with the prospects outlined in the last Quarterly Survey (No. 3/4-1969). The divergence between the expansion of internal demand and that of external demand could however well be rather larger than previously assumed. The forces of expansion inherent in the internal business situation, for instance, are proving to be somewhat stronger than expected. The very considerable strains still perturbing the markets of the Community will ease only when the expansion of demand returns to normal, and this will not be before the second half of the year at the earliest.

The outlook for the world business trend until the end of the year is still much the same as outlined in the last Quarterly Survey. The current tendency for the world business climate to cool down is likely to continue and entail an appreciable slackening of world trade. In almost all major industrial countries the growth of demand, production and employment will be lower in 1970 than it was in 1969. Given the generally still very strong upward thrust of prices and costs and the rather precarious external finance position of some non-member countries, most governments are likely to maintain their measures to curb domestic demand. In this context it must not be overlooked that the balance-of-payments difficulties of non-member countries may grow more serious still should the rapid growth that has been registered by their exports give way to a calmer trend owing to a decline in the vigour of world trade.

In the United States, important economic pointers have been provided by the maintenance of the restrictive line of credit policy, the tax reform adopted at the end of 1969 and the presentation of the budget for the fiscal year 1970/71. Given the continuing upward tendency of prices and the inflationary behaviour of transactors, the monetary authorities have so far done little if anything to ease credit restrictions, despite the decline of production. As a result of present tendencies on the market there is, however, some easing of the situation on the money markets, reflected mainly in the interest rates offered for short-term money, which had been extremely dear at the end of 1969. The tax and social laws adopted at the end of 1969 contain provisions that from 1 January 1970 the income tax surcharge is to be reduced from 10% to 5% and that social benefits covering 25 million people are to be raised by 15%. These measures reduce the surplus on the federal budget 1969/70 from the early estimate of $6 000 million to $1 500 million. This less restrictive budget policy will, however, not yet produce any major change in the first half of 1970 on the American economic scene as described in the last Quarterly Survey. During this period, the spontaneous forces of the market will probably lead to a further slight decline in economic activity, and this implies a weak propensity to import. Although the tax reform is certain to encourage private consumption, corporate investment must be expected to stagnate, stockbuilding to slow down and investment in residential construction to decline.

The draft budget for 1970/71, submitted on 30 January 1970, still provides for a small surplus of $1 300 million. Expenditure is to be only 1.5% higher than spending in the current budget year. Heavy cuts were made particularly in spending on space projects (down $2 800 million) and defence (down $5 800 million). Expenditure in the social field, by contrast, was up considerably. Revenue is to reach $202 100 million, compared with $199 400 million in the preceding budget year. The small growth of only 1.4% is mainly a result of the tax concessions on private incomes.

All in all, the budget is of a slightly restrictive nature. Although the effects of the budget surplus should not be over-estimated—it is only some 0.1% of GNP and might be reduced further in the course of the budget discussions—the smallness of the rise in public expenditure should exert a generally dampening influence on economic growth. Even if, during the period ahead, changes in the inflationary behaviour of transactors and developments in the level of employment make it possible to relax credit policy somewhat, the average real GNP for 1970 will be little higher than a year earlier. For this small growth to be achieved there must be some measure of expansion in the second half of the year. The development of private consumers' expenditure may contribute to such a revival, as disposable incomes will rise very appreciably not only because of the substantial wage increases but also because of the tax cuts, including in particular the complete disappearence of the income tax surcharge on 1 July 1970. On the other hand, the further trend of investment, especially corporate investment, is still a factor of considerable uncertainty. When account is taken of the time it usually takes for imports to be affected, imports by the United States are likely to show little if any rise in the later part of the year. At the moment there even appears to be a fair chance of a further decline in the trend.

In the United Kingdom, the economic trend is likely to remain much the same until the summer. Industrial production will probably continue to revive, though at a slow pace. Investment and exports will be the main expansionary elements in economic activity. Given the wage demands put forward for some 2.5 million workers, incomes must be expected to go up sharply, particularly in the second half of 1970, which will entail an acceleration of private consumers' expenditure and consequently also of the growth of production. These tendencies may, however, be changed by the 1970/71 budget, which will have to be adopted against the background of a balance of payments that has been improving considerably but carries the burden of heavy foreign indebtedness. The outlook for the trend of Community exports to the United Kingdom is at all events rather favourable.

In several other EFTA countries expansion is likely to weaken distinctly in the months ahead, particularly in the Scandinavian countries, where there will probably not only be a slowdown of the growth of export demand but where domestic demand is also likely to be curbed, mainly as a result of the more restrictive economic and finance policy. In Sweden, for instance, the increase in indirect taxation from February on will probably affect private consumption. In Austria and Switzerland, by contrast, the economic trend will presumably remain very dynamic.

For the Japanese economy 1970 will be another year of vigorous economic growth, despite the persistent tendency for prices to climb and despite the restrictive money and credit policy. The draft budget for the financial year 1970, submitted at the beginning of February, provides for a sharp rise in social expenditure and may thus give a further impetus to consumption. The tendency for foreign trade to be liberalized will provide an additional stimulus to the rapid growth of imports. In other industrial countries such as Spain, by contrast, the restrictive measures taken by the authorities to restore external equilibrium may considerably impede the development of imports in the course of the year.

In the developing countries, especially those most heavily dependent on trade with the United States, the growth of imports may slacken as the year advances, mainly because the external position of these countries is deteriorating.

On balance, the persistently slower growth of imports by the non-member countries as a whole, coupled with the high level of capacity utilization in major export industries in the Community, will probably be reflected in a steadily less expansionary trend of Community exports.

As pointed out at the beginning of this Chapter, internal demand, particularly private consumers' expenditure, will probably expand more vigorously from 1969 to 1970 than was assumed in the last Quarterly Survey. This may lead to a delay in the easing of what are still very severe strains. Internal demand is likely to rise with especial vigour in the first half of the year, but towards the end of the year it may well slow down fairly appreciably.

In the months ahead, actual investment spending by enterprises will still be rising vigorously in all member countries. Later in the year, however, the propensity to invest may gradually lose in vigour. A number of indicators point in this direction: the less favourable outlook for world business, the mounting pressure on corporate profit margins, and the effects of the credit restrictions. The acute manpower shortage and the high degree of capacity utilization are on the other hand still major factors encouraging investment by enterprises.

Building investment as a whole can for a while be expected to maintain a lively rate of expansion, especially since the production losses suffered during the winter of 1969/70 were heavier than usual for the season. However, to judge by the latest trend of new orders and building starts, some member countries may register a certain slowdown of growth in the second half of the year.

In most member countries, stockbuilding is certain to continue providing fairly lively stimuli to growth throughout the greater part of the year. Stocks of finished products are generally considered to be very low; in addition, the vigour of the economic upswing, coupled in Italy with labour disputes, have in many cases led to a situation where stocks of raw materials and semi-manufactures have failed to keep up with the growth of production.

The stimuli provided by private consumer spending will remain very vigorous throughout the year, notably in view of the expected trend of mass incomes. This will be mainly determined by the vigorous wage increases awarded since September under collective wage agreements and those to be expected when further wage agreements come up for renewal, the wage drift engendered by the persistent strains on the labour market, and the expected appreciable increase in prices, which in most countries is more or less automatically reflected in wage increases because wages are linked to the cost of living. Most countries will in addition register a vigorous rise in social transfer payments. In view, too, of the upward thrust of prices, the propensity to consume of households may well grow.

Only in France, where the savings ratio has for some time been going up considerably, is it at all likely that the growth rate of private consumers' expenditure, which has been slackening since the early autumn of 1969, will turn out to be fairly modest—provided always that savings activity does not change radically.

All in all, the latest estimates suggest that the rise in private consumers' expenditure from 1969 to 1970 will be 11.5% in money terms and some 6% in real terms. In the last Quarterly Survey, these growth rates were put at 10% and 5%, respectively.

Industrial production in the Community as a whole is likely to expand distinctly, although the rate of growth may slow down further. In most industries and countries the acute manpower shortage and the shortage of technical capacity are indeed likely to have a considerably inhibiting effect on the growth of production. Towards the end of the year, production in some basic materials industries may also weaken, because the trend of demand will be more differentiated. The industries near the consumer stage, by contrast, will throughout the year find it difficult to keep abreast of the probable expansion of demand.

The gross Community product in real terms may increase by some 5 ½%, despite the slowdown in growth to be expected for the second half of 1970.

Imports from non-member countries will continue to soar, as the pressure of demand on supply will certainly persist during the greater part of the year. Additional stimuli will come from the cooling down of the business climate, with the resultant increase in the ability of some major industrial countries to make deliveries, and from the effects of the DM revaluation, which will make themselves felt more strongly. The growth of imports from 1969 to 1970 will, therefore, scarcely be lower than a year earlier, when it had been 17% in terms of value. With the rise in exports expected to be comparatively weak, the deficit on the Community's balance of trade (cif—fob) is likely to expand appreciably.

For the time being there should nevertheless still be a distinct tendency for prices to move upwards. The prices for industrial consumer goods, in particular, may rise appreciably further, though in most member countries they have been climbing vigorously since the middle of 1969; as strains on the market will persist for a while, the chances are that the increase in unit costs, which has gathered momentum in the meantime, will be largely passed on to prices. Only towards the end of the year may a change in the business climate exert a moderating influence. The appreciable upward thrust of wages may also entail a faster rise in the cost of services.

Major economic measures taken

January:

On 1 January 1970 special drawing rights in the amount of $3 500 million were created within the IMF. The share of the EEC member countries is $633.4 million.

Elimination of the customs duties still affecting trade within the Community, particularly in the agricultural sector, and another cut in the external customs tariff under the Kennedy Round agreements.

On 26 January 1970, decision by the representatives of the ECSC Member States meeting in the Council to suspend or reduce until 31 May 1970 the customs duties on certain products falling under the ECSC Treaty.

At the session of 26 January the Council approved joint action to fix, in quantitative terms, medium-term targets which would contribute to the effective harmonization of medium-term policies.

At the same session, the Governors of the Central Banks were invited to sign the agreement setting up a system of short-term monetary support between the Central Banks of the Member States.

On the same date the Council, acting on a proposal from the Commission, approved the procedure for the short-term economic policy consultations between the Member States.

Also on 26 January, the Council approved the guidelines, put forward by the Commission in a memorandum, intended to improve the control of short-term economic developments in 1970.

February:

On 9 February the Central Bank Governors of the Community signed the agreement setting up a system of short-term monetary support between the Member States. The agreement took effect with the date of signature.

Community

TABLE 1: **Basic data 1968**

	Community	Germany	France	Italy	Netherlands	Belgium	Luxemburg
Total area ('000 sq. km.)	1 167.5	248.5	551.2	301.2	33.5	30.5	2.6
Total population ('000)	185 806	60 184	50 188	52 778	12 725	9 619	335.5
Density of population per sq. km.	159	242	91	175	380	315	129
Numbers in employment ('000)	73 898	26 342	19 675	19 069	4 547	3 615	138.8
Numbers in employment, breakdown by main sector (%) :							
— Agriculture	14	10.1	15	22.3	7.7	5.6	12.1
— Industry	43	47.4	40	41.4	40.2	44.9	45.3
— Services	43	42.5	45	36.3	52.1	49.5	42.6
Share of gross domestic product (%) :							
— Agriculture	.	4.5	8	11.1	7.0	5.4	6.2
— Industry	.	50.8	41	38.6	42.2	40.6	50.0
— Services	.	44.7	52	50.3	50.8	54.0	42.9
In % of gross domestic product :							
— Private consumers' expenditure	.	55.9	60.9	63.6	56.4	64.0	61.1
— Public current expenditure on goods and services	.	15.5	12.8	13.5	15.5	14.3	12.0
— Gross fixed asset formation	.	23.2	24.9	19.4	26.7	21.3	25.1
— Total exports	.	23.1	14.3	19.5	43.0	38.2	81.2
— Total imports	.	19.8	14.3	14.1	43.1	38.9	78.9

TABLE 2: **Key indicators**

	% change by volume on preceding year					Volume indices (1963 = 100)
	1964	1965	1966	1967	1968	1968
Gross Community product	6.1	5.0	4.1	3.3	6	127
Industrial production	7.0	4.4	5.3	1.3	8.8	130
Visible imports	6.9	5.0	6.8	0.6	11.5	135
Private customers' expenditure	4.8	5.0	4.5	3.8	4.5	125
Gross fixed asset formation	9.4	3.8	4.7	1.2	6.5	128
Visible exports	9.3	11.0	8.4	7.7	13.1	160
Intra-Community visible trade	13.2	12.2	10.9	6.1	18.9	178
Gross product per capita	5.0	3.9	3.2	2.7	5.1	121

TABLE 3: Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1967	115	118	120	122	121	122	110	92	122	126	130	131
	1968	120	126	131	133	121	130	119	106	136	141	148	146
	1969	138	142	146	150	151	152	135	115	145	150	158	154
Imports from non-member countries (cif, million u.a.)	1967	2 607	2 392	2 610	2 515	2 564	2 654	2 366	2 376	2 444	2 620	2 784	2 837
	1968	2 694	2 606	2 811	2 709	5 408		2 850	2 608	2 790	2 991	3 061	3 008
	1969	3 173	2 793	3 105	3 283	3 321	3 376	3 259	2 858	3 365	3 637	3 407	.
Exports to non-member countries (fob, million u.a.)	1967	2 563	2 413	2 678	2 681	2 595	2 721	2 543	2 358	2 525	2 918	2 763	2 876
	1968	2 781	2 771	3 025	2 848	5 323		3 206	2 772	2 784	3 297	3 171	3 286
	1969	2 887	2 745	3 261	3 305	3 295	3 296	3 584	2 801	3 225	3 729	3 425	.
Balance of trade (million u.a.)	1967	− 44	+ 21	+ 68	+ 166	+ 31	+ 67	+ 177	− 18	+ 81	+ 298	− 21	+ 39
	1968	+ 87	+ 165	+ 214	+ 139	− 85		+ 356	+ 164	− 6	+ 306	+ 110	+ 278
	1969	− 286	− 48	+ 156	+ 22	− 26	− 80	+ 325	− 57	− 140	+ 92	+ 18	.
Intra-Community trade (million u.a.)	1967	1 925	1 861	2 145	2 002	1 974	2 099	1 913	1 734	1 956	2 245	2 182	2 126
	1968	2 123	2 162	2 371	2 287	4 248		2 479	2 085	2 409	2 773	2 658	2 724
	1969	2 695	2 727	3 057	3 043	3 013	3 101	3 157	2 415	3 089	3 554	3 144	.

NOTES TO GRAPHS AND TABLES

Source: Community: Statistical Office of the European Communities (SOEC).
Germany: SOEC; Statistisches Bundesamt.
France: SOEC.
Italy: Relazione generale sulla situazione economico del Paese (1968).
Netherlands: SOEC; Ministerie van Sociale Zaken en Volksgezondheid; Centraal Bureau voor de Statistiek.
Belgium: SOEC; Ministère de l'emploi et du travail;
Luxembourg: SOEC.

Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US \$1) at the official exchange rates.

Graph 1

— Trend curve; estimate established on the basis of indices adjusted for seasonal and fortuitous variations (excluding construction, food, beverages and tobacco).

Graph 2

— Three-month moving averages of the seasonally adjusted value of trade between member countries, as shown by foreign trade statistics on imports.

Graph 3

— Three-month moving averages of the seasonally adjusted value of exports to non-member countries (fob) and imports from these countries (cif), as shown by foreign trade statistics.

Graph 4

— Total gross reserves of gold and foreign exchange held by the monetary authorities of the member countries at the end of each month.

Community

Table 1

- Total population at mid-year; for Germany, estimated average for year; for Italy, average for year.
- Resident population in employment at mid-year; for Germany, estimated average for year; for Italy, average for year less persons temporarily working abroad.
- Breakdown by agriculture, industry and services at factor cost; for Luxembourg, 1967 figures.
- Shares of the major aggregates in the gross domestic product at market prices.
- Total exports and imports: goods, services and factor income.

Table 2

- Industrial production: index of the Statistical Office of the European Communities, excluding construction, food, beverages and tobacco.
- Imports (cif) from non-member countries, as shown by foreign trade statistics.
- Exports (fob) to non-member countries, as shown by foreign trade statistics.
- Trade between member countries, as shown by foreign trade statistics on imports.

Table 3

- See note to Table 2.

II. THE SITUATION IN EACH OF THE COMMUNITY COUNTRIES

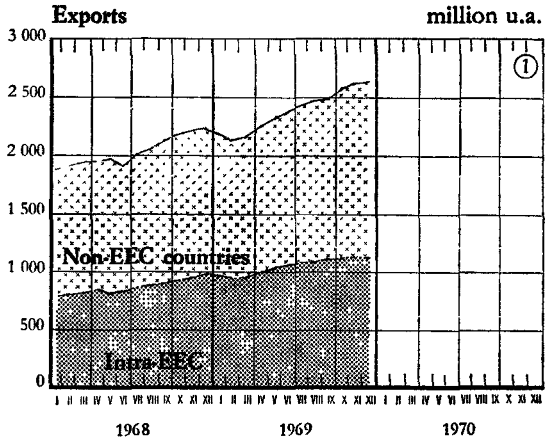
A. Germany

Although the inflow of orders to firms has become somewhat less vigorous, the German economy was still under heavy strain at the beginning of 1970. However, exports, previously growing extremely fast, are now expanding at a more normal pace. Investment remains brisk. The rise of private consumers' expenditure has further quickened under the impact of very considerable wage increases. The boom is unlikely to lose appreciable momentum for some months to come, so that high capacity utilization is bound to continue. In spite of the stabilizing effects of revaluation, excess demand together with a strong increase in production costs must be expected to push up prices to a further considerable extent.

1. Recent developments

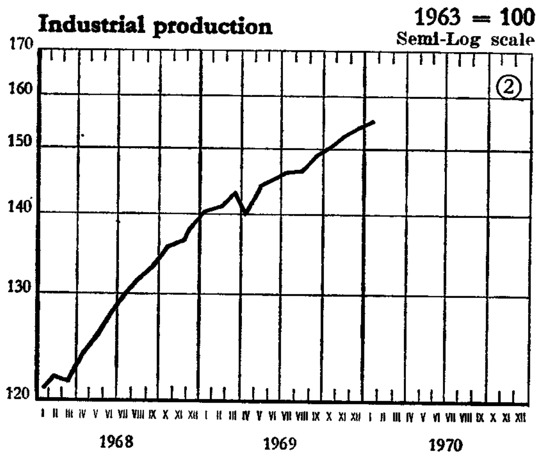
Although there has been evidence lately that revaluation is being followed by some slackening in the hectic pace of demand expansion, the economy of the Federal Republic is still under heavy strain, with both goods and services in short supply and most firms running at or very near capacity. Because of the vigour of expansionary forces at home, of the imbalance on labour markets which, if anything, was still getting worse a few weeks ago, and of the backlog of orders firms still have on their books, no adequate solution has yet been found for the problem of transition from boom to balanced growth. It does not help, incidentally, that in the world at large efforts to deal with inflationary pressure have obviously been less quickly and less conclusively successful than might have been generally desirable.

However, *exports* at any rate had clearly lost momentum round the turn of the year. Seasonally adjusted exports for the months November-January even fell slightly short of their pre-revaluation peak figure, which admittedly was no doubt swollen by firms speeding up export deliveries in the expectation of revaluation. Demand continues to expand vigorously in several major importing countries, and this is keeping the trend of German exports buoyant. Shipments to Italy and France, in particular, were still rising appreciably in recent weeks. Foreign buyers took the brunt of the immediate revaluation effect on German export prices, which rose by 1.6% between October 1969 and January 1970 to a level about 6% higher than in January 1969.



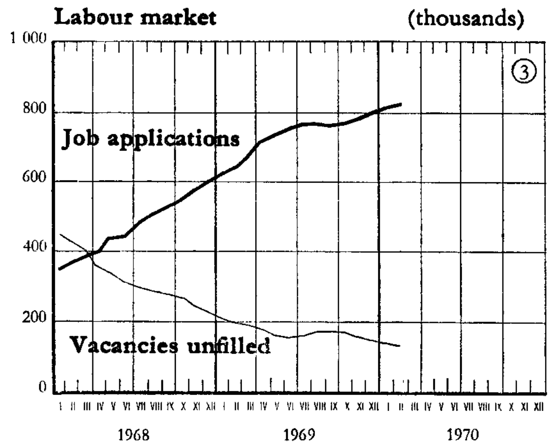
Latest figures again show *investment* as a strongly expanding component of domestic demand. The past year's expansionary momentum was so strong that firms again and again found their investment programmes inadequate to requirements. Although a good deal of new plant came into operation, the previously already very high degree of capacity utilization rose even further. Such figures as are available suggest that expenditure for plant and machinery was climbing steadily and sharply during the early months of this year. In its turn, the steep increase in building and construction investment, especially on the part of firms, continued and was accompanied by unusually large price increases.

Heavy claims on available resources were made, moreover, by *private consumer demand* during the early months of this year. The wave of wage increases which began last autumn has by now spread to nearly all industries and, as of February, had raised the level of agreed weekly wages and salaries by 10.5% on a year-on-year comparison, while actual earnings had gone up even more. Households adjusted expenditure to rapidly rising incomes fairly promptly. The ensuing "spending spree" was mainly concentrated on car purchases and expenditures on travel and services, but was reflected also in sales of traditional consumer goods.

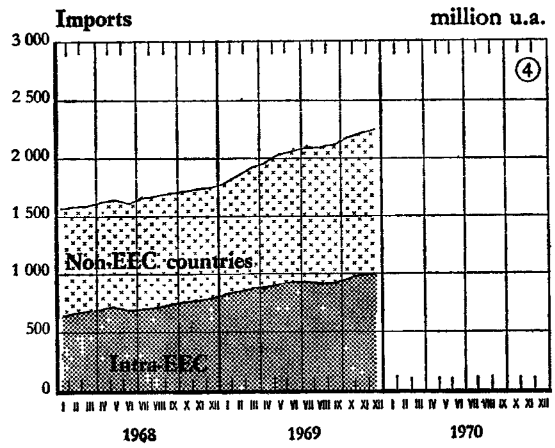


Thus the pressure of demand has not as yet weakened to any significant degree. On the supply side, production again increased very considerably. This applies especially to *industry,* which mobilized its full potential to maximize output. In seasonally adjusted figures, industrial production increased from November to January by about 4%, compared with 1.5% in the preceding three months. In January it was about 11% higher than twelve months earlier.

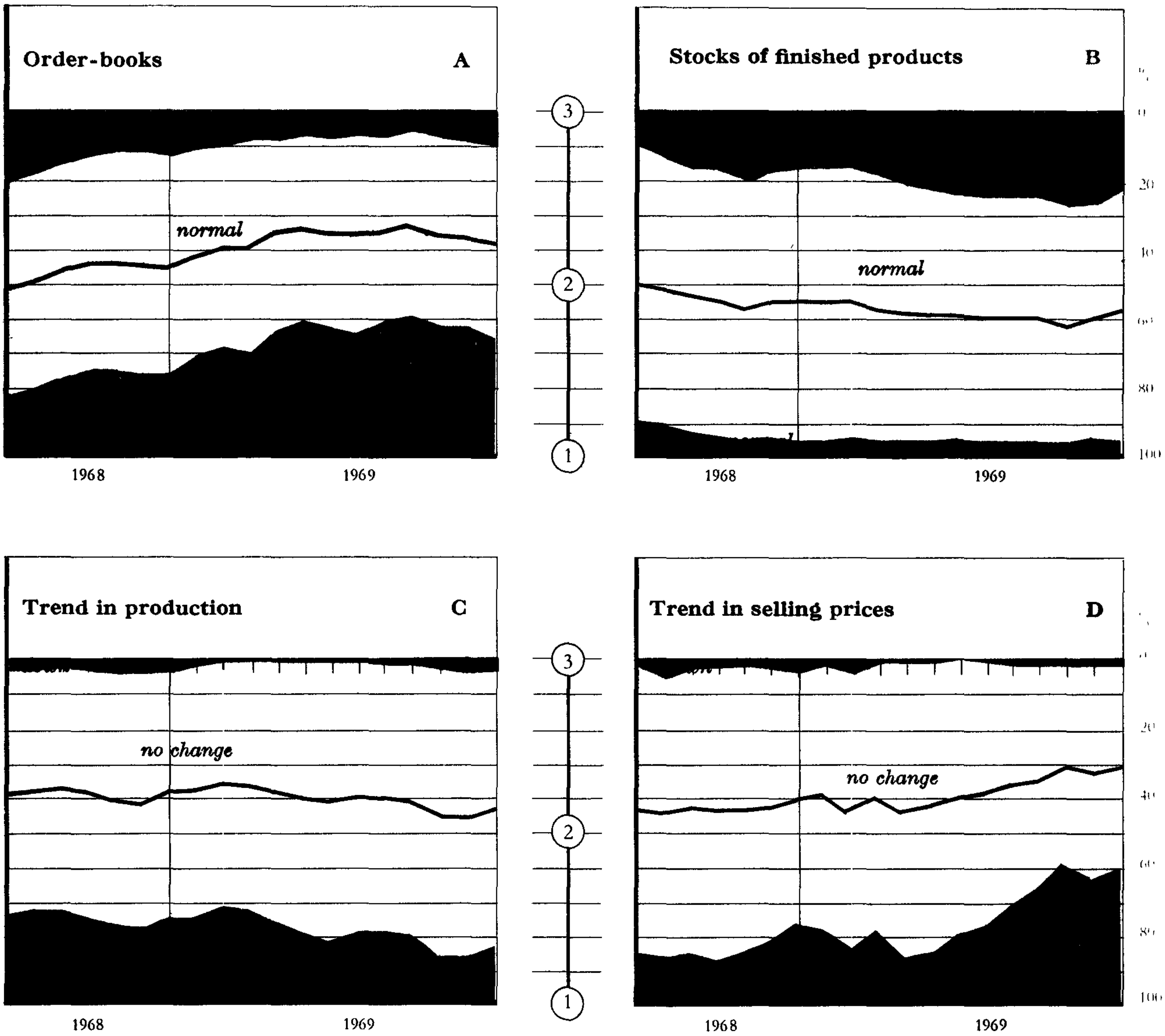
The relatively high elasticity of production was the result of productivity gains, which were considerable largely because of the more widespread application of new technological knowledge linked with large-scale new investment. The *labour market* had been suffering from an extreme shortage of supply ever since the spring of 1969, and the fourth quarter's further appreciable rise in industrial employment was based almost solely on an increase in the employment of foreign workers. At the end of January roughly 1.57 million foreigners were at work in Germany, 438 000 more than a year earlier. The number of unemployed remained extremely low even during the winter months; at the end of February, the unemployment rate was 1.2%, compared with 1.8% at the corresponding date of 1969. In seasonally adjusted terms, there were five times as many job vacancies as there were job seekers.



Apart from variations, visible *imports* climbed steadily until the beginning of the year, with finished products making the strongest gains. But this did not suffice to bridge the wide gap between supply and potential demand or to prevent a further appreciable *price* rise. The upward movement of producers' prices which began in the autumn of 1969 continued unabated in the early months of this year. A



BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



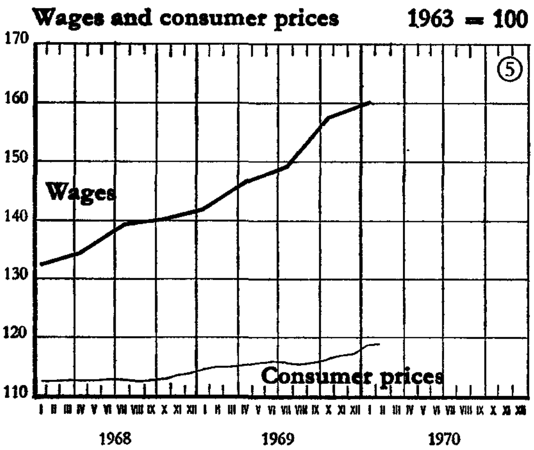
Answers to questions in the EEC business survey, carried out in the German Federal Republic by the IFO-Institut.

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

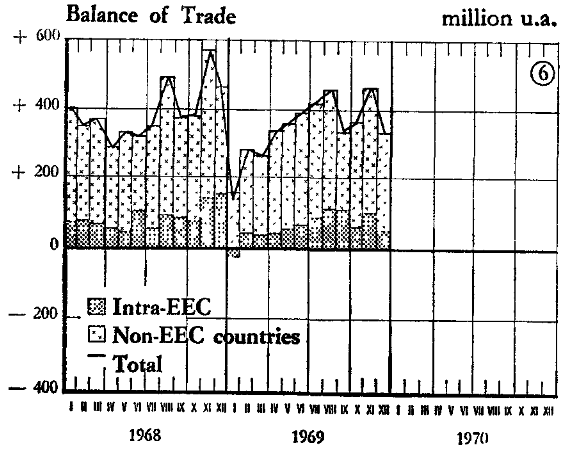
The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

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".

rise of 2.2% in the index of industrial producers' prices during the fourth quarter of last year was followed by another rise of 1.9% in January/February, which lifted it to 6.2% above its corresponding 1969 level. The cost-of-living index rose by 3.5% during the twelve months ending in February.

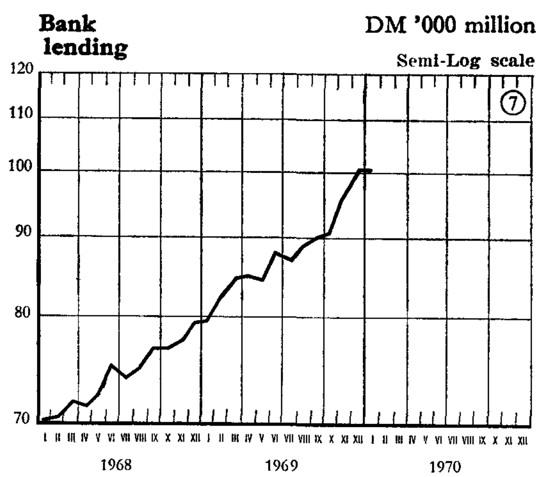


Revaluation, then, did little at first to erode the visible trade surplus, since it improved Germany's terms of trade with the rest of the world and any further expansion of imports came up against limits imposed by the prices and capacity of foreign suppliers. However, sizable deficits developed in other sections of the *balance of payments*. For one thing, revaluation disposed of a great deal of hot money that speculators had previously switched to Germany. Very heavy long-term capital exports during the last few months further swelled the outflow of foreign exchange, for they amounted to about DM 11 700 million between October and January. Not counting the DM 4 100 million by which revaluation reduced the book value of reserves, nor the allocation of special drawing rights in an amount of DM 738 million, the official gold and foreign exchange reserves of the Bundesbank (including the German reserve position with the IMF as well as foreign exchange reserves invested on a longer-term basis) declined by DM 19 500 million between the beginning of October and the end of February. Even so, they still amounted to DM 28 000 million at that date. The net foreign position of commercial banks, in its turn, has deteriorated fairly sharply since revaluation, by close to DM 4 000 million between October and January.



The excess liquidity in the banking system and the economy, which had left little scope for an effective monetary and credit policy, was rapidly re-absorbed after revaluation, partly because of the outflow of foreign exchange and partly because of cash withdrawals—some very heavy—linked with the cash transactions of the authorities. Thus the banks' liquidity ratio (available liquid assets as a proportion of deposits) had, by the end of February, plummeted to an estimated 6%, compared with 11% last summer. In these circumstances the banks were on several occasions compelled to procure funds abroad.

At the same time the expansion of bank credit gathered momentum, not only because firms found themselves short of funds after revaluation, but also because self-financing margins were narrower. Free market forces tended to strengthen restrictions, with severely adverse results for the money and capital markets. In addition, domestic interest rates now became more susceptible to the pressure of high rates of interest abroad.



Demand for and supply of goods and services

	1967 [1]	1968 [1]		1969 [1]		1970 [2]
	At current prices (in DM '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume [4]
Exports [3]	110.5	+ 13.4	+ 12.5	+ 11.9	+ 13.8	+ 6
Gross fixed asset formation	114.4	+ 8.0	+ 9.0	+ 12.8	+ 17.7	+ 8½
Public current expenditure on goods and services	81.0	— 0.9	+ 3.3	+ 4.1	+ 11.4	+ 5
Private consumers' expenditure	284.2	+ 4.0	+ 5.9	+ 7.7	+ 10.3	+ 7
Gross national product	494.6	+ 7.2	+ 8.9	+ 8.0	+ 11.6	+ 5
Imports [3]	94.3	+ 14.7	+ 12.8	+ 16.2	+ 18.8	+ 13½

[1] Federal Statistical Office, "Wirtschaft und Statistik", No. 2/1970.
[2] Commission forecasts.
[3] Goods, services and factor income.
[4] At preceding year's prices.

Note :
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts of the member countries but are established and published on the sole responsibility of the Commission.

2. Outlook

The future course of *export demand* is difficult to predict for a number of important reasons. Revaluation has certainly removed the attraction of speculative excess and opened the way for a return to more normal export developments. But it does not look as though Germany's competitive position has as yet suffered any drastic deterioration, notably because, in view of the preceding spot and forward rates on the foreign exchange market and of the removal of the 4% border taxes, the effective rate of revaluation was not particularly high. The spreading deterioration of world economic conditions, on the other hand, could have severe repercussions on exports, especially if European economies follow the American lead in this respect. For the time being, the weakness of American business conditions is affecting German exports to only a limited extent, because growth is still vigorous in Europe, and more especially in some of the countries of the European Economic Community. In any case, industry's export order-books are so well-filled that heavy exports are bound to continue for the next few months. For the whole of 1970, the increase in monetary terms may well amount to 8%, which, in terms of dollars as reckoned by foreign importers, would mean an increase of about 15%.

It is impossible to predict at this stage whether and to what extent the *propensity to invest* will in fact decline as a combined result of a slackening of export demand and of the much greater difficulties firms will experience in finding funds from self-financing margins or from outside sources. Although the flow of new orders to the capital goods industries has weakened recently, there is much to suggest that investment will remain high for the time being. The order-books of the key capital goods industries were still lengthening recently, and there is still a good deal of follow-up investment to come after last year's investment boom. In addition, continuing pressure on capacity and rising wage costs may well lead to more plant extension and rationalization. Until quite recently, furthermore, many firms placed new construction orders on a considerable scale, which may subsequently lead to corresponding investment in plant and equipment. The fourth quarter's figures for new permits for industrial construction were 35% higher in 1969 than in 1968, and the backlog of orders was also high in other sectors of the building industry.

It may be taken for granted that *private consumers' expenditure* will go on expanding very vigorously. In some sectors incomes have leapt forward since last autumn, and new wage agreements early this year brought wage awards of 9-12%. In view of rising prices, furthermore, the propensity to consume may well go up.

Taking account of present demand trends, including a significant rise in public current expenditure on goods and services, it is estimated that the gross national product will grow by 10% in 1970 (current prices). Allowing for inflation, this would correspond to real growth of around 5%, or slightly more than predicted in the last Quarterly Survey.

On the supply side, a gradual slackening of the overall pressure of demand—which is only now becoming discernible—should make it possible to return to more normal degrees of capacity utilization. But until well into the year, heavy claims will still be made on available resources. *Industrial production* is expected to rise by about 7 ½% for the full year.

Given the demand situation and the improved competitive position of foreign suppliers as a result of revaluation, *imports* may be expected to go on expanding in coming months. The present growth rate, which is high, may well actually increase, especially as regards capital goods and consumer durables.

While there is every likelihood, therefore, that the foreign trade surplus will drop sharply, sizable surpluses will no doubt continue to accumulate on the current external account.

Prices, and more particularly consumer prices, must be expected to go on rising appreciably for some months to come.

During the months ahead, therefore, those responsible for *economic policy* should continue to concentrate on eliminating excess demand as quickly as possible and on stabilizing prices, for if the phase of rising prices lasts too long, this would not only have undesirable structural effects but would jeopardize the maintenance of steady and satisfactory economic growth. Any measures taken to relieve the strain will have to be all the more vigorous the greater the degree by which the income rise exceeds the limit compatible with the requirements of balanced growth. Every care should be taken, however, to choose measures that are both flexible and reversible, so as to leave the way open for a quick policy change in case of need.

In January the Federal Government introduced a stabilization programme, the details of which are described in the Annex, and which follows the line recommended in the Commission's economic policy memorandum, as approved by the Council of Ministers of the European Communities. The main stress is on the restriction of public expenditure and the establishment of a counter-cyclical equalization fund. In the meantime the Länder have followed suit, the idea being not only to "freeze" revenue, but also to block certain expenditures. In these circumstances the public sector (including social insurance) may be expected to achieve a substantial cash surplus. There may be problems in the second half of the year, however, should a spurt in public expenditure occur before enough excess demand has been neutralized. To avoid such a situation, the measures to block expenditures should be maintained and perhaps even tightened up. If new expenditure decisions are taken in a supplementary budget, these should not entail any additional increase in total expenditure. Budgetary decisions should be so co-ordinated that the requirements

The Federal Budget

	1969		1970	1969	1970
	Original budget	Provisional results	Draft [3] budget	Original budget	Draft [3] budget
	DM '000 million			% changes on the preceding year's original budget	
Expenditure [1]	82.6	81.6	88.7	+ 5.8	+ 7.5
of which :					
current expenditure	67.6	67.1	73.8	+ 5.6	+ 9.3
capital expenditure [2]	15.0	14.5	14.9	+ 6.7	— 0.5
Revenue	78.6	83.1	88.7	+ 11.4	+ 12.9
of which :					
direct taxes	19.2	20.9	29.8	+ 9.5	+ 55.4
indirect taxes	55.2	58.2	55.0	+ 13.1	— 0.4
Net borrowing requirement [1]	4.0	— 1.6	0	.	.

[1] Disregarding debt extinction.
[2] Including participations and loans.
[3] Allowing for temporary disinflationary blocking of DM 2 680 million, of which DM 1 260 million current and DM 1 420 million capital expenditure.

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

of counter-cyclical public finance management are satisfied not only by the Federal Government, but also by the Länder and municipal authorities.

Since the Federal Government gave up the idea of a temporary increase in tax rates, an expedient which might also help to ease strain in the economy and especially to stem the overflowing tide of private consumers' expenditure, the Bundesbank imposed heavier restrictions of its own. As of 9 March Bank rate was raised from 6 to 7.5% and the Lombard rate (the rate of borrowing against collateral) from 9 to 9.5%. To prevent the squeeze on bank liquidity being frustrated by recourse to foreign funds, the minimum reserve requirement for new foreign liabilities was raised by 30% with effect from 1 April.

But from the point of view of flexible handling of short-term economic policy and especially of its reversibility, budget and taxation policy should be the main elements in the "policy mix". The additional monetary and credit restrictions may well work too slowly and begin to bite only when the economy is emerging from the stress situation anyway, as a result of the normal working of market forces. Quite apart from that, there is the danger that falling interest rates on major international capital markets may deflect to the Federal Republic flows of long- and short-term funds that for domestic reasons are unwanted.

3. The economic situation in West Berlin

The stimulating effects of last year's generally rising demand did not by-pass West Berlin and there, as in the Federal Republic, growth was very vigorous.

In response to a rapid and large-scale transmission of demand, West Berlin's deliveries to the Federal area increased by no less than 15.3% in 1969, while the overall rate of expansion of visible exports, at 6.3%, fell considerably short of the corresponding figure for the Federal Republic.

The investment boom continues, though, with bad weather in the winter having had a more than average seasonal depressing effect on building investment, gross fixed asset formation owed most to exceptionally high investment in plant and machinery.

Private consumers' expenditure has been growing steadily, though, given the large proportion of pensions in private incomes, less fast than the Federal average. Public current expenditure on goods and services has also expanded briskly, thanks to salary increases in public administration and an increase in the number of persons in paid employment.

Because of the peculiar structure of the Berlin labour market—owing to the decline of the population, it is dependent on an inflow of labour from outside—most of economic growth was attributable to an increase in the productivity of labour. With the real gross product rising by 8% and only a slight increase in numbers employed, the productivity gain was somewhat higher than the Federal average. It would no doubt have been higher still if bad weather had not caused considerable production losses in the Berlin building industry. Be that as it may, the pace of reinforcements to the labour force arriving from West Germany and abroad has quickened very distinctly since 1969. Industrial production rose by 12.5% during 1969.

After a winter which hit the construction industry particularly hard, the city can look forward to vigorous expansion in the coming months. The order situation is very favourable, and a qualitative change in tax preferences may lead to improvements in the production structure.

Major economic policy measures

January

(1) Under a new collective agreement of 15 January 1970 wages and salaries in public administration were raised by 8% with effect from 1 January 1970, coupled with structural improvements and asset-creating benefits at the lower income levels.

(2) A stabilization programme introduced by the Federal Government on 22 January 1970 included the following decisions:

(a) Budget expenditure in 1970 is not to exceed the final expenditure figures for 1969 by more than 8.8%, this limitation to be achieved by a temporary postponement of expenditure in an amount of DM 2 700 million. The funds may be spent later in the year if economic developments warrant it. Until the budget bill is passed by Parliament (probably in May), spending is to be restricted to the preceding year's actual expenditure, except in cases of contrary legislative obligations; between 30 and 40% of departmental estimates for purchases of goods and materials were blocked. The same expenditure policy is to be followed by the Länder and municipal authorities.

(b) The raising of the tax exemption limit for wage and salary incomes to DM 480 per year, twice the previous exemption, is to be postponed until 1 July 1970, and no start is to be made until 1 January 1971 with the gradual reduction of the surcharge on income and corporation tax.

(c) Creation of a counter-cyclical equalization fund through obligatory deposits, until 30 June 1970, of altogether DM 2 500 million, of which DM 1 500 million are to come from the Federal Government and DM 1 000 million from the Länder. Debt extinction does not enter into the computation.

(d) New asset-formation incentives for wage- and salary-earners. Very soon after, on 26 February, a draft law was passed by which the amount of capital allocated to workers as savings free from tax and social contributions was raised from DM 312 ("the DM-312-law") to DM 624.

(e) In order to prevent undue price increases, a sharper watch is to be kept on infringements of anti-monopoly laws. In addition, the Federal Government is to go slow in the present economic situation with any increases in public charges on which it can exert an influence, and is to give more prominence to market principles in setting administrative prices (e.g. by establishing brackets within which fares, etc. can be varied). The Federal Government further announced its intention of taking a critical look at price movements, especially, with a view to a possible reduction in food prices, revaluation having brought down agricultural producers' prices.

(f) With a view to keeping the economy in adequate liquid funds and to stabilizing capital movements, the Federal Government, in agreement with the Bundesbank, intends to abolish the coupon tax on interest from fixed-interest securities in foreign hands, a tax that was introduced in 1965 for foreign exchange and economic policy reasons.

(3) On 23 January 1970 the Federal Government approved the draft budget for 1970 with the revision and extrapolation of the medium-term finance plan until 1973. The total budget for 1970 comes to DM 91 400 million. According to the medium-term finance plan, Federal expenditures are to rise by 7.1% in 1971, by 6% in 1972 and by 7.3% in 1973.

February

Parliamentary approval, on 27 February 1970, of the Government's proposal for an 8% linear rise in civil service salaries as well as for structural improvements for those in lower-paid jobs and for pensioners, to take effect retroactively as of 1 January 1970. The additional expenditure involved for 1970 will be around DM 1 200 million.

March

With effect from 9 March 1970 the Bundesbank raised Bank rate from 6 to 7.5% and the Lombard rate from 9 to 9.5%. In order to make sure that the squeeze on bank liquidity was not going to be frustrated by the banks raising too much money abroad, the minimum reserve requirement for new foreign liabilities was raised by 30% with effect from 1 April 1970.

TABLE 1 : **Key indicators**

	1965	1966	1967	1968	1969	1969
	% change by volume on preceding year					1963 = 100
Gross national product	5.6	2.9	− 0.3	7.2	8.0	134
Industrial production	7.3	2.5	− 2.4	9.5	10.4	141
Total imports	14.2	2.6	− 1.3	14.7	16.2	172
Private consumers' expenditure	6.7	3.7	0.6	4.0	7.7	131
Public current expenditure on goods and services	4.8	2.1	3.3	− 0.9	4.1	113
Gross fixed asset formation	4.6	0.9	− 8.4	8.0	12.8	132
Total exports	7.5	10.7	8.5	13.4	11.9	181
Gross national product per head of population	4.3	1.8	− 0.7	6.6	6.6	126
Gross national product per person in employment	4.9	3.2	2.7	2.7	6.0	134
	% change by value on preceding year					
Gross income per employee	8.9	7.5	3.4	6.5	9.7	153

TABLE 2 : **Indicators for internal and external equilibrium**

	1965	1966	1967	1968	1969
Balance exports less imports					
in million u.a.	− 135	+ 1 613	+ 4 063	+ 4 063	+ 3 906
as percentage of GNP	− 0.1	1.3	3.3	3.3	2.5
Unemployment rate	0.5	0.6	1.7	1.2	0.7
prices to private consumers (% change on preceding year)	+ 3.2	+ 3.5	+ 1.7	+ 1.8	+ 2.5

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					1963 = 100	Million u.a.	% of totals
	1964	1965	1966	1967	1968	1968	1968	1968
Visible exports								
Total	10.9	10.3	12.5	8.0	14.3	170	24 843	100.0
Intra-EEC	8.4	6.7	16.0	9.4	16.7	171	9 340	37.6
To non-EEC countries	12.5	12.4	10.6	7.2	12.9	169	15 503	62.4
Exports of food, beverages and tobacco								
Total	20.5	25.0	− 2.0	26.9	21.8	228	658	2.6
Intra-EEC	22.1	22.6	6.6	61.2	32.8	341	379	1.5
To non-EEC countries	19.5	26.6	− 7.3	2.6	9.4	157	279	1.1
Exports of raw materials, fuel and power								
Total	1.1	3.4	7.1	1.3	10.7	126	1 569	6.4
Intra-EEC	− 1.1	4.1	8.5	1.5	10.6	125	957	3.9
To non-EEC countries	4.5	2.3	5.0	0.4	11.5	126	612	2.5
Exports of semi-finished and finished industrial goods								
Total	11.7	10.1	13.8	6.6	15.9	173	22 615	91.0
Intra-EEC	9.3	5.3	18.9	4.7	21.6	175	8 004	32.2
To non-EEC countries	12.8	12.7	11.3	7.6	13.0	172	14 611	58.8
Visible imports								
Total	12.2	19.6	3.2	− 3.7	16.1	155	20 150	100.0
Intra-EEC	17.4	30.7	4.2	− 1.0	21.7	193	8 359	41.5
From non-EEC countries	9.7	13.6	2.5	− 5.4	12.5	136	11 792	58.5
Imports of food, beverages and tobacco								
Total	8.3	21.6	2.4	− 4.2	3.7	134	3 712	18.4
Intra-EEC	9.3	28.0	6.8	0.1	11.9	167	1 613	8.0
From non-EEC countries	7.8	18.1	− 0.1	− 6.9	− 1.9	116	2 099	10.4
Imports of raw materials, fuel and power								
Total	16.4	4.6	2.8	− 0.6	15.8	144	5 190	25.8
Intra-EEC	16.8	8.3	8.1	9.4	18.1	177	970	4.8
From non-EEC countries	16.4	3.9	1.8	− 2.5	15.3	138	4 420	21.0
Imports of semi-finished and finished industrial goods								
Total	11.6	27.2	3.6	− 5.0	21.1	169	11 429	55.8
Intra-EEC	20.3	35.7	2.8	− 3.0	25.4	204	5 776	28.7
From non-EEC countries	5.2	20.0	4.3	− 6.9	16.8	143	5 473	27.1

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production	1968	*118.3*	*119.7*	*123.7*	*122.1*	*123.8*	*131.5*	*126.3*	*135.7*	*133.0*	*131.2*	*139.7*	*139.6*
(1963 = 100)	1969	*138.9*	*141.4*	*143.5*	*142.1*	*146.0*	*146.3*	*144.4*	*150.4*	*145.7*	*147.5*	*157.6*	*153.9*
	1970	*155.5*											
New orders received	1968	*128.2*	*132.3*	*127.0*	*135.2*	*145.5*	*127.4*	*140.9*	*143.2*	*143.9*	*155.0*	*149.7*	*147.8*
(1963 = 100)	1969	*163.0*	*161.6*	*166.7*	*169.7*	*168.0*	*166.1*	*176.6*	*171.9*	*178.2*	*181.5*	*172.8*	*168.9*
	1970	*(170.7)*											
Unemployed	1968	*460.0*	*388.5*	*387.8*	*331.9*	*313.1*	*301.7*	*287.0*	*287.1*	*264.7*	*252.3*	*235.7*	*209.4*
(1 000)	1969	*197.0*	*203.3*	*185.0*	*156.0*	*161.9*	*170.0*	*175.8*	*175.8*	*175.6*	*169.6*	*152.8*	*143.1*
	1970	*136.5*	*112.3*										
Construction : permits for	1968	*43.3*	*48.5*	*19.7*	*47.7*	*43.9*	*40.7*	*42.4*	*45.3*	*45.5*	*43.6*	*42.6*	*44.0*
residential construction	1969	*43.4*	*47.2*	*44.8*	*45.5*	*47.2*	*47.9*	*48.2*	*45.3*	*46.7*	*49.0*	*48.7*	*44.3*
(1 000)	1970												
Private consumers' expen-	1968	*150.2*	*152.9*	*148.9*	*158.5*	*155.1*	*152.1*	*158.7*	*162.1*	*157.5*	*159.5*	*167.9*	*156.1*
diture : department store	1969	*164.1*	*155.7*	*162.3*	*159.4*	*170.6*	*167.7*	*170.1*	*172.0*	*175.4*	*180.8*	*180.3*	*183.6*
turnover (1963 = 100)	1970												
Consumer prices	1968	112.8	112.8	112.9	112.9	112.9	113.1	113.1	112.8	112.9	112.3	113.9	114.3
(1963 = 100)	1969	115.1	115.4	115.5	115.7	115.9	116.2	116.1	115.8	116.1	116.5	117.0	117.6
	1970	119.1	119.3										
Visible imports	1968	*1 530*	*1 618*	*1 606*	*1 638*	*1 686*	*1 504*	*1 829*	*1 686*	*1 674*	*1 833*	*1 732*	*1 694*
(million u.a.)	1969	*1 933*	*1 800*	*1 987*	*2 070*	*2 019*	*2 041*	*2 142*	*1 982*	*2 120*	*2 437*	*2 148*	*2 163*
	1970												
Visible exports	1968	*1 930*	*1 965*	*1 979*	*1 922*	*2 011*	*1 818*	*2 181*	*2 181*	*2 053*	*2 215*	*2 305*	*2 171*
(million u.a.)	1969	*2 069*	*2 156*	*2 245*	*2 402*	*2 380*	*2 427*	*2 559*	*2 437*	*2 457*	*2 794*	*2 616*	*2 495*
	1970												
Balance of trade	1968	*+ 400*	*+ 348*	*+ 373*	*+ 284*	*+ 325*	*+ 314*	*+ 352*	*+ 495*	*+ 379*	*+ 382*	*+ 573*	*+ 477*
(million u.a.)	1969	*+ 137*	*+ 276*	*+ 259*	*+ 332*	*+ 361*	*+ 387*	*+ 416*	*+ 455*	*+ 337*	*+ 357*	*+ 468*	*+ 332*
	1970												
Official gold and foreign	1968	6 486	6 749	7 030	6 842	6 732	6 733	6 721	6 695	6 962	6 665	8 543	7 497
exchange reserves	1969	6 229	6 169	5 926	6 473	9 326	7 738	7 762	8 322	9 664	8 165	6 889	5 679
(million u.a.)	1970	5 951											
Money supply	1968	*83.4*	*82.8*	*83.3*	*83.3*	*83.9*	*84.8*	*84.9*	*85.7*	*86.8*	*86.3*	*87.5*	*88.3*
(DM '000 million)	1969	*89.2*	*89.2*	*90.7*	*90.4*	*91.5*	*92.1*	*93.2*	*94.4*	*94.3*	*93.7*	*95.6*	*94.1*
	1970												

NOTES TO GRAPHS AND TABLES

Source: Statistical Office of the European Communities (except as otherwise indicated).
Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US $ 1) at official exchange rates.

Graph 1

— Exports (fob) : series adjusted for seasonal variations; three-month moving averages.

Graph 3

— Industrial production: trend curve; estimate established on the basis of indices adjusted for seasonal and fortuitous variations, excluding construction, food, beverages and tobacco.

Graph 2

— Labour market: series adjusted for seasonal variations; three-month moving averages; position at end of month.

Graph 4

— Imports (cif) : series adjusted for seasonal variations; three-month moving averages.

Graph 5

— Wages and consumer prices: index of average hourly gross earnings in industry (including construction); cost-of-living index (all households) at middle of month, not adjusted for seasonal variations.

Graph 6

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

Graph 7

— Bank lending: short-term loans to business and private customers within the country; position at end of month, not adjusted for seasonal variations.

Table 1

— Gross national product at market prices.
— Industrial production: value added by industry (including small workshops).
— Total exports and imports: goods, services and factor income.
— Gross income per employee: income from paid employment (including employers' share of social insurance contributions).

Table 2

— Balance exports less imports: as defined for the national accounts.
— Unemployment rate: number of unemployed as percentage of total labour force (annual averages); source: Statistisches Bundesamt and Bundesanstalt für Arbeit.
— Price index: price index of private consumption adjusted by the GNP deflator, computed from the national accounts.

Table 3

— Exports fob, imports cif. The products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST): food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production: adjusted for seasonal variations, excluding construction, food, beverages and tobacco.
— New orders received: manufacturing industry (excluding food, beverages and tobacco); seasonally adjusted value index.
— Unemployed: position at end of month, adjusted for seasonal variations.
— Construction: seasonally adjusted number of dwellings authorized.
— Private consumers' expenditure: seasonally adjusted value index of department store turnovers.
— Consumer prices: cost-of-living index (all households), not adjusted for seasonal variations.
— Imports cif, exports fob; value, adjusted for seasonal variations.
— Balance of trade: difference between values of imports and exports seasonally adjusted.
— Official gold and foreign exchange reserves: gross reserves of gold and convertible currency with Bundesbank at end of month.
— Money supply: notes and coin in circulation (excluding cash holdings of credit institutions) and sight deposits of domestic non-banks (excluding public authorities' deposits with the Bundesbank); seasonally adjusted end-of-month figures.

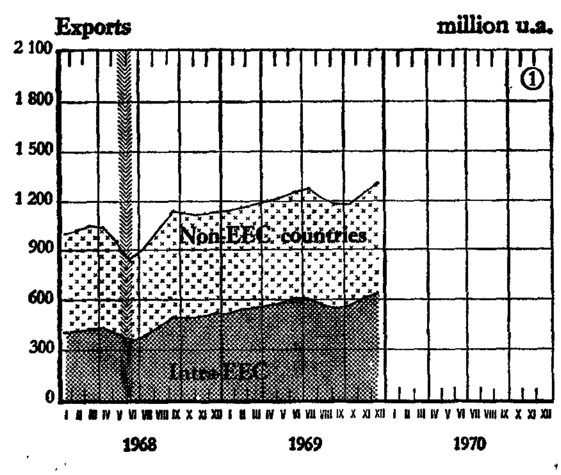
B. France

Last September's recovery programme has already yielded excellent results in some fields. External trade and payments helped the foreign exchange situation to a very substantial improvement. The propensity to save of households is higher, and this has entailed a substantial slowdown of consumption so that the continuing investment boom is being financed on a sounder basis. But the future still holds some threats. Prices are still under heavy upward pressure, and the wage rise does not seem to be slowing down significantly. Hence it is quite likely that private consumers' expenditure may begin to climb again, and this might well jeopardize the consolidation of the external position and thereby considerably narrow the scope for later efforts to lead the French economy into a new phase of strong, balanced and durable growth.

1. Recent developments

Under the impact of the recovery programme launched after the devaluation of the franc and thanks partly to the restoration of stability in the international monetary situation following the revaluation of the mark, equilibrium conditions in the external and domestic economic affairs of France improved during the winter. Most impressive progress was made in the foreign exchange position, both on the trade and the payments accounts. At home, the expansion of the money supply seems to have been curbed. More normal consumption patterns on the part of private households, a lower budget deficit and a severely restrictive monetary policy made it possible to nudge the economy back to financing more of its requirements with funds drawn from real savings. In spite of these encouraging results, the underlying situation is apparently by no means consolidated. As before, the pressure of domestic demand is extremely heavy on certain markets, production and the labour market are under strain and factors tending to force up wages and prices remain strong.

The economy has been slow to release capacities for export work, as is essential if external equilibrium is to be restored on a lasting basis. What is now preventing France from taking full advantage of its better competitive position following the parity changes is not any weakness of foreign demand, but the inadequate production and delivery potential of major industries in the semi-manufactures and capital goods sectors. But French managements do seem to be more anxious to secure foreign business now that exporting is more profitable. Since devaluation, French export prices expressed in francs have been raised by about 8-10% (in terms of average unit values of export). While export developments in the late summer and the autumn months of 1969 almost exclusively reflected price adjustments of this kind, the export volume has now begun to grow in its turn. Expressed in seasonally adjusted dollar

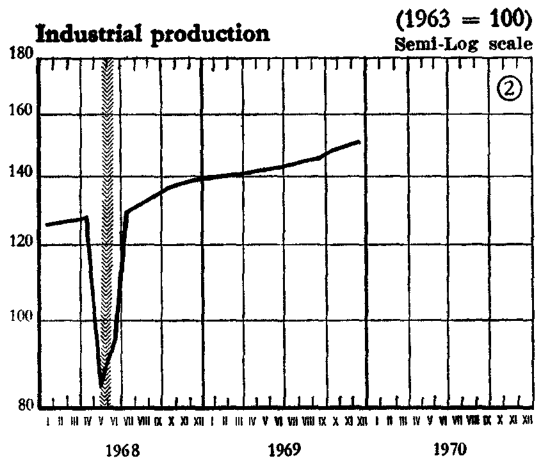


values, exports in January/February 1970 were 7% higher than in June/July 1969, and 16% higher than in January/February 1969.

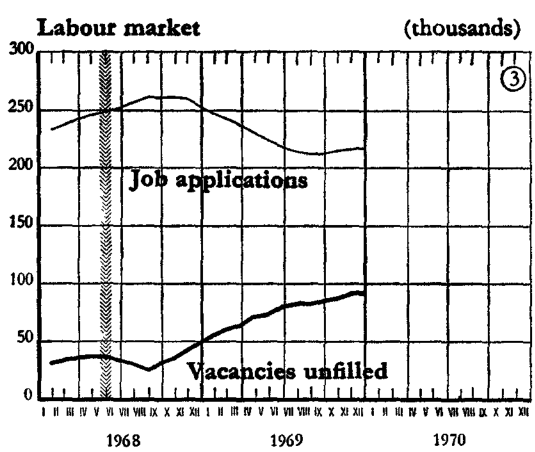
The combination of exceptionally favourable export conditions, continued capacity shortage at home and businessmen's continuing expectations that price inflation will go on seems to have been the main determinant of private investment decisions during the last few months. At all events, replies to last November's INSEE investment survey suggested that industrial expenditure both for construction and for plant and machinery was still going to expand vigorously around the turn of the year and early in 1970.

On the other hand, the propensity to consume of households, which had been too strong until the summer months, is now weaker; private consumers' expenditure probably rose very little from the third to the fourth quarter of 1969, and there is evidence that consumers were still holding back early this year. Yet the growth of gross incomes, and especially of wage incomes, has not lost momentum. The total number of hours worked has been rising steadily, and hourly wage rates rose even faster during the last quarter of 1969 (by 2.4% in private trade and industry) than the 2% average of the preceding three quarters. There are a number of reasons for the divergent course of consumption and incomes during the last few months. Households had exceptionally heavy tax bills to meet at the end of 1969 since the balance of the 1968 liability was due for settlement; hire-purchase restrictions were tightened up; confidence in the franc having been restored, former savings habits were resumed, and the new savings incentives may well have begun to "bite".

But although private consumers' expenditure has reverted to a much steadier pace, domestic supply and demand are still out of step. In the consumer goods industries, it is true, the intake of new orders is tending to slow down and order books are shortening, so that capacity is less fully stretched and production is expanding noticeably less fast. But the basic materials and capital goods industries are still hampered by bottlenecks and are finding it difficult to meet delivery dates. In all, industrial production has been rising in recent months at a steady annual rate of about 6 to 7%.

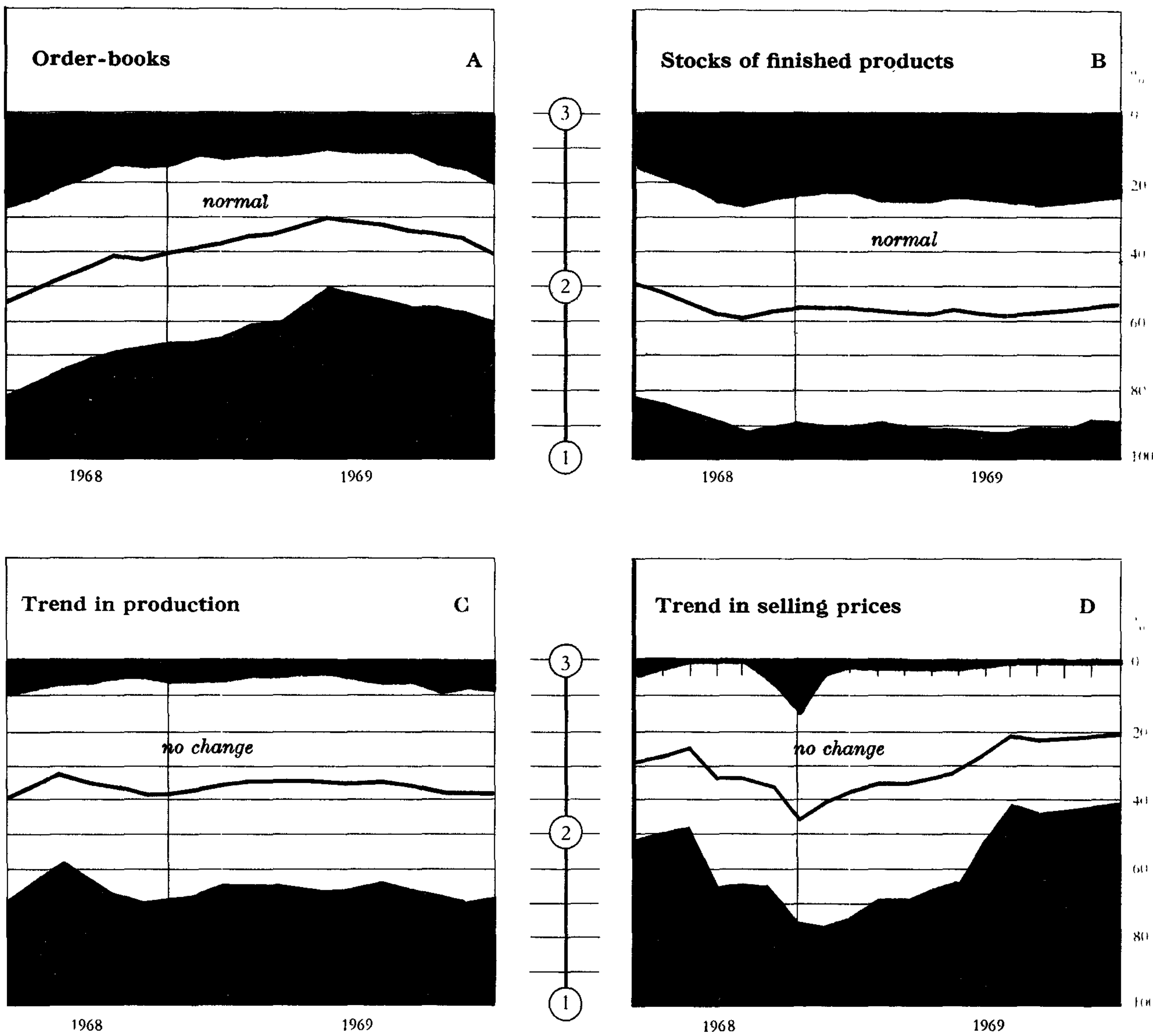


Given the rate of progress of productivity and appreciable cuts in the working week, output growth could obviously not have been maintained without additional workers. In seasonally adjusted figures the number of persons in paid employment in industry and commerce rose by no less than 0.5% during the last quarter of 1969, and on 1 January 1970 was more than 2% higher than twelve months earlier. Job applications did not, however, decline any further. It looks as though such unemployment as still exists is a hard core, about which, at any rate for the time being, nothing can be done. The skills possessed by new recruits to the labour force fall short of requirements. As against that, immigration of foreign workers speeded up. Job vacancies were running at a record level in January 1970.



Imports during the last few months largely reflected the impact of devaluation. Speculative purchases of raw materials and semi-manu-

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



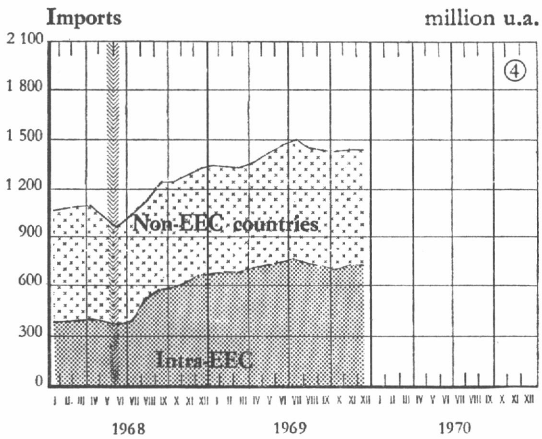
Answers to questions in the EEC business survey, carried out in France by INSEE.

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

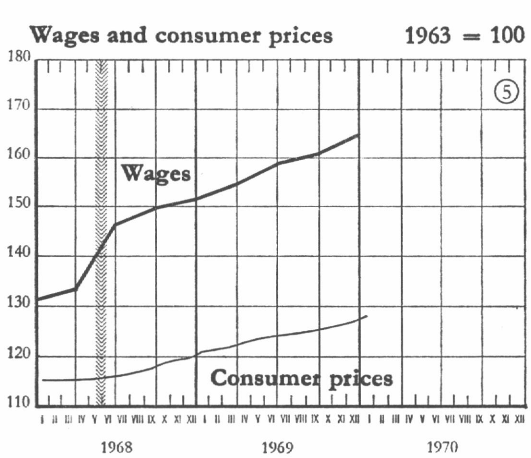
The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

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".

factures came to a halt, and imports of consumer goods were adjusted to a change in the consumption pattern of households. In terms of average unit values, the franc prices of imports have risen by 14 to 16% since June/July 1969, and their volume dropped; in January/February 1970 it was 7% lower (in seasonally adjusted figures) than in June/July 1969.

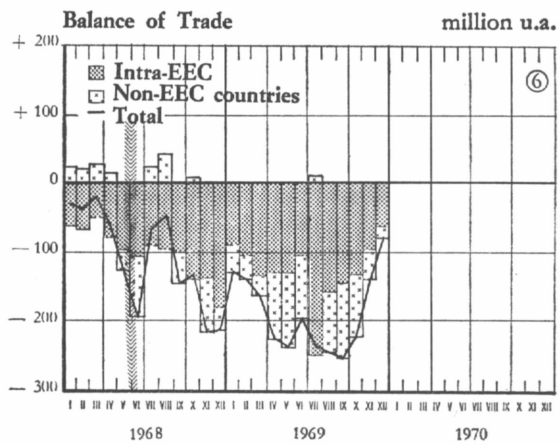


No relief is yet apparent in the price situation. Demand pull remains strong, and the cost push has, if anything, been growing stronger more rapidly. In particular, labour costs per unit of output have risen, and imported raw materials and producer goods are dearer not only because of devaluation but also because of world-wide inflationary pressures. The fact that in the given conditions of the market these cost increases have not so far been more fully reflected in the domestic price level is largely explained by strict official price controls. Nevertheless, industrial producer prices probably



rose during the last few months at the quicker pace of something like 6% in annual terms. Consumer prices, according to the INSEE index of 259 items, increased by 2.2% from September to January, and at the beginning of 1970 were 5.6% higher than a year earlier.

But while the domestic economy still has a long way to go before it reaches a new equilibrium, a prompt and substantial improvement has taken place in the external balance. The visible trade account has tended to improve, the leads and lags effect now favours France and the capital account reflects sizable flows of funds returning from abroad. The net foreign-exchange position of the monetary authorities is thought to have improved by at least $200 million during the last quarter of 1969. In January the official gross gold and foreign exchange reserves rose by $52 million, although more than $410 million of short-term foreign credits were repaid during the same month.



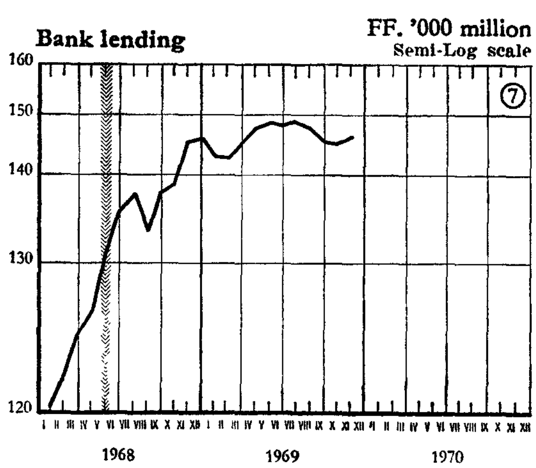
In spite of this net inflow of foreign exchange, the expansion of domestic liquidity slowed down distinctly around the turn of the year. The money supply stopped rising more than very slightly. The main restrictive factor was budget management; the cash deficit, which exceeded FF 8 000 million at the end of August, had come down to about FF 3 500 million by the end of the year and debts to the banking system had been much reduced. At the same time credit restrictions sharply curtailed the expansion of short-term credit. At the end of December 1969 the total volume of credit outstanding to business and private customers was no more than 10% higher than a year earlier, compared with a corresponding 16% or so around the middle of the year.

Demand for and supply of goods and services

	1967 [1]	1968 [1]		1969 [2]		1970 [3]
	At current prices in FF '000 million	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports [4]	82.4	+ 7.8	+ 8.2	+ 15	+ 21½	+ 13
Gross fixed asset formation	144.0	+ 5.2	+ 8.0	+ 9½	+ 16½	+ 6
Public current expenditure on goods and services	70.5	+ 5.2	+ 13.0	+ 4½	+ 12½	+ 2½
Private consumers' expenditure	345.9	+ 5.0	+ 10.0	+ 7½	+ 14½	+ 4
Gross national product	572.4	+ 4.2	+ 9.3	+ 8½	+ 15½	+ 4½
Imports [4]	80.2	+10.6	+ 11.1	+ 19	+ 25	+ 5½

[1] *Source :* Statistical Office of the European Communities.
[2] Commission estimates.
[3] Commission forecasts.
[4] Goods, services and factor income.

Note :
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, worked out by the Commission and generally mentioned in the Quarterly Surveys. They have been discussed with the experts from the member countries but are established and published on the sole responsibility of the Commission.



The usual seasonal easing of conditions on the money market after the New Year was hardly noticeable in 1970. Interest rates remained exceptionally high, partly because the Banque de France continued to relate its interventions to balance-of-payments requirements. On the capital market, new issues have been coming out at a lively pace recently, with first class industrial bonds carrying a coupon of up to 8.75%.

2. Outlook

Despite satisfactory achievements in some fields since the introduction of the recovery programme, there are still certain threats to the further consolidation of internal and external balance. Price and income trends, the consumption potential of households and a possible slowdown in the expansion of export demand are the main dangers.

It is true that, although business activity in the United States is slackening, export demand is likely to go on expanding vigorously for some months, mainly because inflation will continue in most of the member countries. Given the considerably improved competitive position of France, exports will no doubt grow fast, or at any rate as fast as the delivery capacity of firms permits. The outlook for later in the year is, however, rather more uncertain. There is every possibility that export demand will weaken as domestic economic conditions gradually settle and return to normal in countries accounting for the bulk of world trade.

At the moment, however, export growth is still exerting so great an influence on the propensity to invest of industry that gross fixed asset formation is bound to go on rising for most of the current year, especially since orders in hand for new construction and for plant and machinery are still increasing and since certain deadlines must be met if firms are to qualify for temporary tax reliefs. The replies to last November's INSEE business survey suggest that investment expenditure by private industry will be 19% higher in 1970 than in 1969. It is true that narrowing profit margins and the restrictions on bank credit may begin to affect the liquidity position of firms, but there still seems ample scope for recourse to other sources of finance. The domestic capital market is most responsive to new claims upon it, and foreign assets can be repatriated on a larger scale.

In any event, the crucial factor for equilibrium in France this years is private consumers' expenditure. The trend of incomes suggests that consumption will rise quite fast. Overall wage incomes, in particular, can hardly be expected to go up any less quickly than they have done so far, given the size of pending wage claims, the continuing strain on the labour market and the steady increase in employment. Other types of income are also expected to improve and the burden of direct taxation, though it will remain heavy, will be relatively a little less onerous, so that the disposable income of households as a whole will probably go on rising for some months at least as fast as at the end of 1969 and early this year. The future course of consumption will therefore be largely a function—inverted—of the trend of private saving. This trend is hard to predict at this stage. It may well be that the early successes of the recovery programme will lead households to replenish depleted savings, in which case consumption will settle down to a slower rate of expansion in the coming months. Other evidence, however, not least the results of the INSEE consumer survey in January/February, suggests that in the expectation of further price rises households, which have been saving more since the autumn of 1969, will stop increasing the sums retained for this purpose; and in that case private consumers' expenditure is in for another phase of faster expansion.

For all the uncertainties which at present surround the future of private consumption, it can be taken for granted that overall demand will expand enough to keep industrial production growing in the months immediately ahead. In some sectors like basic materials, capital goods, and consumer goods for export, where order-books are long anyway, growth should be particularly brisk. This does not mean that firms may not find themselves working a little below capacity, for technical capacity is now being extended under major investment programmes.

Given the outlook for overall demand and domestic production it must be assumed that the volume of imports will cease to contract (the declining trend dates from devaluation) and will begin to expand again. But exports are so dynamic that the visible trade balance will no doubt go on improving for some time and yield sizable surpluses around the middle of 1970.

The present and future movements of prices are still a matter of great concern. Domestic prices can hardly be studied without reference to the world-wide inflationary pressures arising because monetary demand exceeds real supply potential nearly everywhere. But France has special problems which might force prices up rapidly in the coming months. For one thing, strict price control has caused distortions in the price structure which must sooner or later be corrected if optimum factor utilization is not to be lastingly prejudiced. Secondly, sizable increases in the prices of agricultural products are impending, in connection with the commitment to re-establish a fully functioning common agricultural market. Another factor is that

The Central Government Budget

	1969		1970	1969	1970
	Original budget	Revised budget	Budget	Original budget	Budget
	FF '000 million			% changes on the preceding year's original budget	
Expenditure [1]	153.8	155.7	162.6	+ 16.8	+ 5.7
of which :					
current exependiture	128.6	130.4	138.6	+ 18.9	+ 7.8
capital expenditure [2]	25.2	25.3	23.9	+ 2.1	— 5.2
Revenue	147.4	152.2	162.6	+ 13.7	+ 10.3
of which :					
direct taxes	40.8	44.8	49.7	+ 12.8	+ 21.9
indirect taxes	91.9	93.2	97.8	+ 12.0	+ 6.4
Net borrowing requirement [1]	6.4	3.5	0	.	.

[1] Disregarding debt extinction.

[2] Including participations, advances and loans.

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

charges in the public sector will have to be raised steeply again if management is to be rational in the longer run. Finally rising costs, especially wage costs, will have an increasingly important impact on prices in the next few months. All in all it cannot be expected that the rise in consumer prices will flatten out before the middle of the year, at the very earliest.

Given the outlook and the dangers ahead, those in charge of economic policy have no option but to maintain for the time being the restrictions applied since last autumn through an effective combination of many separate measures. Such external balance as has been achieved can be consolidated only by a speedy return to internal equilibrium. Unless the expansion of domestic demand and the price rise are contained very soon and to lasting effect, the external position will remain precarious and considerably narrow the scope of later efforts to lead the French economy into a new phase of strong, balanced and durable growth.

In these circumstances, the budget should be so administered as to concentrate the restrictive effects built into the finance law for 1970 in the first half of the year, and to prevent the utilization of unexpended appropriations for 1969 putting additional strains on cash transactions. Tax revenue is bound to exceed estimates, because of the larger than expected increase in taxable incomes and turnover, and this surplus should be used for a further reduction of the Treasury deficit, which would allow of speedier redemption of debts to the banking system.

Budget management along these lines would have the additional merit of helping to offset the tendency for an improvement in the balance of payments to increase domestic liquidity, especially if the return flow of short-term capital continues. Certainly there is no strong case as yet for a relaxation of the credit squeeze. So long as the risk of a considerable—and in present circumstances premature—re-expansion of private consumers' expenditure has not been removed, the difficulties which some firms may experience in financing heavy increases in investment expenditure do not constitute sufficient reason for a general relaxation of monetary and credit policy at this stage.

Only if it is established in the later part of the year that internal and external equilibria have been restored on sufficiently sound bases might there be a case for a policy adjustment designed to set the economy once again along the road towards brisk and lasting growth. To this effect the authorities dispose of instruments for rapid intervention, such as the power to "unfreeze" appropriations earmarked for public capital spending in the "economic contingency fund" and the possibility of granting further reliefs in the field of indirect taxation, a move which would help to keep prices down.

Major economic policy measures

January

(1) Entry into force of new rules on the statutory minimum wage (SMIG) approved early in December by the National Assembly. As of 1 January, some 750 000 (out of a total of 15.5 million) wage-earners get instead the so-called "minimum growth wage" (SMIC), which is no longer linked solely to the index of consumer prices (with immediate adjustment to any price rise of 2% or more) but also to average hourly wage rates in industry and commerce (annual adjustment in July by at least half the shortfall compared with the general wage rise).

(2) The Government decides to introduce in 1970 a new system to replace the "Toutée procedure", by which wages in the public sector had so far been determined (the Government fixing a total wage bill for each public undertaking every year, leaving the management free to distribute this total among separate wage categories at its discretion and in agreement with the appropriate unions). Now, for example, a kind of productivity contract (*convention sociale*) has been concluded with the State electricity and gas corporations (Electricité de France and Gaz de France)—despite the vigorous opposition of many workers. This contract is valid for two years and combines certain restraints on the right to strike with automatic wage increases geared to the increase in the gross domestic product at current prices, company turnover and cuts in running costs.

(3) To encourage saving for home ownership, new incentives are introduced. The present "building savings accounts" are made more attractive (interest rates, etc.) and a new system is started called "building savings plan", under which special advantages are offered for contractual saving of at least FF 1 200 per year for four years (tax-free interest of 4%, a bonus of 4% on the accumulated capital sum and, after certain time-limits, allocation of low-interest building loans up to FF 100 000).

(4) With effect from 1 January sharp reduction, from 17.6 to 6.5%, of TVA rates on certain food products and books. The resulting loss of revenue is estimated at close to FF 1 000 million for 1970, which has to be added to a shortfall of the same order of magnitude already budgeted for in the Finance Act for 1970 in consequence of a general simplification of TVA rates.

(5) A number of charges in public services were raised at the beginning of the year, notably fares and freight rates on railways, Paris transport and postal charges. In addition, considerable price increases were authorized for important raw materials and producer goods (coal, steel, nickel, etc.).

(6) Further liberalization of imports from communist countries, together with sizable quota increases under new trade agreements with Poland, Hungary, Rumania, Bulgaria and East Germany.

(7) In mid-January the Government asked local authorities not to increase their expenditure for the fiscal year 1970 by more than 6.25%.

(8) The Conseil National du Crédit decides that the hire-purchase restrictions introduced on 28 August 1969 as part of the recovery programme are to be extended beyond 31 January, subject to the slight concession that the maximum duration of consumer credit for the purchase of passenger cars and station wagons, of household appliances and machines and of furniture is raised from 15 to 18 months; no change was made in the existing regulations concerning the deposit (50% for motor-cars, 40% for household machines and furniture 20-30% for radio and TV sets).

February

(1) The Banque de France is given better institutional means of controlling the expansion of credit by commercial banks to business and private custome
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non-interest-bearing

(2) In mid-Februar
Caisse nationale de ... sed
a little so as to enable ... more medium- and long-term investment credits to farmers in certain structurally weak areas.

(3) In mid-February the Government announced a number of measures to facilitate export business. These involve better terms for export credit and guarantees, relaxation of exchange control for exporters and incentives for the creation and extension of sales networks, service stations, etc. abroad.

TABLE 1 : **Key indicators**

	1964	1965	1966	1967	1968	1968
	% change by volume on preceding year					Indices 1963=100
Gross national product	+ 6.6	+ 4.7	+ 5.6	+ 4.8	+ 4.2	127
Industrial production	+ 8.5	+ 5.1	+ 7.6	+ 4.4	+ 4.2	134
Total imports	+ 12.8	+ 3.4	+ 13.7	+ 7.1	+ 10.4	157
Private consumers' expenditure	+ 5.6	+ 4.4	+ 4.7	+ 4.8	+ 5.0	127
Public current expenditure on goods and services	+ 3.6	+ 2.7	+ 2.7	+ 3.6	+ 5.2	119
Gross fixed asset formation	+ 13.8	+ 7.2	+ 8.9	+ 5.7	+ 5.2	148
Total exports	+ 8.0	+ 11.8	+ 8.2	+ 6.6	+ 7.5	150
Gross national product per head of population	+ 5.4	+ 3.7	+ 4.7	+ 3.9	+ 3.4	123
Gross national product per person in employment	+ 5.3	+ 4.3	+ 4.8	+ 4.4	+ 4.4	125
	% change by value on preceding year					
Gross income per employee	+ 8.6	+ 6.6	+ 6.2	+ 6.2	+ 11.2	145

TABLE 2 : **Indicators for internal and external equilibrium**

	1964	1965	1966	1967	1968
Balance exports less imports					
in million u.a.	– 26	+ 1 012	+ 353	+ 420	– 8
as percentage of GNP	0	+ 1.0	+ 0.3	+ 0.4	0
Unemployment rate	1.1	1.3	1.4	1.8	2.1
consumer prices (% change on preceding year)	+ 3.4	+ 2.5	+ 3.0	+ 2.8	+ 4.7

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					Indices 1963=100	Million u.a.	% of totals
	1964	1965	1966	1967	1968	1968	1968	1968
Visible exports								
Total	+ 11.3	+ 11.8	+ 8.3	+ 4.5	+ 11.4	157	12 672	100.0
Intra-EEC	+ 12.8	+ 18.0	+ 12.0	+ 2.0	+ 16.0	176	5 452	43.0
To non-EEC countries	+ 10.3	+ 7.8	+ 5.8	+ 6.3	+ 8.2	145	7 220	57.0
Exports of food, beverages and tobacco								
Total	+ 14.4	+ 11.4	+ 7.5	+ 2.9	+ 19.8	169	2 118	16.7
Intra-EEC	+ 16.6	+ 26.3	+ 19.4	+ 6.0	+ 26.6	236	1 127	8.9
To non-EEC countries	+ 13.0	+ 2.0	− 2.0	− 1.0	+ 12.8	127	991	7.8
Exports of raw materials, fuel and power								
Total	+ 9.7	+ 4.4	+ 7.3	− 3.7	+ 1.6	120	1 125	8.9
Intra-EEC	+ 19.1	+ 8.9	+ 7.4	− 3.7	+ 0.9	135	679	5.4
To non-EEC countries	− 1.1	− 1.8	+ 7.2	− 3.6	+ 2.6	103	446	3.5
Exports of semi-finished and finished industrial goods								
Total	+ 10.8	+ 13.2	+ 8.7	+ 6.1	+ 11.1	160	9 429	74.4
Intra-EEC	+ 10.4	+ 18.3	+ 11.2	+ 2.3	+ 16.2	173	3 646	28.8
To non-EEC countries	+ 11.1	+ 10.3	+ 7.2	+ 8.5	+ 8.1	153	5 783	45.6
Visible imports								
Total	+ 15.4	+ 2.7	+ 14.6	+ 4.5	+ 12.5	160	13 927	100.0
Intra-EEC	+ 20.4	+ 6.7	+ 20.8	+ 10.7	+ 23.1	212	6 617	47.5
From non-EEC countries	+ 12.6	+ 0.3	+ 10.5	+ 0.2	+ 4.4	131	7 310	52.5
Imports of food, beverages and tobacco								
Total	+ 14.9	− 0.5	+ 8.4	− 2.6	+ 2.7	124	1 921	13.8
Intra-EEC	+ 26.2	+ 8.9	+ 1.3	+ 16.6	+ 31.8	214	588	4.2
From non-EEC countries	+ 12.5	− 2.8	+ 10.3	− 7.4	− 6.4	104	1 333	9.6
Imports of raw materials, fuel and power								
Total	+ 7.1	+ 0	+ 5.9	+ 0.3	+ 3.6	118	3 633	26.1
Intra-EEC	+ 3.7	− 5.0	+ 9.5	− 2.3	+ 14.2	120	603	4.3
From non-EEC countries	+ 7.7	+ 0.9	+ 5.3	+ 0.8	+ 1.7	117	3 030	21.8
Imports of semi-finished and finished industrial goods								
Total	+ 21.8	+ 5.6	+ 22.0	+ 9.0	+ 19.6	205	8 373	60.1
Intra-EEC	+ 23.2	+ 8.6	+ 25.0	+ 11.9	+ 23.3	231	5 426	39.0
From non-EEC countries	+ 19.9	+ 1.5	+ 17.6	+ 4.3	+ 13.3	169	2 947	21.1

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1968	127.1	126.5	129.2	128.2	86.1	94.7	130.2	129.7	132.1	138.9	140.2	142.2
	1969	144.1	140.5	139.9	143.0	142.8	133.8	144.4	135.4	143.7	146.0	144.2	150.8
	1970												
Number of persons seeking employment (1 000)	1968	237.5	243.6	247.4	247.7	249.1	265.9	260.0	262.1	263.5	260.8	253.5	246.3
	1969	242.7	237.9	231.7	224.4	220.3	213.3	214.6	215.6	216.1	218.4	217.6	219.9
	1970												
Construction: building permits issued for housing (1 000)	1968	42.0	38.5	42.4	39.7	41.3	44.5	46.3	52.1	41.0	54.4	52.8	65.8
	1969	48.5	44.2	44.1	44.9	48.5	51.9	56.2	50.6	52.2	53.6		
	1970												
Private consumers' expenditure: turnover of department stores (1963 = 100)	1968	127.1	128.0	129.8	124.5	89.9	123.8	142.7	143.7	134.8	141.2	161.6	143.0
	1969	146.4	139.4	143.2	139.3	151.1	138.9	146.8	154.9	136.7			
	1970												
Consumer prices (1963 = 100)	1968	114.9	115.0	115.1	115.4	115.8	116.2	116.6	117.1	117.9	119.1	119.5	119.8
	1969	121.1	121.5	122.1	122.7	123.2	123.6	124.2	124.5	125.1	125.9	126.5	126.9
	1970	128.0											
Visible imports (million u.a.)	1968	1 086.9	1 102.8	1 097.9	1 101.3	909.5	917.8	1 307.5	1 205.1	1 227.4	1 315.4	1 348.0	1 342.9
	1969	1 362.7	1 317.0	1 325.9	1 492.7	1 475.2	1 484.2	1 554.8	1 300.0	1 446.9	1 540.9	1 376.2	1 435.3
	1970												
Visible exports (million u.a.)	1968	1 055.4	1 065.5	1 077.8	1 039.6	788.3	721.6	1 242.6	1 157.1	1 082.0	1 186.8	1 134.0	1 132.4
	1969	1 235.2	1 179.0	1 167.1	1 265.3	1 231.8	1 287.0	1 312.2	1 049.9	1 188.8	1 319.3	1 238.9	1 357.0
	1970												
Balance of trade (million u.a.)	1968	− 31.5	− 37.3	− 20.1	− 61.7	− 121.2	− 196.2	− 64.9	− 48.0	− 145.4	− 128.6	− 214.0	− 210.5
	1969	− 127.5	− 138.0	− 158.8	− 227.4	− 243.4	− 197.2	− 242.6	− 250.1	− 258.1	− 221.6	− 137.3	− 78.3
	1970												
Official gold and foreign exchange reserves (million u.a.)	1968	6 053	6 014	6 023	6 027	5 720	5 517	4 850	4 601	4 374	4 265	3 985	4 200
	1969	4 215	4 125	3 986	3 774	3 636	3 610	3 594	3 781	4 006	3 913	3 989	3 832
	1970	3 885	3 950										
Money supply (FF '000 million)	1968	192.3	193.1	193.1	193.6	207.6	207.0	203.0	204.3	207.9	209.0	209.7	211.5
	1969	209.1	210.9	213.0	215.9	213.8	216.1	216.0	215.3	216.6	214.1	214.4	
	1970												

NOTES TO GRAPHS AND TABLES

Source : Statistical Office of the European Communities (except as otherwise indicated). Conversion into units of account (1 u.a. = 0,888671 g of fine gold = US $ 1) at the official exchange rate.

Graph 1

— Exports fob. Series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Industrial production : trend curve; estimate established on the basis of indices of the Statistical Office of the European Communities (excluding construction, food, beverages and tobacco), adjusted for seasonal and fortuitous variations.

Graph 3

— Labour market; series adjusted for seasonal variations, three-month moving averages; position at end of month.

Graph 4

— Imports cif. Series adjusted for seasonal variations; three-month moving averages.

Graph 5

— Wages and consumer prices; index of hourly wage rates, all activities, all regions; national index of consumer prices (259 items).

Graph 6

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

Graph 7

— Bank lending; Source : Conseil National du Crédit; short-term loans (up to 2 years) from monetary institutions to business and private customers; end of period figures.

Table 1

— GNP at market prices (new series on 1962 basis).
— Industrial production: value added by industry.
— Total exports and imports: goods, services and factor income.
— Gross income per employee: income from paid employment (including employers' share of social insurance contributions).

Table 2

— Balance exports less imports: as defined for the national accounts.
— Unemployment rate: number of unemployed (persons available for and seeking employment, estimated on the basis of the number of job applicants, in the light of the latest population census) as percentage of the total domestic labour force; source: INSEE.
— Consumer prices: implicit price index of private consumption computed from the national accounts.

Table 3

— Exports fob, imports cif; the products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST): food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production: adjusted for seasonal variations, excluding construction, food, beverages and tobacco.
— Number of persons seeking employment: seasonally adjusted figures, position at end of month.
— Construction: seasonally adjusted number of dwellings authorized.
— Private consumers' expenditure: seasonally adjusted indices of department store turnovers, constant samples.
— Consumer prices: national index of 259 items.
— Imports cif, exports fob, adjusted for seasonal variations.
— Balance of trade: difference between seasonally adjusted imports and exports.
— Official gold and foreign exchange reserves: gross reserves of gold and convertible currency held by the Banque de France and the Fonds de Stabilisation des changes at the end of month.
— Money supply: fiduciary circulation (total notes and coin in circulation, excluding notes and coin held by the Banque de France) plus sight deposits (deposits made with the Banque de France by private persons or enterprises, deposits with the Post Office giro or with public accountants, plus sight deposits relating to the activities of the banks within metropolitan France. Seasonally adjusted prices, at end of month.

C. Italy

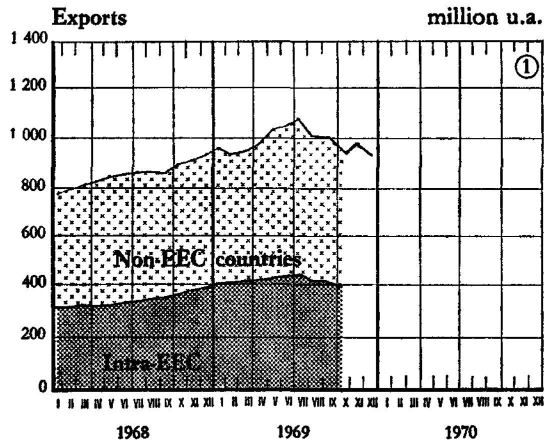
In Italy, strikes and wage awards were the main factors affecting the economic trend around the turn of the year. Labour conflicts curbed both demand and production and the rate of growth of industrial production for the year 1969 as a whole dropped to a shade under 3 ½%, more than 4 percentage points below original forecasts. There was still an underlying upward trend, however, which, combining with backlog effects, means that both demand and supply should stage a rapid recovery during the first quarter of 1970. Additional demand was generated during these months by the wage increases, which were large and gave further impetus to the already strong cost push towards higher prices. The balance of payments remained in deficit. The future course of the economy depends not only upon the re-establishment of lasting peace on the labour front but also on the extent to which those in charge of economic policy succeed in their drive to establish conditions allowing of a return to more balanced economic growth.

1. Recent developments

The key factor in the trend of the Italian economy towards the end of last year was a wave of extremely large-scale labour conflicts, the effects of which temporarily masked what was basically a rising trend. According to ISTAT figures some 200 million working hours were lost through strikes during the period September-December. In consequence, demand weakened and production losses were large. The estimates of annual results for 1969, as published in the last Quarterly Survey, must therefore be revised sharply downwards.

The wage increases granted during the labour conflicts were very generous indeed and create important new conditions governing future economic developments. In contracts valid for several years, for example, the hourly wage rates in building and construction, the engineering and chemical industries were raised by 14 to 15% for the year 1970. Additional wage increases are pending, but these are to be differentiated by employer firms. Labour costs in the above-named industries will go up further as a result of shorter working hours.

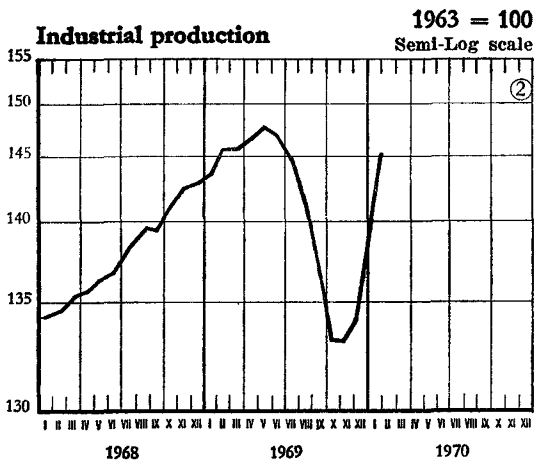
With strikes curtailing supply, exports were weak during the last quarter of 1969. According to customs returns, the value of visible exports rose by only 3.5% in annual terms, compared with 21% for the first nine months of the year.



Domestic demand probably suffered even more than exports from the labour conflicts. This applies especially to gross fixed asset formation. There is much to suggest, furthermore, that stocks declined very sharply, since the combined supply from domestic production and imports was insufficient in the short run to satisfy demand in full.

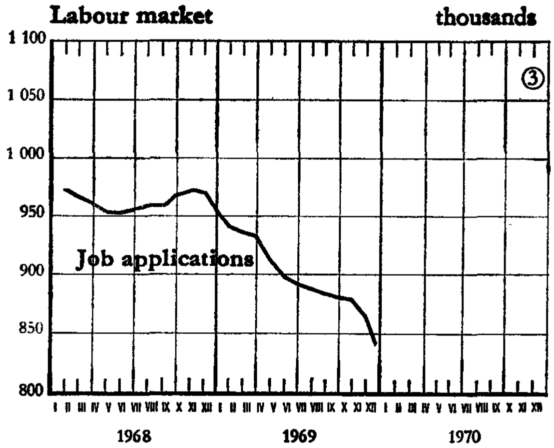
Income losses due to the strikes led to marked weaknesses in private consumers' expenditure late in 1969; this applies especially to the more expensive consumer goods. With the wave of strikes dying out early in 1970 and after the signature of the new collective agreements in major industries, consumer demand no doubt picked up sharply again, not least thanks to a spectacular increase in the cost-of-living bonus in accordance with existing sliding scales.

Industrial production (excluding building and construction) declined steeply during the fourth quarter of 1969—in seasonally adjusted figures by about 9% from the third quarter's level. This depressed the total annual rate of growth to 3.3% according to ISTAT indices, compared with legitimate expectations of about 8% a year ago. Virtually the whole of this loss of growth is attributable to strikes more serious than any that have taken place before in Italy—especially in the metal-using and chemical industries. Stoppages in building and construction also caused production losses. But the first quarter's seasonally adjusted figures this year will no doubt show a fast increase again, not least because firms must have made an effort to catch up.

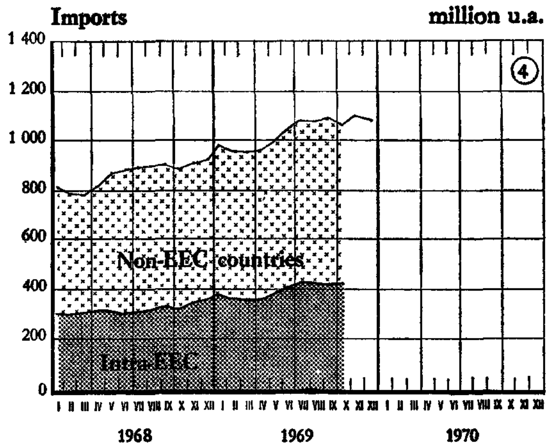


Although the ISTAT quarterly sample surveys show the number of persons in paid employment to have risen once more during the last quarter of 1969, the strikes naturally cut down sharply the number of hours actually worked. At the same time there was another decrease of unemployment.

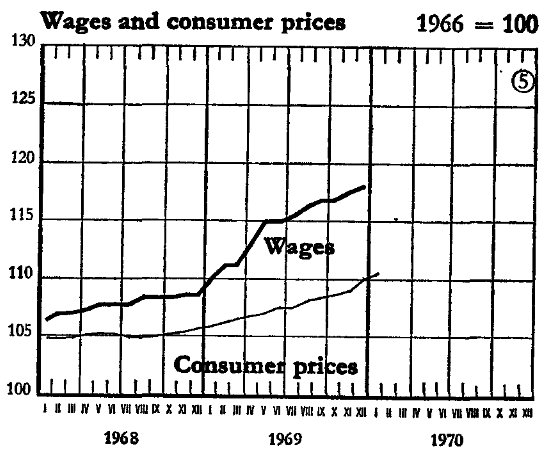
The import trend towards the end of 1969 was relatively firm, inasmuch as production losses were to some extent offset by increased recourse to foreign suppliers. According to customs



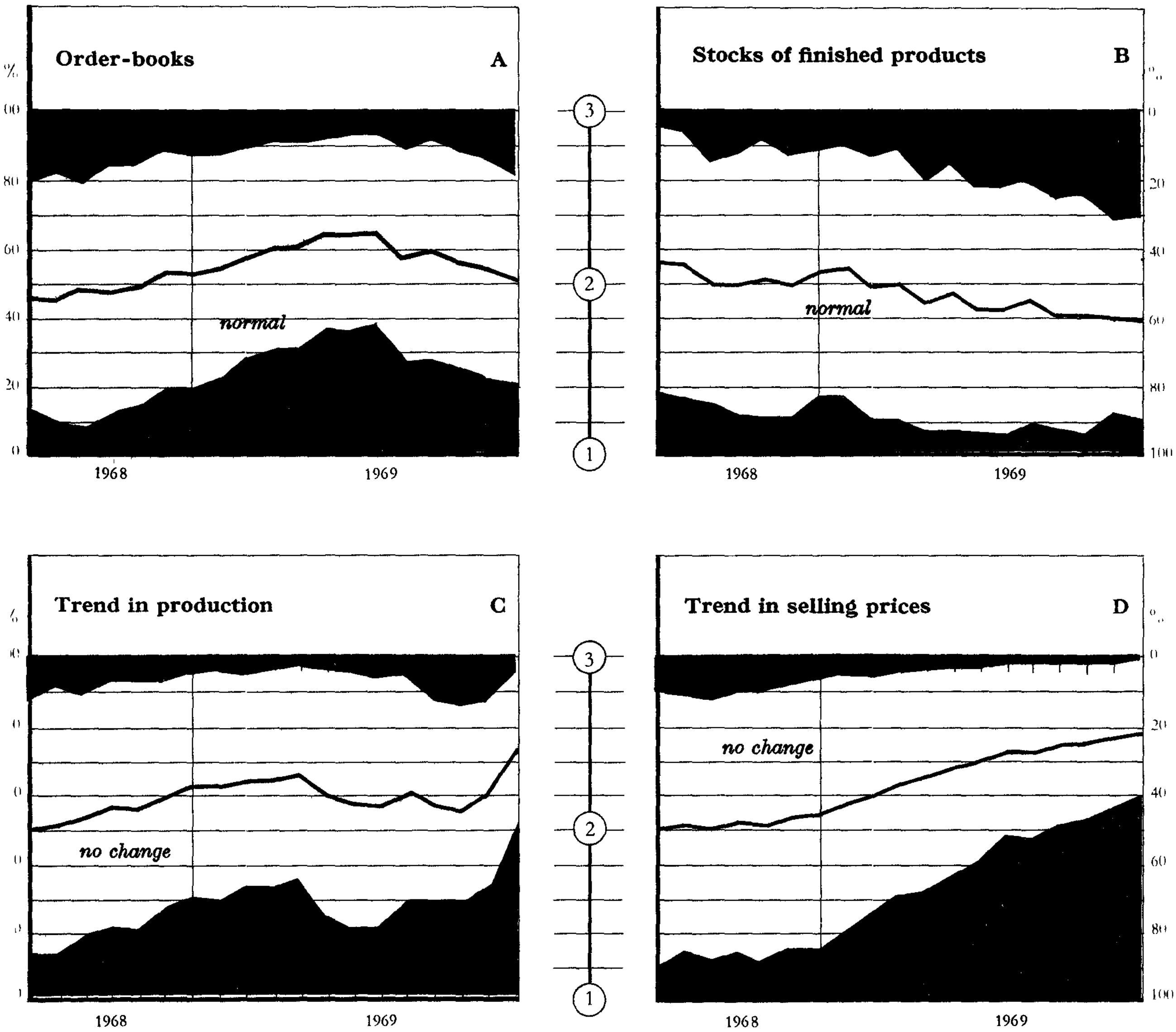
returns, the value of visible imports in the fourth quarter of 1969 exceeded the preceding year's corresponding level by 21%.



Prices had been rising fairly steeply even before, and in the last months of 1969 the movement gathered speed. In the first place, excess



BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

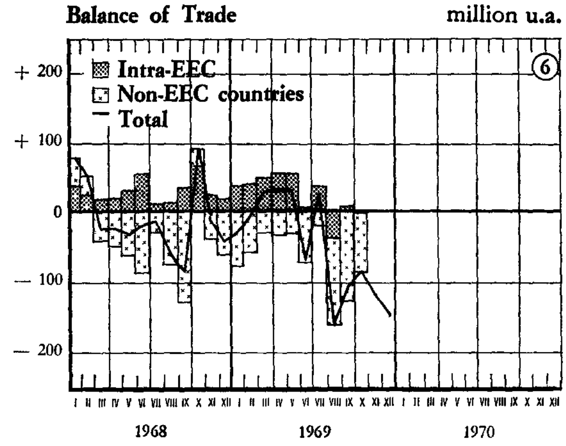
GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

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".

demand grew even more, and secondly there was a vigorous push from the cost side, mainly owing to strongly rising wage costs, another rise of import prices and an increase in fixed costs per unit of output during the months of the strikes. In year-on-year terms, wholesale prices showed an increase of 7.9% in January, and retail prices one of 4.3%.

The balance of payments did a little less badly late in 1969 than earlier last year, but the first few months of 1970 brought another distinct deterioration. Given the import and export trends, the visible trade deficit increased to an extent offset only briefly by a decrease in net capital exports. In spite of rising interest rates, the capital outflow during the months October-January exceeded the current surplus by Lit. 320 000 million. Although the commercial banks brought in more money from abroad, the official gold and foreign exchange reserves (net and not counting the special drawing rights) dropped between the end of September and the end of January by Lit. 140 000 million to



Demand for and supply of goods and services

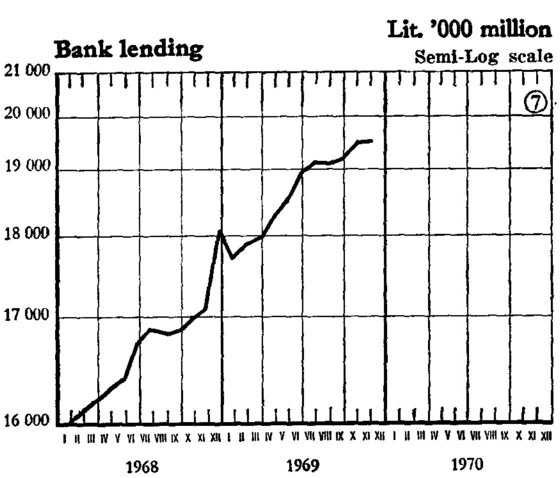
	1967 [1]	1968 [1]		1969 [1]		1970 [2]
	At current prices (in Lit. '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports [3]	7 965	+ 15.4	+ 14.5	+ 14.1	+ 15.6	+ 10
Gross fixed asset formation	8 323	+ 7.7	+ 10.1	+ 8.2	+ 15.0	+ 10
Public current expenditure on goods and services	5 861	+ 4.1	+ 8.6	+ 3.1	+ 8.1	+ 5
Private consumers' expenditure	28 214	+ 4.7	+ 6.3	+ 5.7	+ 8.8	+ 9
Gross national product	43 804	+ 6.0	+ 7.6	+ 5.0	+ 9.2	+ 8
Imports [3]	7 193	+ 7.5	+ 7.0	+ 20.7	+ 21.3	+ 21

[1] « Relazione generale sulla situazione economica del Paese (1969) ».
[2] Commission forecasts.
[3] Goods, services and factor income.

Note :
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with experts from the member countries, but are established and published on the sole responsibility of the Commission.

Lit. 2 714 000 million, at which level they cover the value of about four months' imports.

The domestic liquidity of the banking system again tended to decline; at 2.9%, the ratio of liquid assets to deposits last November was the lowest in five years: in the fourth quarter factors making for increased liquidity—connected chiefly with the Treasury's cash transactions—were more than offset by factors tending to reduce bank liquidity, mainly an exceptionally large increase in cash circulation and a (seasonally adjusted) decrease in the monetary authorities' refinancing credits. Nevertheless, bank lending continued to expand with virtually unabated vigour, and in the fourth quarter of 1969 exceeded the corresponding 1968 level by 14.5%.



On the capital market share prices had a definitely firm tendency, at any rate until the end of January. The prices of fixed-interest securities, on the other hand, continued to decline although the Banca d'Italia took in new bond issues on a large scale during the fourth quarter. As a result, bond yields have risen appreciably in response to the policy line followed by the monetary authorities since the spring of last year. When two state-controlled banks recently offered bonds yielding about 7 ½ %, the issues were highly successful.

2. Outlook

There can be no doubt that economic developments during the rest of this year will be strongly influenced by the effects of the production losses caused by the 1969 strikes and the ensuing wage increases. Assuming durable peace on the labour front, both these circumstances are likely to raise the rate of growth of production and especially of total monetary demand this year well above the 1969 figures, with domestic demand probably again expanding markedly faster.

Export growth will no doubt remain vigorous, though probably less so than before, because of a number of inhibiting factors. These include higher pressure on resources by domestic demand, less favourable prospects for world trade and some deterioration in Italy's competitive position—at present still strong—as a result of rising prices and the reduction of certain export rebates due on 1 April.

As regards domestic demand, expenditure on gross fixed asset formation as a whole is likely to go up sharply, an assumption supported for industry by the results of the EEC investment survey and in any case reasonable enough in the light of the expected growth of consumption, the high degree of capacity utilization, the urgent need to rationalize production and, not least, the necessary replenishment of stocks after their depletion during the labour conflicts. In addition, there may be some acceleration in public works to catch up with last year's delays. By contrast, the expansion of residential construction investment is likely to lose some of its impetus, for the reasons explained in the last Quarterly Survey.

The large wage increases granted so far in several industries are likely to set new targets for wage negotiations elsewhere. Allowing for the wage level already existing at the end of 1969, for further wage increases to be negotiated at the level of individual firms, and for the effects of the sliding scale and the probable increase in employment, the nation's wage bill may well rise by something like 16 to 18%. With the propensity to consume of households likewise expected to rise, there is every likelihood of a strong acceleration in the expansion of private consumers' expenditure.

If these assumptions are correct, production is bound to increase very considerably. The real gross national product might well grow by about 8%, though this figure is somewhat inflated by special factors (production losses in 1969, after-effects in 1970) and implies no more than that some of the 1969 losses will be made

The Central Government Budget

	1969		1970	1969	1970
	Budget	Revised budget	Budget	Budget	Budget
	Lit. '000.000 million			% changes on the preceding year's budget	
Expenditure [1]	11.1	12.3	12.9	+ 11.3	+ 15.8
of which :					
current expenditure	8.5	9.3	10.1	+ 13.1	+ 17.9
capital expenditure [2]	2.6	3.0	2.8	+ 5.9	+ 8.9
Revenue	9.1	9.3	10.3	+ 8.7	+ 13.0
of which :					
direct taxes	2.4	2.4	2.8	+ 8.5	+ 15.1
indirect taxes	6.1	6.3	6.9	+ 8.8	+ 13.1
Net expenditure [1]	2.0	3.1	2.6	.	.

[1] Disregarding debt extinction.
[2] Including participations, advances and loans.

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

good. For the same reasons imports, too, may increase more than originally expected.

The number of persons in paid employment will assuredly go up, if only because recent labour agreements have reinforced the trend towards shortening the contractual working week. The Ministry of Labour sample survey suggests an increase this year of about 3% in the number of wage- and salary-earners in industry.

The outlook for demand and supply raises major problems for external and internal balance. First of all, a further considerable deterioration must be expected in the current balance of payments, and the same applies to the climate of prices. On the minimum assumption that the average increase in wage costs per unit of output is fully transferred to prices—this would entail appreciably narrower profit margins—prices would go up by around 6%.

In these circumstances, as already suggested in the last Quarterly Survey, disinflation must be the main economic policy priority. Prompt and energetic action to this end is needed, in particular, to help maintain the purchasing power of wages. A cumulative price-wage spiral would, furthermore, sooner or later pose a threat to employment. Beyond that, the speedy consolidation of the Italian economy is an important condition governing balance-of-payments equilibrium, which was upset last year by heavy capital outflows.

The leading part should be assigned to budget policy, with sharp cuts to contain the growth of expenditure, especially current expenditure. This would enable the authorities to re-establish social infrastructure investment programmes on a sound and durable basis in the near future—a field where pressing requirements need to be met. There might be a case for tax increases allowable against future tax payments. There is likewise a case for raising tax revenue, for instance through more stringent methods of tax assessment and collection. The cash deficit should be financed as far as possible from real savings and not, as happened frequently in 1969, by direct or indirect recourse to the central bank. Administrative price increases as a device to avoid recourse to the money market for funds are inadvisable especially in cases where they would activate the sliding wage scale.

Those responsible for monetary and credit policy have for some time been trying to create a "counterpoise" by reverting to a restrictive course, and these efforts should be strengthened as far as possible, bearing in mind the need for flexibility in a situation where rising costs are cutting into the self-financing margins of firms and where it is necessary, therefore, to avoid any abrupt developments liable to have a "domino" effect. It is entirely in line with current requirements that the monetary authorities, not least with an eye on the balance of payments, have been encouraging higher interest rates by various measures, including the recent further increase in Bank and Lombard rates. While the growth of the banks' credit potential must be contained, restrictions need to be selective in the sense, for instance, of being fairly generous with credits to finance investment likely to yield quick productivity gains. All the stricter must be the standards applied to other credits, including those for consumption purposes.

As regards the capital market, where an important problem is that of stemming capital exports, current efforts to create attractive opportunities for savers in Italy should continue. The basic requirement, of course, is that prices and price expectations should revert to normal. But the bill for authorizing the creation of suitably attractive investment funds, which is now before Parliament, would likewise be a major step in the right direction. There might be a case for covering part of the economy's steadily growing finance needs by security issues abroad, which would have favourable effects on the balance of payments. Fiscal and other incentives for an asset-creating use of wage increases would be valuable, especially since they would help to contain consumer demand.

Generally speaking, employment policy, too, should help to reduce the gap between supply and demand. Apart from promoting the occupational and geographical mobility of workers, this purpose would be served also by labour agreements aiming at maximum utilization of production potential.

Finally, to diminish the cost-push on prices, steps should be taken—for example, by an appropriate adjustment of policy concerning the licensing of shops—to rationalize the distribution channels, a field in which there is still much progress to be made in Italy.

Major economic policy measures

January

(1) The Ministerial Committee for Credit and Saving decides on credit measures to facilitate home ownership. The sluggish sales of mortgage bonds are to be revived by more attractive terms (the interest ceiling is raised from 5 to 6% for new issues, and there is to be an annually rising premium in the redemption of existing ones). Part of the compulsory reserves, moreover, have to be invested in mortgage bonds—in the case of commercial banks, the full future increment of savings deposits, and in the case of savings banks, one quarter of their reserve requirement.

(2) The same Committee decides to increase interest subsidies with a view to expanding the supply of privileged credits (e.g. for medium- and small-sized industrial firms and for investment in southern Italy), which was shrinking because of the general rise of interest rates.

February

The monetary authorities reduce the permissible maximum time-limit for deferred payment on exports of goods and services to 120 days, and that for corresponding advance payment on imports to 30 days. This measure is intended to improve the leads and lags effect. With a view to more stringent control of capital exports it was decided at the same time that notes in Lit. may no longer be credited to foreign banks by authorized banks in Italy, but only by the Banca d'Italia itself.

March

Bank rate and the Lombard rate—last raised in August 1969—are put up again, from 4 to 5.5%. The effective rate at which the banks can draw refinancing funds is, however, considerably higher in most cases, since the surcharges introduced in March and July 1969 are still applied (0.5 to 1.5 points for certain central bank advances of fixed duration, 1.5 points for rediscounts in the case of banks whose total volume of rediscounts exceeds a certain limit).

Italy

TABLE 1 : **Key indicators**

	1965	1966	1967	1968	1969	1969
	% change by volume on preceding year					Indices 1958=100
Gross national product	3.6	5.9	6.4	6.0	5.0	134
Industrial production	3.3	7.4	8.7	8.7	5.2	140
Total imports	1.9	13.7	12.6	7.5	20.7	161
Private consumers' expenditure	2.7	6.8	7.3	4.7	5.7	134
Public current expenditure on goods and services	3.6	3.2	2.8	4.1	3.1	123
Gross fixed asset formation	– 8.7	4.0	10.5	7.7	8.2	115
Total exports	20.1	13.2	6.2	15.4	14.1	212
Gross national product per head of population	2.4	4.8	5.4	5.3	4.2	126
Gross national product per person in employment	4.7	7.4	5.7	6.2	6.3	138
	% change by value on preceding year					
Gross income per employee	8.6	8.2	7.8	7.2	7.5	165

TABLE 2 : **Indicators for internal and external equilibrium**

	1965	1966	1967	1968	1969
Balance exports less imports					
in million u.a.	729	673	483	888	754
as percentage of GNP	3.3	2.7	1.8	3.0	2.3
Unemployment rate	3.6	3.9	3.5	3.5	3.4
price index of private consumers' expenditure (% change on preceding year)	4.1	2.9	2.9	1.5	2.9

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					Indices 1963=100	Million u.a.	% of totals
	1964	1965	1966	1967	1968	1968	1968	1968
Visible exports								
Total	18.0	20.7	11.7	8.3	17.0	201.8	10 183.2	100
Intra-EEC	26.4	27.6	12.8	3.3	20.9	227.6	4 079.1	40.1
To non-EEC countries	13.4	16.4	11.0	11.6	14.5	187.6	6 104.1	59.9
Exports of food, beverages and tobacco								
Total	2.4	20.5	1.5	4.7	– 3.7	126.4	870.1	8.5
Intra-EEC	8.8	31.4	0.4	– 1.7	– 1.3	139.2	453.4	4.4
To non-EEC countries	– 3.3	9.5	2.8	12.4	– 6.1	114.9	416.7	4.1
Exports of raw materials, fuel and power								
Total	14.5	18.7	10.6	9.1	14.1	187.0	885.0	8.7
Intra-EEC	23.3	34.2	21.5	15.9	14.7	267.0	341.0	3.3
To non-EEC countries	11.2	12.4	5.2	5.3	13.7	157.5	544.0	5.4
Exports of semi-finished and finished industrial goods								
Total	21.2	20.9	13.4	8.8	20.2	216.9	8 428.1	82.8
Intra-EEC	31.0	26.2	14.6	3.2	25.4	245.3	3 284.7	32.4
To non-EEC countries	16.1	17.8	12.6	12.4	16.7	202.0	5 143.4	50.4
Visible imports								
Total	– 4.1	1.6	16.7	12.9	4.3	136.0	10 252.6	100
Intra-EEC	– 4.5	– 3.1	21.6	21.5	9.1	149.9	3 709.2	36.2
From non-EEC countries	– 3.9	3.9	14.4	8.8	1.8	129.5	6 543.4	63.8
Imports of food, beverages and tobacco								
Total	2.4	18.9	9.7	0.7	8.5	145.9	1 931.1	18.8
Intra-EEC	15.7	20.6	13.5	26.6	29.0	259.3	622.3	6.1
From non-EEC countries	– 0.6	18.4	8.7	– 6.4	0.9	120.8	1 308.8	12.7
Imports of raw materials, fuel and power								
Total	– 0.7	8.5	15.1	13.7	1.0	142.3	3 691.1	36.0
Intra-EEC	– 0.1	18.7	18.2	14.2	– 3.0	155.4	495.6	4.8
From non-EEC countries	– 0.8	7.0	14.6	13.6	1.7	140.5	3 195.5	31.2
Imports of semi-finished and finished industrial goods								
Total	– 8.9	– 10.8	22.0	18.8	8.6	127.8	4 630.4	45.2
Intra-EEC	– 7.7	– 10.8	24.2	22.3	8.1	135.3	2 591.3	25.3
From non-EEC countries	– 10.2	– 10.9	19.4	14.5	9.2	119.5	2 039.1	19.9

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1968	136.3	127.5	136.7	133.7	135.0	138.2	137.3	138.7	142.3	141.9	136.8	144.4
	1969	146.1	143.9	147.0	147.0	143.8	150.4	150.0	143.0	136.9	126.6	125.2	133.6
	1970	(152.9)											
Unemployed (1 000)	1968	970.4	963.8	952.7	943.7	962.1	958.2	962.3	962.9	975.3	976.6	952.1	931.3
	1969	933.8	938.7	915.5	895.6	882.2	895.2	883.5	879.5	886.3	871.5	843.0	816.3
	1970	(825.0)											
Construction : permits for residential construction (1 000)	1968	31.3	48.1	55.3	55.6	53.6	60.5	69.0	313.4	78.6	72.7	38.6	45.6
	1969	19.4	21.4	23.3	21.4	25.3	22.8	25.1	22.6	25.8	25.3		
	1970												
Private consumers' expenditure : department store turnover (1963 = 100)	1968	137.9	150.3	146.8	154.1	149.7	149.6	159.5	159.9	152.2	155.0	161.1	156.7
	1969	155.1	150.9	164.8	159.9	182.4	162.7	174.5	182.4	183.2	173.5		
	1970												
Consumer prices (1963 = 100)	1968	118.7	118.7	118.8	119.0	119.1	119.0	118.8	118.8	118.9	119.0	119.2	119.6
	1969	119.9	120.1	120.6	121.1	121.4	121.8	123.1	122.9	123.1	123.4	124.1	124.6
	1970	125.1											
Visible imports (million u.a.)	1968	713.0	734.5	826.1	844.9	876.2	850.4	860.1	903.3	910.1	778.9	1 013.6	946.5
	1969	971.5	940.0	934.3	996.4	1 047.2	1 078.5	1 093.7	1 036.4	1 109.2	1 019.5	(1123.1)	(1072.4)
	1970												
Visible exports (million u.a.)	1968	796.5	794.0	800.9	820.1	843.2	829.4	846.6	842.4	822.7	870.0	1 002.5	907.5
	1969	938.4	930.7	962.8	1 026.2	1 076.8	1 009.6	1 118.4	876.9	996.5	933.1	(1004.5)	(851.2)
	1970												
Balance of trade (million u.a.)	1968	+ 83.5	+ 59.5	– 25.2	– 24.8	– 33.0	– 21.0	– 13.5	– 60.9	– 87.4	+ 91.1	– 11.1	– 39.0
	1969	– 33.1	– 9.3	+ 28.5	+ 29.8	+ 29.6	– 68.9	+ 24.7	– 159.5	– 112.7	– 86.4	(–112.6)	(–221.2)
	1970												
Official gold and foreign exchange reserves (net million u.a.)	1968	5 138.7	5 149.6	5 104.5	5 081.9	5 042.4	5 086.4	5 140.9	5 269.7	5 188.3	5 194.9	5 069.1	4 878.3
	1969	4 727.2	4 636.3	4 492.6	4 571.0	4 365.8	4 514.2	4 581.7	4 645.9	4 567.0	4 566.3	4 667.7	4 697.0
	1970	4 457.1	(3940.0)										
Money supply (Lit. '000 million)	1968	17 863	17 652	17 976	18 235	18 463	18 795	18 993	18 975	19 379	19 373	19 695	21 104
	1969	20 440	20 379	20 836	20 845	21 282	21 558	21 590	21 681	22 138	22 351	22 831	24 387
	1970												

Italy

NOTES TO GRAPHS AND TABLES

Source : Statistical Office of the European Communities (except as otherwise indicated).
Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US $ 1) at official exchange rates.

Graph 1

— Exports fob : series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Industrial production (excluding construction, food, beverages and tobacco) : trend curve; estimates established on the basis of indices adjusted for seasonal and fortuitous variations.

Graph 3

— Labour market : number of registered unemployed; series prepared by the Ministero del Lavoro e della Previdenza Sociale and adjusted for seasonal variations by the Statistical Office of the European Communities; three-month moving averages.

Graph 4

— Imports cif : series adjusted for seasonal variations; three-month moving averages.

Graph 5

— Wages and consumer prices : source ISTAT. Agreed minimum wages in industry (incl. family allowances).

Graph 6

— Merchandise trade balance : difference between the figures for seasonally adjusted exports and seasonally adjusted imports.

Graph 7

— Bank lending to commerce and industry : source Banca d'Italia. Short-term loans to business and private consumers; position at end of month.

Table 1

Source for 1968 and 1969 : Relazione generale sulla situazione economica del Paese (1969).

— GNP at market prices.
— Industrial production : value added by industry at factor cost.
— Total exports and imports : goods, services and factor income.
— Gross income per employee : income from paid employment (not including social insurance contributions borne by the State).

Table 2

— Net exports : goods, services and factor income.
— Unemployment rate : number of unemployed as percentage of labour force (annual average); Source ISTAT.
— Price index : implicit price index for private consumption, computed from the national accounts.

Table 3

— Exports fob, imports cif; the products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST) : food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production : adjusted for seasonal variations, excluding construction, food, beverages and tobacco.
— Unemployed : series provided by the Ministero del Lavoro e della Previdenza Sociale, adjusted for seasonal variations by the Statistical Office of the European Communities.
— Construction : dwellings authorized in the provincial capitals and in other communes with more than 20 000 inhabitants; figures not seasonally adjusted.
— Private consumers' expenditure : value index of department store turnovers, adjusted for seasonal variations.
— Consumer prices : unadjusted index.
— Imports cif, exports fob; adjusted for seasonal variations.
— Balance of trade; difference between seasonally adjusted exports and imports.
— Official gold and foreign exchange reserves (net); source Ufficio Italiano dei Cambi; position at end of month.
— Money supply : notes and coin in circulation excluding cash holdings of the Treasury. Sight deposits of non-banking sector with credit institutions, bank drafts in circulation (whether *vaglia* or *assegni*) issued by the Banca d'Italia and other banks and credit institutions; position at end of month.

D. Netherlands

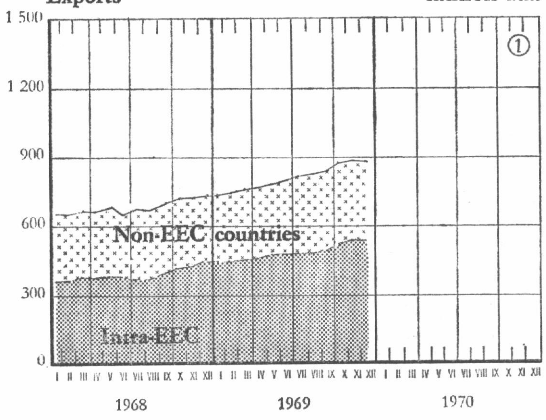
The vigorous expansion of overall demand in monetary terms in the Netherlands was maintained in the early months of 1970. Strong expansionary impulses came from export demand, especially from demand in other EEC countries, and final demand at home remained buoyant. At the same time the elasticity of supply decreased still further, with a large number of firms running at or near capacity and more labour shortages. Even if the expansion of demand loses a little momentum, the boom in the Dutch economy is likely to last throughout the rest of the year. Increasing strains on the markets for goods and services, together with rising wage cots, and certain autonomous factors, such as official rent increases, higher charges for public services and rising import costs, will keep prices under considerable upward pressure.

1. Recent developments

With demand still growing vigorously, there is very little slack left in the Dutch economy. The degree of capacity utilization is very high, virtually all available labour is employed and prices are still going up. At the beginning of the year the alteration in the pattern of demand expected for 1970—mainly because of a weakening of export demand—was not yet discernible.

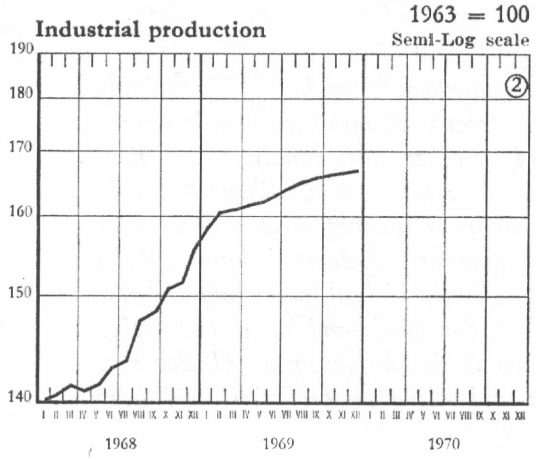
Exports have in fact again increased strongly. Although supply is now inelastic in some industries, firms were able to cope with most export orders. Customs returns put the value of visible exports 22% higher on the two-month average January-February this year than in 1969.

Stockbuilding has slowed down, but gross fixed asset formation still increased. So far as firms are concerned, a revival of investment in industrial construction probably more than offset the less vigorous growth of expenditures on plant and machinery. Although the tax reliefs on depreciation were revoked last year and some branches of industry are less inclined to invest in this new phase of rising production costs, firms—especially in industries working mainly for export markets—probably still have ample resources for self-financing.



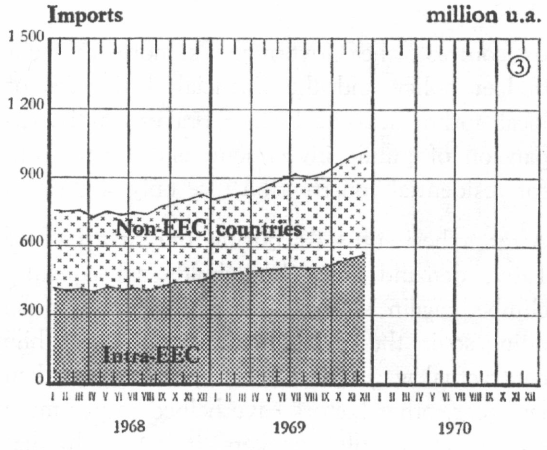
By contrast, the Government's more stringent budget policy and the financial difficulties of local authorities put further brakes on the expansion of public investment, and expenditure for residential construction rose only slightly.

After a hesitant start during the first half of 1969, demand from households subsequently climbed again steeply and still seemed to be doing so in the early months of 1970. While contractual wages have gone up less so far than last year, other factors have helped to put more money into people's pockets: it is thought that the wage drift is once again more vigorous, there has been an increase in the number of persons employed, social benefits rose appreciably early this year and a reduction in direct taxes has meant less progressive taxes.

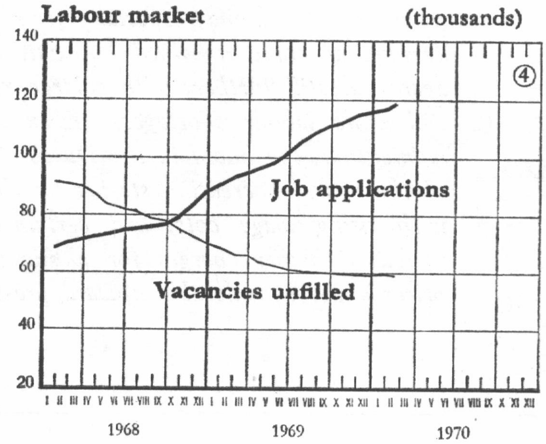


Bad weather and, even more so, factor shortages seem to have combined early this year to slow down the—seasonally adjusted—increase of domestic supply. Even in the last quarter of 1969 the CBS index showed industrial production to have risen by only 2.5% over the preceding quarter's level, after a rise of 3.5% each in the second and third quarters (all seasonally adjusted figures).

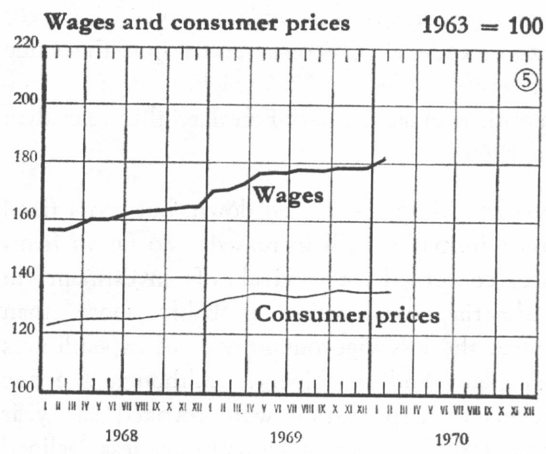
Imports began rising fast in the fourth quarter of 1969 and went on doing so in the first months of this year. Customs returns put the volume of visible imports for December/January at 17% above the level of twelve months earlier. The expansion was led by manufactures, especially consumer goods.



The situation on the labour market is more strained than ever. Workers made redundant by mergers and closures quickly found new jobs, and firms have had to recruit more and more foreign labour. The seasonally adjusted rate of unemployment (number of unemployed as a percentage of the civilian labour force) was down to 1.2% in February.

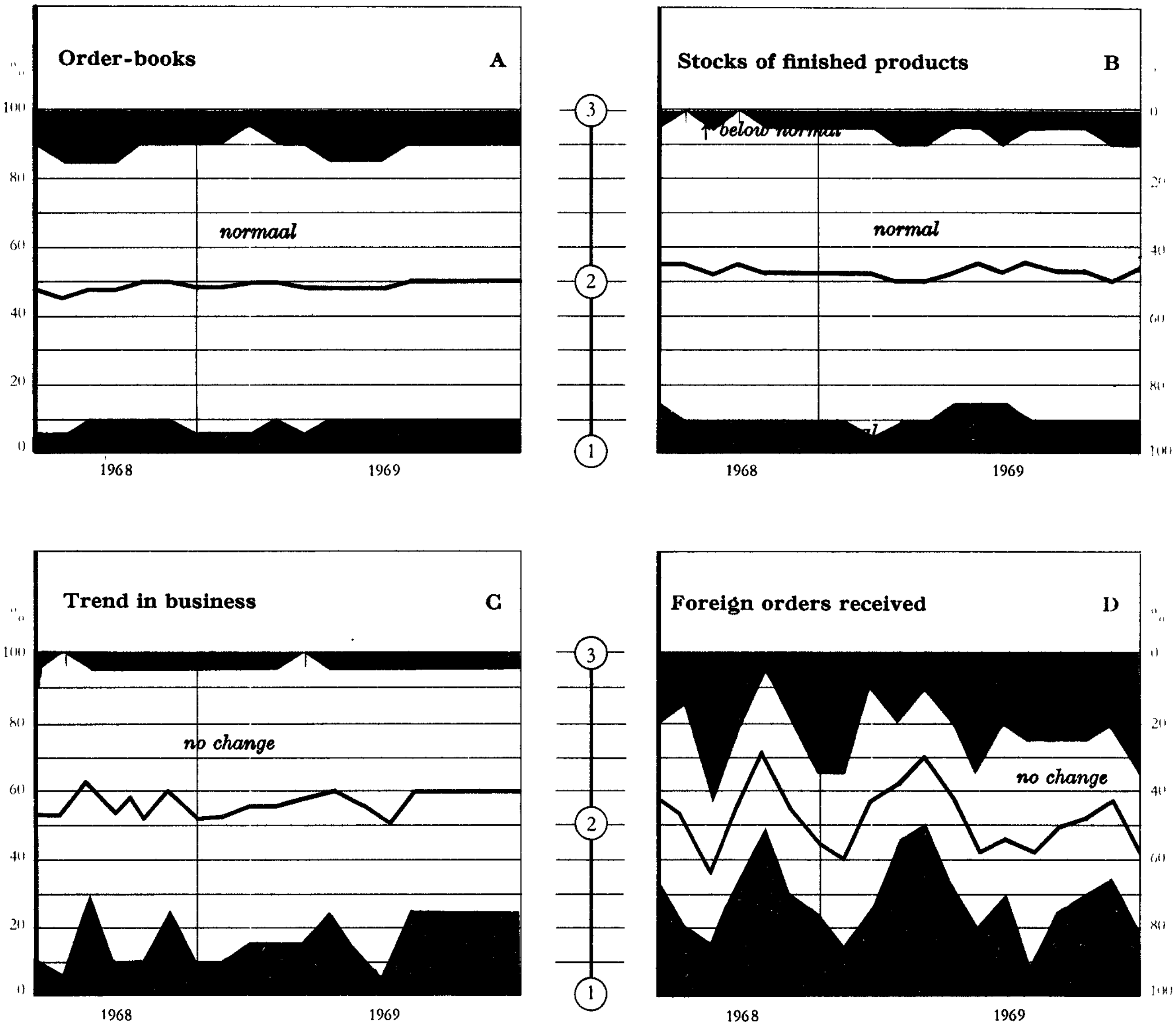


Prices are still under considerable upward pressure although the pronounced rise of import prices since last September is not so far fully reflected in the level of retail prices. The cost-of-living index rose by 1.2% from December to February to a level 3.2% above that of February 1969. The relative moderation of the latest rise is largely explained by the fact that the effects of some autonomous factors (rents, charges for public services, etc.) are not now bunched at the beginning of the year as much as they used to be.



With imports growing faster than exports, the current balance of payments has been deteriorating a little since the autumn of 1969. After

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

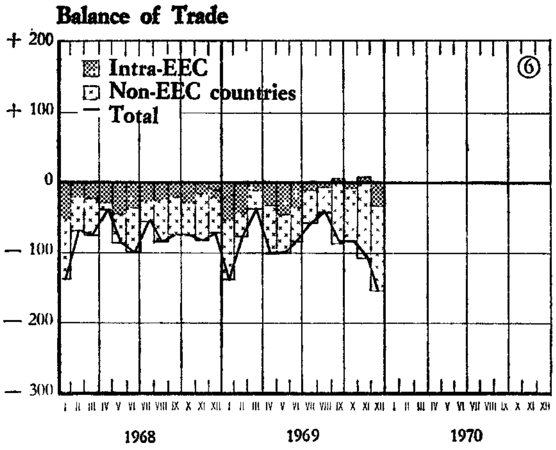
Note : The survey includes construction but not paper, petroleum, non-metallic minerals.

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

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

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

a sudden rush of hot money into the country in October capital outflows were recorded for the first time for some months. Official gold and foreign exchange reserves declined by Fl. 680 million between the end of October and the end of January, but at the same time the foreign exchange position of commercial banks improved appreciably.



Domestic liquidity was boosted in October by the inflow of short-term foreign capital, but subsequently the economy's liquidity ratio (ratio of primary and secondary liquid assets to national income) again declined slightly, the Government's handling of the budget having contributed to this development. Until last November the expansion of short-term bank credits to business and private customers kept exceeding the maximum rate fixed by the regulations on credit restriction, but since then has kept within the ceiling.

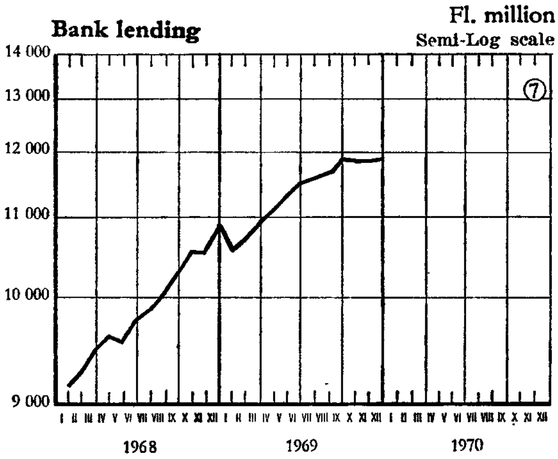
Demand for and supply of goods and services

	1967 [1]	1968 [1]		1969 [2]		1970 [3]
	At current prices (in Fl. '000 million)	% change on preceding year				
		Volume	Value	Volume [4]	Value	Volume [4]
Exports [5]	37.48	+ 13.1	+ 11.9	+ 16	+ 18	+ 10½
Gross fixed asset formation	21.53	+ 10.1	+ 12.6	— 1½	+ 7½	+ 5
Public current expenditure on goods and services	13.11	+ 1.8	+ 7.1	+ 4	+ 13	+ 3
Private consumers' expenditure	47.29	+ 5.7	+ 8.4	+ 3½	+ 10½	+ 5½
Gross national product	82.97	+ 6.2	+ 10.1	+ 5	+ 11½	+ 4½
Imports [5]	37.54	+ 13.8	+ 10.6	+ 14	+ 18½	+ 8½

[1] Statistical Office of the European Communities.
[2] CPB estimates.
[3] Commission forecasts.
[4] In the preceding year's prices.
[5] Goods, services and factor income.

Note :
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts of the member countries but are established and published on the sole responsibility of the Commission.

The money and capital markets have both become tighter again since October, and by February interest rates had very nearly climbed back to their previous peak.



2. Outlook

Demand, production and employment will continue to rise as the year goes on, though most probably at a somewhat slower pace. But since any general slowdown would, because of a further diminution of the elasticity of production, be more pronounced on the supply than on the demand side, not much relief can be expected in the strains on the markets for goods and services.

Export growth may well slow down, with sales to countries outside the EEC suffering from the direct and indirect effects of the cooler economic climate in the United States. Exports to member countries, on the other hand, should expand vigorously once again, thanks to the boom in Germany, Italy and Belgium, which between them take up almost half of all Dutch exports; these countries will need to rely on outside supplies on a large scale, and Dutch exports cannot fail to benefit.

Domestic demand as a whole is expected to weaken somewhat in the next few months, if only because stockbuilding must revert to more normal rates. Fixed investment, on the other hand, is not likely to slow down to any appreciable extent, although there is an element of uncertainty here inasmuch as the propensity to invest may, as the year goes on, be inhibited somewhat by less favourable world prospects and narrowing financing margins. But very large-scale projects are already in hand, so that actual investment expenditure is virtually certain to expand strongly until well into the year. Residential construction, in its turn, should revive, thanks to the larger number of housing projects qualifying for public subsidies during the first half of 1970; but the credit squeeze and the prohibitively high interest rates for mortgage loans remain an obstacle to expansion. Public investment, finally, will be slowed down by the Government's budget policy and by the difficulties local authorities are encountering in raising funds.

Private consumers' expenditure, by contrast, will no doubt go on expanding briskly, chiefly in response to a much larger wage- and salary-bill. The new wages contract of the metal-using industries, which has set an important precedent for the other negotiations, provides for a considerable increase in contractual wage rates. In addition, wages are being tied more and more closely to the cost-of-living index, social benefits are going up and the disposable income of households will benefit from the income tax reduction. Finally, the savings ratio may decline a little.

But although demand is likely to expand at a somewhat slower pace, domestic supply will most probably not be able to keep in step, the less so since labour shortages are bound to increase when the contractually agreed cuts in the working week become effective in the middle of the year. Given the high level of industrial production at the beginning of 1970, however, the last Quarterly Survey's forecast for the growth of the real gross national product can be revised slightly upwards to about 4.5%.

Although the continuing high degree of capacity utilization should draw in foreign supplies, import growth is expected to slow down, with barely any further increase in purchases of raw materials and capital goods. But the slowdown here will probably not be as pronounced as in exports and the terms of trade may well deteriorate, so that no surplus on current account is likely to be achieved.

Consumer prices, after their relatively moderate rise early this year, may resume a steeper climb in the coming months, more especially under the influence of some autonomous factors like rent increases, higher sickness benefits, etc., but

The Central Government Budget

	1969		1970	1969	1970
	Original budget	Provisional results	Budget	Original budget	Budget
	Fl. '000 million			% changes on the preceding year's original budget	
Expenditure [1]	25.1	25.9	27.9	+ 12.8	+ 11.2
of which :					
current expenditure	18.4	19.0	20.7	+ 14.7	+ 12.3
capital expenditure [2]	6.7	6.9	7.3	+ 8.1	+ 8.4
Revenue	23.2	23.4	26.3	+ 15.6	+ 13.7
of which :					
direct taxes	11.7	12.3	13.4	+ 17.4	+ 15.0
indirect taxes	9.3	8.9	10.5	+ 11.6	+ 12.7
Net borrowing requirement [1]	1.9	2.5	1.6	.	.

[1] Disregarding debt extinction.
[2] Including participations, advances and loans.

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

also because of persistent shortages on the markets for goods and services and because of higher wage costs.

So far as economic policy is concerned, therefore, the first priority must still be to curb inflation. Most important of all is the adoption of a counter-cyclical policy in public finances, a matter which seems to be particularly difficult in the Netherlands. On latest estimates, net spending by central and local government together came to more than Fl. 4 000 million in 1969, when the boom was already in full swing, compared with Fl. 2 260 million in 1968 and Fl. 2 310 million in 1967, when the Dutch economy was at the trough of recession. Unlike local authorities, however, the central government last year sharply diminished its recourse to the money market as a means of financing its deficit.

The central government is making an effort at present to render its budget policy more flexible. To this end a draft law provides for increased powers to alter certain tax rates. It will probably be too late for the Government to use these powers during the current boom, but they will still be a useful addition to the instruments of short-term economic policy and help to avoid delays in their application in the future. This appears all the more necessary as there are plans to adjust tax rates against the rising price level not every five years, as hitherto, but annually—an innovation that would weaken the "built-in stabilizer" effect of graduated taxation during periods of inflation.

The Government's efforts to tighten up its budget policy and in particular to rule out any overspending, assume all the more pressing urgency at the present juncture as further income tax reductions are to take effect at the beginning of 1971 just when an appreciable rise in indirect taxes is due. To avoid undesirable price and wage reactions, which, because of the closer link between contractual wages and the cost-of-living index, would have extremely adverse effects on the economy as a whole, everything possible should be done now to neutralize promptly existing sources of strain.

For the same reason the restrictive course of credit policy should also be maintained for the time being, especially since domestic liquidity is still rather high after the influx of capital from abroad last autumn. Therefore, the decision to extend the enforcement of the credit ceiling until April under more stringent conditions is a wise one. Beyond that it would seem desirable to introduce new incentives for private saving. Measures encouraging the formation of savings on the part of wage-earners and weak social groups could help to reduce the propensity to consume and therefore to mitigate inflationary pressures.

Major economic policy measures

January

(1) Request for an opinion of the Economic and Social Council (SER) on a draft law by which the Government is to be empowered to adjust certain tax rates to immediate economic requirements by ministerial decree; the tax rates concerned are those of income, wage and corporation tax, TVA and the motor vehicles tax, and the consumption tax on motor fuel. Temporary adjustments of at most 5% are envisaged.

(2) Approval of the wage contract for metal-using industries for 1970 and 1971. Wages are to go up by 2.75% at the beginning of each of the two years and to be adjusted twice a year to the cost of living, with a permissible maximum annual adjustment of 6%. As of 1 July 1970 the standard working week is cut by 3%, an extra two days are added to annual holidays and holiday pay is raised.

(3) By virtue of a new agreement between the Nederlandsche Bank and the commercial banks and agricultural credit institutes, the existing restrictions on short-term bank credits to the private sector are extended to cover the period January-April. These credits must not exceed their volume during the last quarter of 1969 by more than 5%.

(4) Decision to raise the interest subsidy on credits granted by shipyards from 2 to 3.5%, for the period ending 31 July.

(5) The Minister of Housing announces to the Second Chamber his new measures to stimulate residential construction. These measures concern in particular an extension of the subsidy system and the introduction of bonuses for contractors who complete projects ahead of schedule.

(6) Opinion of the Economic and Social Council concerning merger rules *(advies inzake gedragsregels bij fusies)*.

(7) A draft law tabled in the Second Chamber provides for a ceiling of Fl. 2 000 million on government loans floated in 1970. The Government can still issue Fl. 474 million worth of bonds under the 1969 Finance Act.

(8) The Senate approves a wages bill *(loonwet)* empowering the Government to invalidate wage contracts for general economic or social reasons.

February

The number of new dwellings to be subsidized in 1970 is raised by 5 000.

TABLE 1 : **Key indicators**

	1964	1965	1966	1967	1968	1968
	% change by volume on preceding year					Indices 1963=100
Gross national product	8.9	5.4	2.6	6.1	6.2	133
Industrial production	11.0	6.3	5.9	5.6	9.8	145
Total imports	14.9	6.5	7.3	6.2	13.8	157
Private consumers' expenditure	6.0	7.4	3.4	5.1	5.7	131
Public current expenditure on goods and services	1.7	1.6	1.6	4.1	1.8	111
Gross fixed asset formation	18.0	4.9	8.5	7.8	10.1	159
Total exports	11.6	7.6	5.2	6.9	13.1	153
Gross national product per head of population	7.5	4.0	1.2	4.9	5.1	125
Gross national product per person in employment	7.1	4.5	1.8	6.5	5.5	128
	% change by value on preceding year					
Gross income per employee	16.4	11.7	11.1	8.4	8.4	170

TABLE 2 : **Indicators for internal and external equilibrium**

	1964	1965	1966	1967	1968
Balance exports less imports					
in million u.a.	− 154	+ 76	− 135	− 17	+ 113
as percentage of GNP	− 0.9	+ 0.4	− 0.6	− 0.1	+ 0.5
Unemployment rate	0.7	0.8	1.0	2.0	1.8
prices to private consumers (% change on preceding year)	+ 6.8	+ 4.2	+ 5.4	+ 3.3	+ 2.3

Netherlands

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					Indices 1963=100	Million u.a.	% of totals
	1964	1965	1966	1967	1968	1968	1968	1968
Visible exports								
Total	+ 17.0	+ 10.1	+ 5.6	+ 7.9	+ 14.5	168	8 342	100
Intra-EEC	+ 22.1	+ 10.2	+ 5.3	+ 6.7	+ 19.7	181	4 790	57.4
To non-EEC countries	+ 11.2	+ 10.0	+ 6.0	+ 9.4	+ 8.2	153	3 552	42.6
Exports of food, beverages and tobacco								
Total	+ 9.5	+ 13.0	+ 0.3	+ 9.9	+ 15.9	158	2 002	24.0
Intra-EEC	+ 12.8	+ 19.7	− 0.2	+ 9.6	+ 22.1	180	1 295	15.5
To non-EEC countries	+ 5.1	+ 3.6	+ 1.0	+ 10.5	+ 6.1	129	707	8.5
Exports of raw materials, fuel and power								
Total	+ 10.9	+ 7.4	− 0.4	+ 10.1	+ 12.8	147	1 374	16.5
Intra-EEC	+ 12.3	+ 3.4	− 0.7	+ 10.7	+ 22.5	156	797	9.6
To non-EEC countries	+ 9.3	+ 12.3	− 0.1	+ 9.5	+ 1.7	136	577	6.9
Exports of semi-finished and finished industrial goods								
Total	+ 22.6	+ 9.7	+ 9.7	+ 6.6	+ 14.4	180	4 966	59.5
Intra-EEC	+ 30.4	+ 8.1	+ 9.8	+ 4.5	+ 17.8	190	2 698	32.3
To non-EEC countries	+ 14.3	+ 11.7	+ 9.6	+ 9.0	+ 10.6	169	2 268	27.2
Visible imports								
Total	+ 18.2	+ 5.9	+ 7.5	+ 4.0	+ 11.5	156	9 297	100
Intra-EEC	+ 19.0	+ 8.7	+ 8.7	+ 5.0	+ 13.2	167	5 146	55.4
From non-EEC countries	+ 17.4	+ 2.9	+ 6.0	+ 2.9	+ 9.5	144	4 151	44.6
Imports of food, beverages and tobacco								
Total	+ 16.2	+ 3.5	+ 3.9	+ 11.3	+ 9.7	152	1 253	13.5
Intra-EEC	+ 22.0	+ 13.1	+ 8.8	+ 22.7	+ 28.1	259	387	4.2
From non-EEC countries	+ 14.9	− 1.2	+ 2.5	+ 7.6	+ 3.2	128	866	9.3
Imports of raw materials, fuel and power								
Total	+ 8.5	+ 1.0	+ 0.9	+ 5.2	+ 8.6	137	1 945	20.9
Intra-EEC	− 23.8	+ 5.7	+ 7.7	+ 9 9.	+ 4.8	141	432	4.6
From non-EEC countries	+ 21.1	− 0.2	− 0.9	+ 3.9	+ 9.7	137	1 513	16.3
Imports of semi-finished and finished industrial goods								
Total	+ 22.9	+ 8.0	+ 10.5	+ 2.2	+ 12.8	163	6 099	65.6
Intra-EEC	+ 26.4	+ 8.0	+ 8.8	+ 3.3	+ 12.9	165	4 327	46.5
From non-EEC countries	+ 15.2	+ 8.1	+ 14.7	− 0.3	+ 12.6	160	1 772	19.1

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production	1968	139.1	140.6	141.2	140.0	142.6	146.3	144.8	152.3	146.8	149.6	154.7	160.2
(1963 = 100)	1969	158.2	161.7	163.5	161.3	162.0	162.9	165.4	166.0	164.2	166.6	177.9	183.0
	1970												
Unemployed	1968	95.8	87.5	89.1	84.9	81.7	81.0	79.7	77.0	74.8	74.4	70.4	66.6
(1 000)	1969	66.8	66.2	67.2	62.3	61.5	60.3	61.0	61.4	59.5	58.9	58.2	60.5
	1970	59.4	58.5										
Construction : permits for	1968	13 356	8 029	11 468	12 158	12 670	11 398	8 303	11 519	12 074	8 873	7 987	12 690
residential construction	1969	9 893	8 959	12 593	11 509	11 065	9 460	6 871	14 615	10 949	9 438	10 437	13 242
(1 000)	1970	10 015											
Private consumers' expen-	1968	166	169	171	168	176	179	171	182	174	183	181	186
diture : department store	1969	171	192	196	192	210	199	185	208	198	201		
turnover (1963 = 100)	1970												
Consumer prices	1968	123.3	124.1	124.6	125.1	125.2	125.5	125.0	126.2	126.6	127.3	127.4	127.8
(1963 = 100)	1969	132.3	133.4	134.4	135.6	135.4	135.4	134.2	134.9	135.8	136.4	136.1	135.0
	1970	136.4	137.5										
Visible imports	1968	823.0	721.7	747.9	704.9	815.1	672.8	775.2	798.3	775.9	836.0	816.8	811.2
(million u.a.)	1969	816.7	846.0	840.5	883.3	916.2	918.7	894.1	888.2	975.8	1 022.2	966.0	1 031.5
	1970	1 003											
Visible exports	1968	680.4	648.7	669.8	662.3	724.9	571.4	715.3	711.0	699.8	759.3	729.3	735.9
(million u.a.)	1969	745.2	766.9	797.6	780.4	816.1	833.8	829.2	843.0	886.6	935.2	858.5	875.1
	1970	901											
Balance of trade	1968	− 142.6	− 73.0	− 78.1	− 42.6	− 90.2	− 101.4	− 59.9	− 87.3	− 76.1	− 76.7	− 87.5	− 75.3
(million u.a.)	1969	− 71.5	− 79.1	− 42.9	− 102.9	− 100.1	− 84.9	− 64.9	− 45.2	− 89.2	− 87.0	− 107.5	− 156.4
	1970	− 102											
Official gold and foreign	1968	2 194	2 164	2 082	2 028	2 008	1 988	2 000	2 030	2 001	1 972	1 968	1 967
exchange reserves	1969	1 892	1 937	1 954	1 981	2 046	1 965	2 031	1 999	2 005	2 502	2 235	2 090
(million u.a.)	1970												
Money supply	1968	19.93	19.91	20.29	20.29	20.40	20.76	20.70	20.95	21.13	21.28	21.50	21.76
(Fl. '000 million)	1969	22.02	22.04	22.02	22.23	22.47	22.55	22.41	22.53	23.11	23.46	29.30	
	1970												

NOTES TO GRAPHS AND TABLES

Source: Statistical Office of the European Communities (except as otherwise indicated).
Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US $ 1) at the official exchange rates.

Graph 1

— Exports fob. Series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Industrial production: trend curve; estimate established on the basis of indices of the Statistical Office of the European Communities (excluding construction, food, beverages and tobacco), adjusted for seasonal and fortuitous variations.

Graph 3

— Imports cif. Series adjusted for seasonal variations; three-month moving averages.

Graph 4

— Labour market : series adjusted for seasonal variations; three-month moving averages; positie at end of month.

Graph 5

— Wages and consumer prices: indices of gross hourly earnings in industry (excluding mining, quarrying and construction); index of agreed wages. Cost-of-living index, source: CBS.

Graph 6

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

Graph 7

— Bank lending : short-term bank loans; end-of-period figures.

Table 1

— GNP at market prices.
— Industrial production: value added by industry.
— Total exports and imports: goods, services and factor income.
— Gross income per employee: income from paid employment, including employers' share of social insurance contributions.

Table 2

— Balance exports less imports: as defined for the national accounts.
— Unemployment rate; source: CBS; number of unemployed as percentage of the civilian labour force in employment.
— Prices to private consumers: price index of private consumption adjusted by the GNP deflator, computed from the national accounts.

Table 3

— Exports fob, imports cif; conversion at official exchange rates; the products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST): food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production: adjusted for seasonal variations, excluding construction and foodstuffs.
— Unemployed: end-of-month figures, adjusted for seasonal variations.
— Construction: seasonally adjusted number of dwellings authorized.
— Private consumers' expenditure: seasonally adjusted indices of department store turnovers.
— Consumer prices: not adjusted for seasonal variations.
— Imports cif, exports fob; conversion at official exchange rates; figures adjusted for seasonal variations.
— Balance of trade: difference between seasonally adjusted imports and exports.
— Official gold and foreign exchange reserves: gross reserves of gold and foreign exchange at end of month.
— Money supply: notes and coin in circulation excluding cash holdings of monetary institutions, plus sight deposits with credit institutions; seasonally adjusted end-of-month figures.

E. Belgo–Luxembourg Economic Union

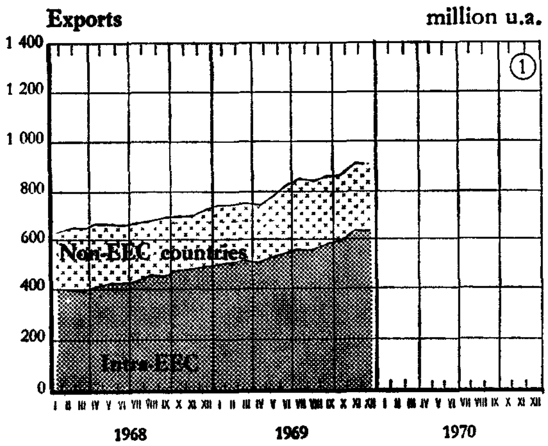
Belgium

Early in 1970 the Belgian economy was still growing fast, although the expansionary effects of export demand had weakened a little. Consumption expenditure and, even more so, investment expenditure by firms were still rising steeply. Domestic supply increased but lost elasticity, in some part at least because of labour conflicts. The coming months are expected to bring further growth of demand, production and employment, but also more imbalances. Yet the need to remove sources of strain is all the more urgent because of the introduction of the tax on value added on 1 January 1971, which needs a relatively calm economic climate if undesirable price reactions are to be avoided.

1. Recent developments

Belgium was still enjoying boom economic conditions around the turn of the year, though just lately the growth of demand has lost some of its extraordinary momentum. But since production has also become less dynamic because of very high capacity utilization and in part also because of a number of labour conflicts, the tendency for disequilibria to emerge remains very strong and finds expression mainly in a steady price rise.

Exports of goods and services were still growing fast, though there have been some signs of slackening speed since last summer. In some industries, deliveries were held up by strikes. Visible exports in December-January were shown by customs returns to be up 14.5% on the preceding year's corresponding figures (value).

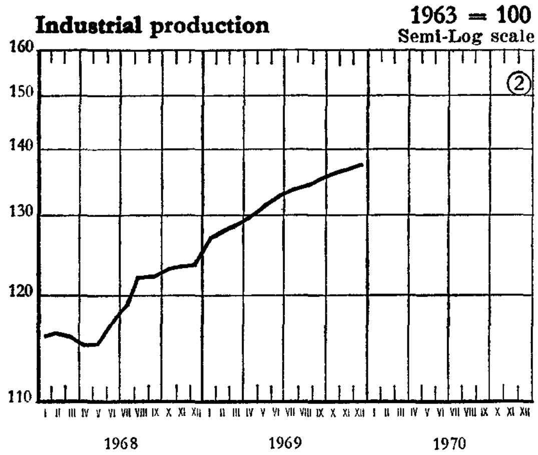


Domestic demand was still going up, and, with firms stepping up their investment spending, fixed investment may well have gained additional impetus early this year. High capacity utilization, good sales prospects and the need to rationalize were all strong investment incentives. Credit restrictions represented no real obstacle, since self-financing margins have improved and the economy's liquidity was swollen by the reflux of short-term capital from abroad from September onwards.

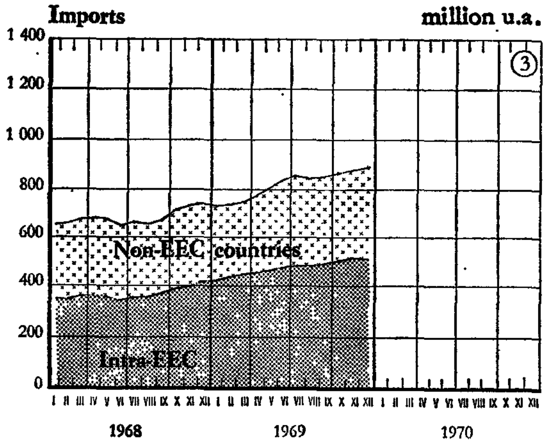
Expenditure on residential construction continued to climb, and so, probably, did public investment expenditure. Stockbuilding demand was as lively as ever.

Public consumption, and even more so, private consumers' expenditure, increased strongly. Since the end of 1969, households' disposable income has been growing even faster than before, thanks to sizable wage increases partly due to activation of the sliding wage scale, and thanks to another rise of employment. It is also likely that the propensity to consume has risen again, after faltering when the Government decided to postpone the introduction of the TVA for a year.

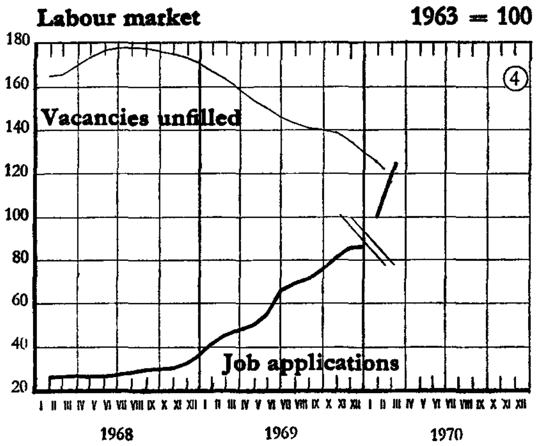
With capacity reserves all but exhausted, domestic supply expanded at a lower rate, especially industrial production. In January and February industrial output growth was also held back by social disturbances in some industries, notably coalmining and motor manufacturing.



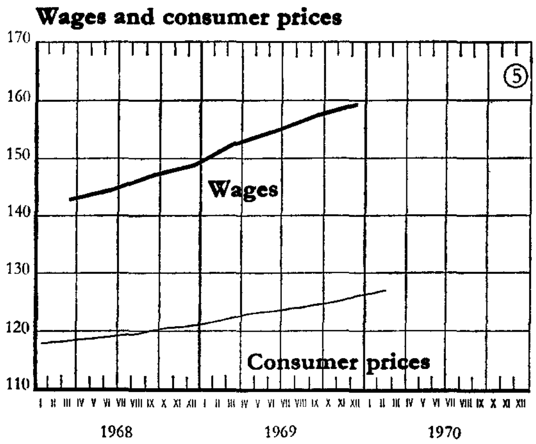
Given the demand/supply situation, rising import prices did not prevent further import growth. The value of visible imports as given by customs returns was 15.5% higher in December/January than twelve months earlier.



The economy's growing manpower requirements and the increasing strains on the labour market were reflected in an increase in the number of job vacancies, especially for skilled workers, and a decline in unemployment. By January, the seasonally adjusted unemployment rate[1] had dwindled to 1.8%. Such unemployment as still persists is largely structural or stems from the difficulties of fitting workers of limited skills into the productive process.



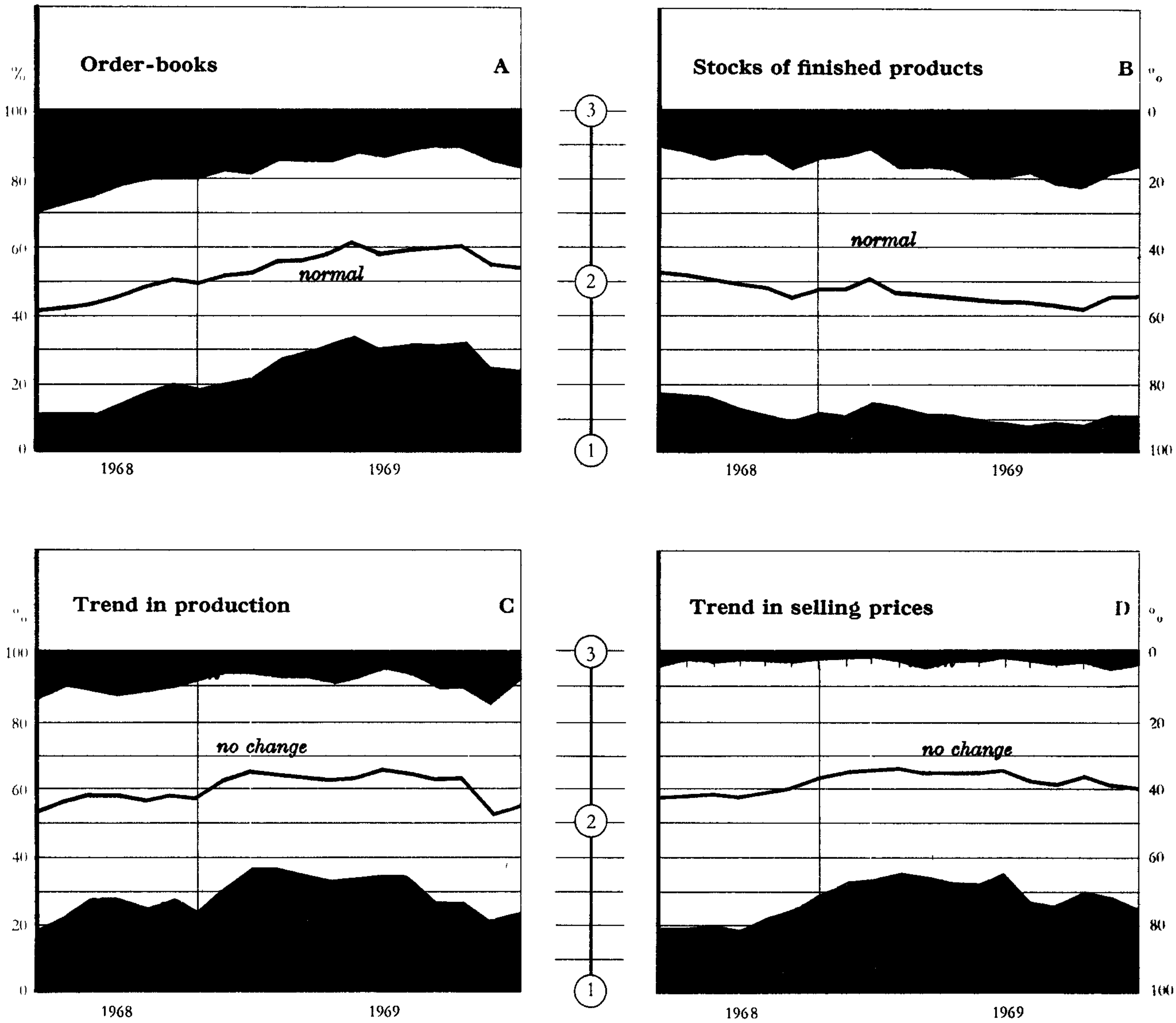
The domestic price level kept rising under the combined impact of the steady pull of demand, the strengthening push of wage costs, higher import prices and an increase in some charges for public services. Between January and March the consumer price index rose at an annual rate of more than 4.5%.



The current account (computed on a payments basis including transfer payments) has been improving ever since October, though the effects of the reversal in the leads and lags position are gradually weakening. A current deficit of Bfrs. 10 900 million during the first nine months

[1] Number of fully unemployed recipients of unemployment benefit per cent of the civilian labour force.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

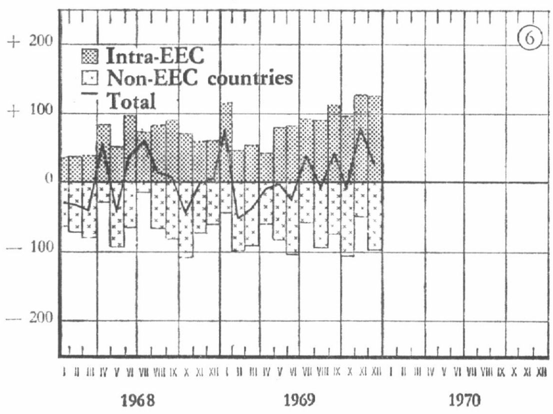
GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

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".

of 1969 gave way to a current surplus of Bfrs. 20 600 million for the months October 1969 to January 1970. With the capital account still in surplus, the BLEU overall balance of payments, which had been in deficit to the tune of Bfrs. 700 million during the first nine months of 1969, showed a surplus of Bfrs. 23 400 million during the last quarter of the year. The net gold and foreign exchange reserves of the Banque nationale declined by Bfrs. 8 400 million from January to September and then rose again by Bfrs. 15 300 million in the period October 1969 to January 1970.

Balance of Trade **million u.a.**



Unlike transactions with abroad, the trend of bank lending to business and private customers had a restrictive effect on domestic liquidity. The volume of bank credit fell considerably short of the ceilings fixed by the Banque nationale for the second half of last year. Firms covered their liquidity requirements mainly by

Demand for and supply of goods and services

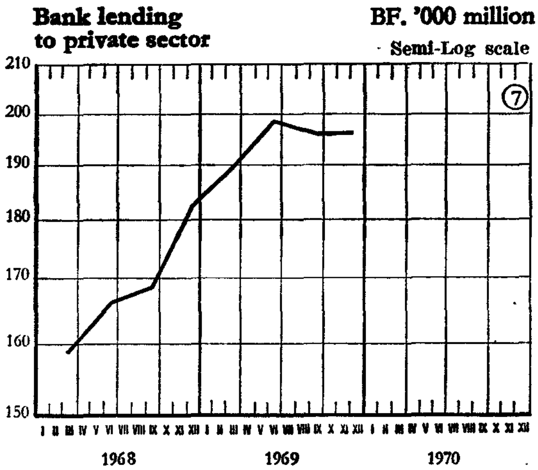
	1967 [1]	1968 [1]		1969 [2]		1970 [3]
	At current prices (in Bfrs. '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports [4]	376.8	+ 11.3	+ 11.7	+ 16½	+ 20	+ 10
Gross fixed asset formation	216.6	— 1.3	+ 1.4	+ 10½	+ 17½	+ 8½
Public current expenditure on goods and services	133.1	+ 6.8	+ 10.7	+ 6½	+ 13½	+ 5
Private consumers' expenditure	613.9	+ 4.9	+ 7.1	+ 5	+ 9½	+ 5½
Gross national product	974.6	+ 3.8	+ 6.3	+ 6½	+ 12	+ 5
Imports [4]	368.7	+ 12.9	+ 13.8	+ 16½	+ 19½	+ 10

[1] Belgian Ministry of Economic Affairs.
[2] Commission estimates.
[3] Commission forecasts.
[4] Goods, services and factor income.

Note :
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with experts from the member countries but are established and published on the sole responsibility of the Commission.

drawing further on their deposits and borrowing more from sources outside the banking system. Government and local authorities as a whole financed their requirements with less recourse to the money market, but again raised more short-term funds abroad.

Interest rates on the money and capital market have been easing down from their unprecedented peak of last September and October.



2. Outlook

It is likely that the level of activity in the Belgian economy will be very high for the rest of this year. While it is possible that the expansion of overall demand, and more especially of export demand, may gradually revert to a more normal pace, there is little elbow room for raising supply and costs are rising, so that the tendency for imbalances to persist or emerge will remain strong.

Exports, especially to countries outside the EEC, will probably grow a little less fast, if only because of the general outlook for world trade and because of the repercussions of the cooler economic climate in the United States. In addition, export growth is bound to be held back for a while by factor shortages in some sectors and because of the special structure of Belgian exports. On the other hand, the competitive strength of Belgian firms has probably suffered little so far from rising production costs, given the world-wide inflationary pressures.

Domestic demand is likely to go on expanding very briskly. This applies especially to fixed investment by firms. Even if the propensity to invest should decline during the second half of the year, curbed by shrinking profit margins and the more pronounced effects of restrictive credit policy, this will come too late to affect actual investment expenditure this year, inasmuch as investment projects on a very large scale are already in hand or planned. In its turn, public investment, especially construction by the local authorities, is likely to go on expanding considerably until the autumn. Housing investment may increase at a somewhat slower pace, though there may be a temporary spurt owing to an attempt to complete certain building projects before the TVA is introduced at the end of the year.

In contrast to fixed investment, stockbuilding is not likely to contribute anything much to economic activity during the second half of the year, since firms will no doubt wish to keep their stocks as low as possible pending the introduction of the TVA.

Private consumers' expenditure will assuredly continue to grow vigorously. In spite of a somewhat slower increase in employment, household incomes are likely to grow a good deal more quickly than in 1969, because of a very distinct rise of wages and salaries. Transfer incomes, too, will again increase fast. The proposed reduction of income tax for the lower-income brackets, although it is to be accompanied by an increase in social insurance contributions, will keep disposable incomes more closely in step with the rise of gross incomes. Finally, the prospect of higher prices due to the TVA may raise the propensity to consume towards the end of the year. But prices may well rise to such an extent that real private consumers' expenditure in the end effect does not grow any faster than in 1969.

The labour market will get more and more difficult, especially since the working week will probably be shortened. For this reason and because of the high degree of capacity utilization, industrial production is in for a period of distinctly slower growth. If the expected annual average increase still appears rather high (about 7% for value added at constant prices), this is largely because its—seasonally adjusted—level had already risen sharply earlier this year.

Imports are likely to be buoyant, in spite of a very conservative stockbuilding policy on the

The Central Government Budget

	1969		1970	1969	1970
	Original budget	Provisional results	Budget	Original budget	Budget
	Bfrs. '000 million			% changes on the preceding year's original budget	
Expenditure [1]	305.5	316.9	339.6	+ 11.7	+ 11.2
of which :					
current expenditure	250.0	262.7	278.5	+ 10.5	+ 11.4
capital expenditure [2]	55.5	54.2	61.0	+ 17.3	+ 9.9
Revenue	265.5	269.8	297.1	+ 9.5	+ 11.9
of which :					
direct taxes	103.3	107.4	121.9	+ 14.5	+ 18.0
indirect taxes	149.6	150.7	159.2	+ 7.9	+ 6.4
Net borrowing requirement [1]	40.0	47.1	42.5	.	.

[1] Disregarding debt extinction and "contingency" appropriations.
[2] Including participations, advances and loans.

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

part of firms. With export growth expected to slow down, the current account may cease to accumulate sizable surpluses and come closer to equilibrium.

With most markets for goods and services still under heavy strain, with rising wage costs and a probable deterioration of the terms of trade, prices will be subject to strong upward pressure in the months ahead. It may well turn out that the average annual rise of consumer prices exceeds any previous figure since the creation of the Common Market and indeed since 1951.

The Belgian Government's declared determination to give the fight against inflation priority over all other economic policy aims found concrete expression last November in a series of new restrictive measures.

Apart from an increase in social contributions by workers and employers with a view to covering the deficits of the State sickness and disablement insurance agency INAMI and other bodies, there is to be a selective decrease of export rebates and more purposeful differentiation of State subsidies for private investment. Stricter standards are to be applied in respect of budget management, with particular reference to the avoidance of overspending. At the same time, however, tax reliefs for incomes in the low and medium brackets were granted on a more generous scale than originally proposed.

So far as the budget is concerned, the latest stabilization package is expected to cut about Bfrs. 800 million off the deficit provided for in the budget estimates for 1970. Allowing for the pace of expenditure growth and autonomous tax changes, however, the overall effect of the budget on the economy is likely to be more expansionary than in 1969, even if the "contingency" appropriations *(tranche conjoncturelle)* remain frozen. The central government budget does not as yet, therefore, seem to be sufficiently aligned on the requirements of short-term economic policy. This verdict is all the more justified as the factors underlying the stabilization measures have altered appreciably since last September. In particular, the effectiveness of credit restrictions has been at least temporarily impaired by the reflux of capital from abroad. If the danger spots generating inflationary pressures are to be removed before the changeover to the TVA system, credit policy and, even more so, budget policy will, therefore, have to be used even more vigorously to stem inflation. Perhaps the best thing to do in this connection would be to freeze or postpone additional expenditures in the course of budget implementation, or to proceed to a temporary adjustment of current revenue.

Major economic policy measures

January

(1) Prolongation until 30 June 1970 of the system of extraordinary grants for the accelerated conversion and development of certain regions and of tax reliefs applicable to company mergers and splits, to losses brought forward and to certain dividend taxes.

(2) Entry into force of new regulations for the computation of social insurance contributions. Workers' holiday pay becomes part of the assessment basis for social insurance contributions. The overall effect of the new social insurance provisions is to raise social contributions by a total of Bfrs. 2 900 million, of which about Bfrs. 900 million are payable by workers.

(3) Entry into force of the law introducing "programme contracts" (agreed prices), the principal aim of which is to mitigate the effects of the TVA on the price level.

(4) Entry into force of the regulations requiring firms employing at least 20 workers to notify all group dismissals and job vacancies.

(5) Reduction of export tax rebates from 6 to 5% for a number of products (including chemical products, rubber, hides and leather, products of metal-using industries, optical instruments, measuring instruments, weapons and ammunition) and diminution of a number of tax-free allowances.

(6) A draft law involving changes in direct taxation is introduced in the Chamber. The changes are intended to "offset to some extent the effects of progressive taxation on the rise of money incomes" and concern reliefs for lower incomes (higher tax exemption limits, allowable occupational expenses and tax-deductible family expenses), tax exemption for income from savings deposits (up to Bfrs. 7 500 instead of Bfrs. 5 000), and the permissible proportion of financial costs in general operating expenditure (which may exceed 9% per year). It is estimated that the tax reduction on low incomes will cost Bfrs. 1 400 million.

February

(1) On 1 February new regulations enter into force which raise the down-payment and shorten the redemption period for hire-purchase and personal loans. For passenger cars, the time-limit is reduced from 30 to 24 months and the down-payment raised from 30 to 35%.

(2) The delay between the implementation and the notification of a price increase is lengthened from 21 to 30 days. In addition, the Minister of Economic Affairs is given power by the new regulations to postpone the application of a price increase twice by 14 days. The maximum delay is thus extended to 2 months.

(3) The Ministerial Committee for Economic and Social Co-ordination approves an increase in railway fares as of 1 March 1970. Ordinary fares are raised by 2.5% and the price of season tickets by 10%.

TABLE 1 : **Key indicators**

	1964	1965	1966	1967	1968	1968
	% ckange by volume on preceding year					Indices 1963 = 100
Gross national product	+ 6.9	+ 3.9	+ 2,8	+ 3.4	+ 3.8	122
Industrial production	+ 10.5	+ 3.0	+ 4.5	+ 2.2	+ 4.4	127
Total imports	+ 10.7	+ 6.6	+ 8.4	+ 3.5	+ 12.9	149
Private consumers' expenditure	+ 3.6	+ 4.6	+ 3.2	+ 2.7	+ 4.9	121
Public current expenditure on goods and services	+ 3.9	+ 5.6	+ 4.3	+ 6.0	+ 6.7	130
Gross fixed asset formation	+ 12.4	+ 3.7	+ 7.2	+ 0.8	— 0.8	124
Total exports	+ 11.1	+ 7.7	+ 3.8	+ 6.7	+ 11.3	147
Gross national product per head of population	+ 5.9	+ 2.6	+ 2.1	+ 2.8	+ 3.4	118
Gross national product per person in employment	+ 10.6	+ 8.3	+ 7.2	+ 7.2	+ 6.4	120
	% change by value on preceding year					
Gross income per employee	+ 9.7	+ 9.0	+ 8.5	+ 6.6	+ 7.1	148

TABLE 2 : **Indicators for internal and external equilibrium**

	1964	1965	1966	1967	1968
Balance exports less imports					
in million u.a.	0	+ 162	– 68	+ 162	+ 28
as percentage of GNP	0	+ 1.0	– 0.4	+ 0.8	+ 0.1
Unemployment rate	1.4	1.5	1.7	2.4	2.8
prices to private consumers (% change on preceding year)	+ 3.8	+ 3.9	+ 4.4	+ 2.7	+ 2.1

Belgium

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					Indices 1963=100	Million u.a.	% of totals
	1964	1965	1966	1967	1968	1968	1968	1968
Visible exports								
Total	+ 15.5	+ 14.2	+ 5.2	+ 3.0	+ 16.0	169	8 155	100.0
Intra-EEC	+ 19.0	+ 12.8	+ 6.1	+ 3.2	+ 18.5	178	5 248	64.4
To non-EEC countries	+ 10.3	+ 16.5	+ 3.9	+ 2.5	+ 11.7	154	2 907	35.6
Exports of food, beverages and tobacco								
Total	+ 3.2	+ 31.5	+ 8.4	+ 18.8	+ 15.5	202	640	7.8
Intra-EEC	+ 5.2	+ 81.6	+ 5.4	+ 25.7	+ 24.6	228	524	6.4
To non-EEC countries	− 2.1	+ 81.3	+ 17.1	+ 1.3	− 13.4	132	116	1.4
Exports of raw materials, fuel and power								
Total	+ 2.3	+ 3.1	+ 0.5	− 2.4	+ 13.4	117	692	8.5
Intra-EEC	+ 5.2	+ 1.4	+ 1.5	− 3.6	+ 10.8	116	413	5.1
To non-EEC countries	− 2.1	+ 5.9	− 1.0	− 0.5	+ 17.4	120	279	3.4
Exports of semi-finished and finished industrial goods								
Total	+ 18.5	+ 14.4	+ 7.7	+ 2.3	+ 16.4	174	6 823	837
Intra-EEC	+ 22.3	+ 12.7	+ 9.8	+ 1.9	+ 18.7	183	4 311	52.9
To non-EEC countries	+ 12.7	+ 17.1	+ 4.2	+ 2.9	+ 12.8	160	2 512	30.8
Visible imports								
Total	+ 15.9	+ 7.6	+ 12.6	0	+ 16.1	163	8 333	100.0
Intra-EEC	+ 17.5	+ 10.1	+ 15.4	− 0.6	+ 14.8	170	4 577	54.9
From non-EEC countries	+ 14.0	+ 4.8	+ 9.1	+ 0.6	+ 17.8	155	3 757	45.1
Imports of food, beverages and tobacco								
Total	+ 16.8	+ 15.2	+ 8.1	+ 10.0	+ 2.8	164	1 009	12.1
Intra-EEC	+ 16.3	+ 22.5	+ 10.6	+ 11.8	+ 24.0	219	520	6.2
From non-EEC countries	+ 17.2	+ 10.6	+ 6.4	+ 8.6	− 13.1	130	489	5.9
Imports of raw materials, fuel and power								
Total	+ 14.3	+ 1.5	+ 1.1	− 2.1	+ 22.8	141	1 972	23.7
Intra-EEC	+ 12.9	+ 3.1	+ 5.2	− 5.5	+ 17.6	136	678	8.1
From non-EEC countries	+ 4.4	+ 0.6	− 1.3	− 0.2	+ 25.7	143	1 294	15.5
Imports of semi-finished and finished industrial goods								
Total	+ 16.4	+ 8.8	+ 18.3	− 1.1	+ 16.7	173	5 352	64.2
Intra-EEC	+ 18.9	+ 10.3	+ 18.4	− 1.1	+ 13.0	173	3 379	40.5
From non-EEC countries	+ 12.1	+ 6.2	+ 18.1	− 1.2	+ 23.6	173	1 974	23.7

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1968	*114.8*	*115.1*	*117.3*	*111.0*	*114.6*	*124.0*	*116.9*	*123.6*	*125.9*	*119.5*	*125.0*	*126.4*
	1969	*130.5*	*127.8*	*130.7*	*125.5*	*133.6*	*138.5*	*134.7*	*136.3*	*125.3*	*135.8*	*139.9*	*140.5*
	1970												
Unemployed (1 000)	1968	*99.2*	*99.9*	*103.4*	*104.2*	*104.4*	*104.3*	*104.4*	*103.6*	*103.4*	*103.6*	*101.4*	*99.6*
	1969	*95.3*	*93.8*	*90.4*	*88.5*	*86.3*	*83.6*	*83.6*	*82.2*	*82.3*	*80.4*	*76.8*	*74.7*
	1970	*68.7*	*70*										
Construction: permits for residential construction (1 000)	1968	*3 158*	*2 189*	*3 427*	*2 507*	*3 374*	*2 810*	*3 447*	*3 277*	*2 988*	*3 701*	*3 458*	*3 297*
	1969	*3 243*	*3 657*	*3 056*	*4 179*	*3 964*	*4 254*	*4 600*	*4 117*				
	1970												
Private consumers' expenditure: department store turnover (1963 = 100)	1968	*128*	*133*	*133*	*133*	*139*	*135*	*136*	*141*	*134*	*134*	*145*	*138*
	1969	*144*	*138*	*145*	*142*	*159*	*146*	*144*	*154*	*145*	*150*	*149*	*155*
	1970												
Consumer prices (1963 = 100)	1968	118.20	118.27	118.38	118.63	118.76	119.18	119.41	119.52	120.00	120.46	120.48	120.91
	1969	121.44	121.96	122.62	122.95	123.32	123.65	124.10	124.28	124.64	125.14	125.70	126.20
	1970	126.73	127.12										
Visible imports (million u.a.)	1968	*644.1*	*703.8*	*682.8*	*644.7*	*706.4*	*591.3*	*670.8*	*- 673.2*	*669.5*	*793.5*	*706.6*	*716.3*
	1969	*765.9*	*746.3*	*778.0*	*813.7*	*830.5*	*859.0*	*871.2*	*779.9*	*867.1*	*932.8*	*827.3*	*881.4*
	1970												
Visible exports (million u.a.)	1968	*617.8*	*671.7*	*645.6*	*701.6*	*663.3*	*627.5*	*728.3*	*682.3*	*672.5*	*749.9*	*701.8*	*720.2*
	1969	*840.0*	*694.4*	*740.6*	*799.4*	*826.6*	*834.1*	*907.1*	*770.5*	*909.1*	*919.8*	*903.4*	*906.8*
	1970												
Balance of trade (million u.a.)	1968	*− 26.3*	*− 32.1*	*− 37.2*	*+ 56.9*	*− 43.1*	*+ 36.2*	*+ 57.5*	*+ 9.1*	*+ 3.0*	*− 43.6*	*− 4.8*	*+ 3.9*
	1969	*+ 74.1*	*− 51.9*	*− 37.4*	*− 14.3*	*− 3.9*	*− 24.9*	*+ 35.9*	*− 9.4*	*+ 42.0*	*− 13.0*	*+ 76.1*	*+ 25.4*
	1970												
Official gold and foreign exchange reserves (million u.a.)	1968	2 168	2 116	2 150	2 116	2 090	1 996	1 972	1 964	1 888	1 896	1 902	1 886
	1969	1 898	1 890	1 880	1 950	2 000	2 024	2 032	2 100	2 106	2 202	2 200	2 232
	1970	2 218											
Money supply (Bfrs '000 million)	1968	*347.7*	*348.3*	*354.1*	*355.7*	*358.7*	*360.3*	*358.0*	*361.9*	*361.9*	*363.0*	*366.8*	*367.4*
	1969	*369.5*	*376.1*	*376.5*	*378.0*	*377.7*	*380.4*	*375.4*	*376.6*	*374.0*	*376.3*	*374.4*	*376.0*
	1970	*380*											

NOTES TO GRAPHS AND TABLES

Source: Statistical Office of the European Communities (except as otherwise indicated).
Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US $ 1) at the official exchange rates.

Graph 1

— Exports fob : series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Industrial production: trend curve; estimate established on the basis of indices of the Statistical Office of the European Communities (excluding construction, food, beverages and tobacco), adjusted for seasonal and fortuitous variations.

Graph 3

— Imports cif : series adjusted for seasonal variations; three-month moving averages.

Graph 4

— Labour market : series adjusted for seasonal variations; three-month moving averages; position at end of month.

Graph 5

— Wages and consumer prices: agreed wages for manual workers, all branches, source: Ministère du Travail et de l'Emploi; consumer prices, source: Ministère des Affaires Economiques.

Graph 6

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

Graph 7

— Bank lending : loans made by monetary institutions; end-of-period figures.

Table 1

— GNP at market prices.
— Industrial production : value added by industry.
— Total exports and imports : goods, services and factor income.
— Gross income per employee : income from plaid employment (including employer's share of social insurance contributions).

Table 2

— Balance exports less imports : as defined for the national accounts.
— Unemployment rate : number of unemployed as percentages of the civilian labour force in employment.
— Consumer prices: implicit price index of private consumption computed from the national accounts.

Table 3

— Exports fob, imports cif; conversion at official exchange rates; the products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST): food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

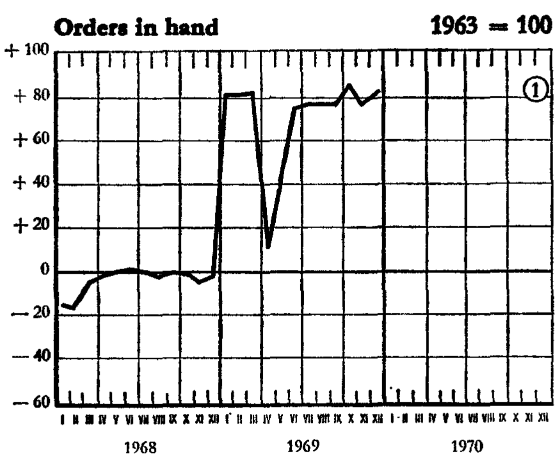
— Industrial production: adjusted for seasonal variations, excluding construction, food, beverages and tobacco.
— Unemployed: end-of-month figures, adjusted for seasonal variations.
— Construction: seasonally adjusted number of residential buildings authorized.
— Private consumers' expenditure: seasonally adjusted indices of department store turnovers.
— Consumer prices: not adjusted for seasonal variations.
— Imports cif, exports fob; conversion at official exchange rates; figures adjusted for seasonal variations.
— Balance of trade: difference between seasonally adjusted imports and exports.
— Official gold and foreign exchange reserves: gross reserves of gold and foreign exchange at end of month.
— Money supply: notes and coin in circulation, excluding cash holdings of the Treasury, the Central Bank and other banking institutions other than the Post Office giro; residents' sight deposits (up to one month) with banking institutions; sums held with the Post Office giro, the special Treasury accountants and non-residents; adjusted for seasonal variation; at end of month.

Luxembourg

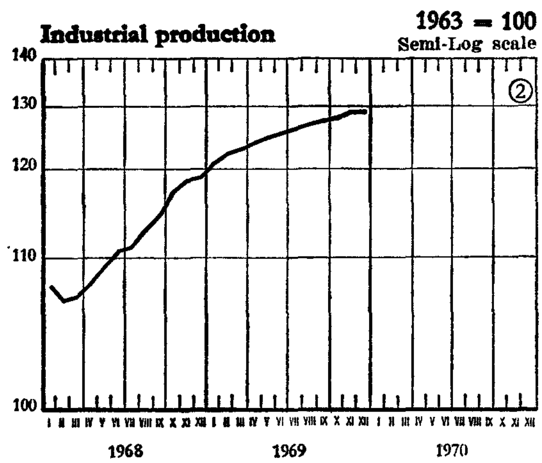
The economic upswing continued early in 1970, though the rate of increase in production and employment slowed down because most industries are working at capacity and the labour shortage is becoming more and more pronounced. While the coming months may bring a weakening of export demand, especially for the products of the iron and steel industry, the Luxembourg economy will probably remain exposed to considerable strain.

1. Recent developments

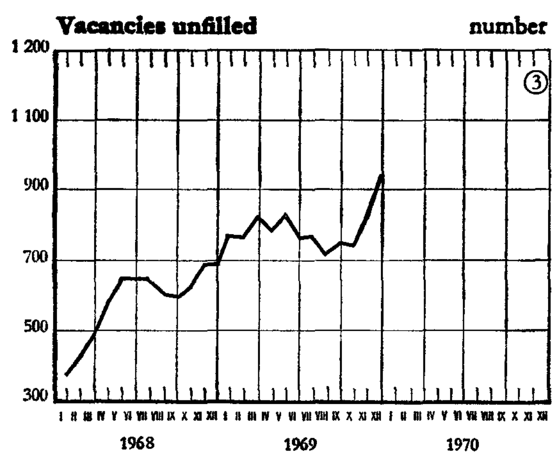
Until the end of 1969 the flow of orders from abroad was well in excess of delivery potential. Since then, in the early months of 1970, export demand, especially for iron and steel products, has been declining a little. But while (seasonally adjusted) sales to other Community countries fell off slightly, those to non-member countries, which so far had been on a hesitant course, began expanding faster. Export prices have been climbing distinctly less steeply.



The vigorous expansion of domestic demand continued, with gross fixed asset formation in the lead. In the iron and steel industry investment growth slackened very slightly; elsewhere in industry there is still a clear upward trend. Investment in residential construction increased fast. In spite of the freezing of the "contingency" appropriations for investment expenditure on administration, schools and hospitals, public investment probably went up a good deal early this year.

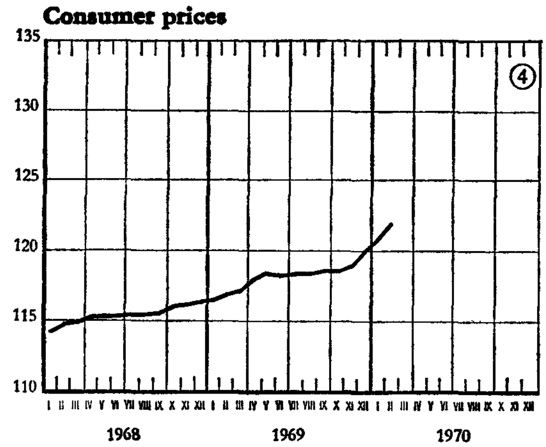


Private consumers' expenditure has clearly picked up speed. Since the beginning of the year household incomes have been rising faster.



The pay awards under the new collective agreement in the iron and steel industry set the pattern for a steeper increase in the wage bill, transfer incomes rose and disposable incomes were further swollen because of the decision to adjust income tax rates to the cost-of-living increase from the beginning of 1970 onwards, in order to mitigate the "overkill" effects of progressive taxation on incomes increasing merely in line with inflation.

High capacity utilization and steadily increasing labour shortages over a wide range of skills were reflected in the failure of domestic supply to keep up its previous rate of expansion. Even so, the STATEC index of industrial production for December and January was still 6.5% above its level of a year earlier. To judge from such information as is available on imports, a good deal more reliance had to be placed on supplies from abroad.



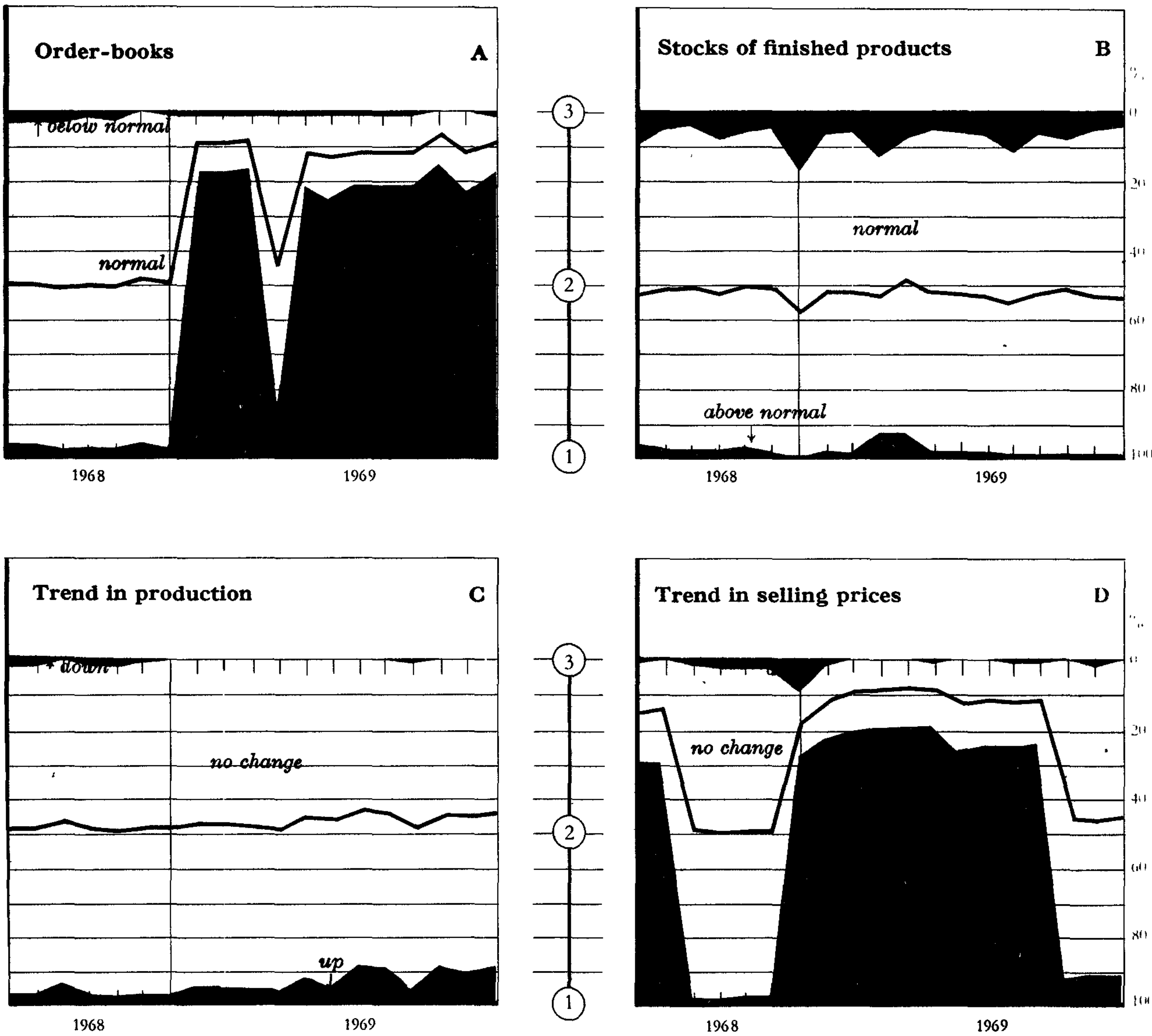
Demand for and supply of goods and services

	1967[1]	1968[1]		1969[1]		1970[2]
	At current prices (in Lfrs. million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports[3]	27 960	+ 10.2	+ 10.2	+ 13½	+ 19	+ 6½
Gross fixed asset formation	8 883	+ 3.2	+ 7.3	+ 17½	+ 25½	+ 10
Public current expenditure on goods and services	4 245	+ 3.1	+ 7.1	+ 2	+ 5½	+ 1½
Private consumers' expenditure	21 648	+ 4.3	+ 7.0	+ 4½	+ 7	+ 5½
Gross national product	35 412	+ 4.0	+ 7.1	+ 7	+ 13	+ 3½
Imports[3]	27 324	+ 9.4	+ 9.5	+15	+ 18	+ 10

[1] Service central de la statistique et des études économiques (STATEC), Luxembourg.
[2] Commission estimates.
[3] Goods, services and factor income.

Note :
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with experts from the member countries but are established and published on the sole responsibility of the Commission.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

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

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

The price climate has become distinctly worse during the last few months, although the Government's price policy, and especially the freeze of trading margins as well as the temporary reduction of TVA rates for certain goods and services, has done much to offset the price effects of the introduction of TVA. Nevertheless the cost of living was forced up by higher rents, food prices and import prices. Between November and February the index rose by 2.7%, and in February exceeded its February 1969 level by 4.2%.

2. Outlook

The expected slower increase of production in the capital goods industries and the restoration of normal steel stocks in the major importing countries are likely to depress world demand for Luxembourg steel products in the period up to the end of 1970. In spite of export expansion in other sectors, notably chemicals, and of the beneficial effects of the transition to the TVA system, therefore, total exports are likely to rise a good deal less fast than in 1969.

Domestic demand will no doubt go on expanding vigorously. No weakening of the contribution from gross fixed asset formation is expected before the end of the year, for any curtailment in the investment plans of public enterprises should be offset by a persistently high propensity to invest of private firms. Residential construction may slow down under the impact of inelastic labour supply and quickly rising prices.

The dynamic factors mentioned in connection with the recent income growth in private

The Central Government Budget

	1969		1970	1969	1970
	Original budget	Revised budget	Budget	Original budget	Budget
	Lfrs. '000 million			% changes on the preceding year's original budget	
Expenditure [1]	10.2	10.1	10.8	+ 7.6	+ 6.8
of which :					
current expenditure	8.2	8.2	8.8	+ 9.0	+ 7.8
capital expenditure [2]	2.0	1.9	2.0	+ 2.2	+ 2.6
Revenue	8.8	8.9	9.5	+ 6.0	+ 9.1
of which :					
direct taxes	4.3	4.3	4.8	+ 10.1	+ 12.4
indirect taxes	3.6	3.8	4.0	— 0.8	+ 10.1
Net borrowing requirement [1]	1.4	1.2	1.3	.	.

[1] Disregarding debt extinction.
[2] Including participations, advances and loans.

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

households will help in the months ahead to keep private consumers' expenditure expanding fast. Wage incomes will receive an additional boost in 1970 from more frequent adjustments under the sliding wage scale in connection with the rising cost-of-living index. Finally, the volume of employment can be expected to go up again.

In the light of the budget estimates for 1970, public consumption expenditure must be expected to rise faster than before.

The combination of slower productivity rises with some flattening out in the rapid expansion of demand might well cause industrial production to rise no more than moderately in the next few months. Allowing for the very high level of output in industry and building early this year, the real gross national product should rise in 1970 by altogether 3½%, that is a little more than was assumed in the last Quarterly Survey.

Although import prices should rise less fast in the future, the combined effect of excess demand and the gradual working through of the TVA may well push up domestic prices again quite noticeably during the next few months. The external balance is likely to deteriorate.

In view of the presence of rather intractable inflationary pressures, the authorities have implemented as vigorously as possible the stabilization programme announced at the beginning of November.[1]

This programme has to be judged in terms of its purpose, which is the creation of conditions—including especially a better psychological climate—by which to avoid a cumulative wage/price spiral. Parliament's decision to cut the 1970 budget deficit from the originally proposed amount of Lfrs. 1 260 million to Lfrs. 1 200 million should assist the restrictive policy. Tax revenues will no doubt be well in excess of estimates because of the continuing boom; yet, from the point of view of stabilizing the economy quickly and in particular lessening the strain in the building sector, it might be even better to observe the utmost caution in budget spending. To this end the appropriations in the 1970 budget for the contingency programme of the Public Funds should remain frozen, and certain other public expenditures should be curtailed or postponed.

Major economic policy measures

January

(1) Entry into force of certain measures forming part of the stabilization programme announced in November 1969. In the fiscal sphere, TVA rates on certain foods and pharmaceuticals, and on processed tobacco, and those applicable to hotels and restaurants, are reduced by half for the period January-June. The Government has powers to prolong these measures, wholly or partly, for up to six months beyond 1 July.

(2) With effect from 1 January 1970 income tax rates are adjusted in relation with the cost-of-living index. The loss of revenue entailed by this measure is estimated at about Lfrs. 75 million.

(3) The statutory minimum wage is raised from Lfrs. 33 to 34 per hour.

(4) Maximum prices become applicable for sales of furniture, household appliances, lamps and solid fuels, and retailers' margins are fixed for the sale of fruit and vegetables.

(5) Maintenance of the temporary fiscal investment incentives.

(6) Introduction of a draft law regarding the establishment of a national industrial corporation to provide venture capital, of a national credit institute to provide loan capital for investment in plant and machinery, and a national rediscount and guarantee agency.

March

(1) Adoption of a number of restrictive measures in the field of monetary and credit policy:

(a) Recommendation to private and autonomous public credit institutes to be more selective in granting long-term loans for building;

[1] The restrictive measures forming part of this programme are summarized in the last Quarterly Survey, 1969 — No. 3/4.

(b) Curtailment of the credit demand of local authorities, whose construction projects are to be reviewed by a special commission before they can qualify for loans;

(c) Greater stringency in granting consumer credits, which may expand by at most 5% during the first half of 1970;

(d) Increase in the interest rates of the State savings bank and other financing institutions.

(2) With effect from 1 March another increase in the statutory minimum wage, to Lfrs. 35 per hour.

(3) Measures to encourage the employment of foreign workers.

Luxembourg

TABLE 1 : **Selected monthly indicators**

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1968	*101.8*	*104.1*	*110.6*	*108.6*	*111.3*	*112.2*	*109.7*	*114.6*	*117.1*	*116.2*	*118.5*	*119.6*
	1969	*122.1*	*123.4*	*125.5*	*125.1*	*123.2*	*128.1*	*126.1*	*126.7*	*130.7*	*129.8*	*133.6*	*131.5*
	1970												
Unfilled vacancies	1968	*456*	*499*	*517*	*728*	*737*	*651*	*586*	*577*	*645*	*692*	*751*	*670*
	1969	*890*	*744*	*825*	*819*	*853*	*647*	*824*	*684*	*746*	*810*	*955*	*1 081*
	1970												
Construction : permits for residential construction	1968	*29*	*12*	*17*	*16*	*18*	*9*	*23*	*15*	*19*	*14*	*22*	*14*
	1969	*16*	*23*	*11*	*29*	*12*	*58*	*27*	*27*	*15*	*35*	*27*	
	1970												
Consumer prices (1963 = 100)	1968	114.24	114.83	114.95	115.19	115.09	115.19	115.41	115.40	115.59	116.12	116.29	116.74
	1969	116.96	117.08	117.30	117.57	118.08	117.94	118.26	118.11	118.31	118.39	118.77	120.03
	1970	121.21	121.98										

NOTES TO GRAPHS AND TABLES

Source: Statistical Office of the European Communities (except as otherwise indicated).

Graph 1

— Orders in hand; source: EEC Business Survey; balance between percentage of managements reporting order books to be above normal (+) and those reporting them to be below normal (—).

Graph 2

— Industrial production: trend curve; estimate established on the basis of indices of the Statistical Office of the European Communities (excluding construction, food, beverages and tobacco), adjusted for seasonal and fortuitous variations.

Graph 3

— Unfilled vacancies: series adjusted for seasonal variations; three-month moving averages.

Graph 4

— Consumer prices; source: STATEC.

Table

— Industrial production: adjusted for seasonal variations, excluding construction and foodstuffs.
— Unfilled vacancies: seasonally adjusted end-of-month figures.
— Construction: seasonally adjusted number of residential buildings authorized.
— Consumer prices: not adjusted for seasonal variations.

Brussels, 22 December 1969

Memorandum from the Commission to the Council on the Community's economic policy in 1970

In July 1969 the Council discussed the problems raised by the development of an inflationary trend in the Community; it endorsed the conclusions of the Commission Memorandum discussing guidelines for a short-term economic policy that would ensure balanced economic growth in the Community. Since then, the Member States have taken far-reaching measures, including the changes in the parities of the French franc and the German mark, with a view to restoring basic equilibrium to their economies.

Developments in the past few months have shown, however, that the inflationary strains are still severe or have even increased. Should they persist at their present level, expansion may fairly soon get completely out of control, and the authorities would then have to resort to a policy of almost Draconian restrictions. The consequences of such a policy could be made even more serious by the concurrent cooling of the economic climate outside the Community.

It therefore appears necessary to lay down the guidelines for short-term economic measures which will redress the Community's economic situation in 1970 and will ensure that short-term economic policy can, if need be, be revised in such a way as to offset any slowdown in world economic activity.

I. Economic developments in the second half of 1969

In the second half of 1969, the strains inherent in the business situation were mounting in most member countries and the gap between supply and demand was widening further.

Exports to non-member countries continued to climb. The expansion of private consumers' expenditure also gathered appreciable momentum, mainly as a result of substantial wage increases, particularly in Germany and Italy. Only in France has the rise in spending by households recently started to flatten out. Corporate investment activity is still running at a high level. The only sectors where growth appears to have been less rapid than in the first half of 1969 were public sector investment and in some countries also residential construction.

At the same time, the growth of production is increasingly being impeded by bottlenecks. This can be seen from the growing discrepancy between the number of persons seeking employment and the number of unfilled vacancies, the rising level of technical capacity utilization, the increase in the backlog of orders and the lengthening of delivery dates. Productivity gains have been substantially smaller. Seasonally adjusted, unemployment has in most member countries fallen to an extent that hardly allows of further reduction.

In almost all member countries the mounting strains in the economy are reflected mainly in a faster rise in prices. The higher cost of imports and the rise in domestic costs are easy to pass on in prices.

The imbalances are also reflected in increasingly heavy strains on the money and capital markets; interest rates have continued to rise, reaching a very high level on the money markets of all Member States.

The Community's balance of trade has persistently deteriorated; while in 1968 it had run a surplus of $1 750 million, it will close with a deficit in 1969.

The parity changes in Germany and France are of too recent a date for their effects to allow of precise assessment at this stage. The information available suggests, however, that the inflow of capital and the trend of the gold and foreign exchange reserves have been reversed. A substantial volume of short-term capital has left Germany again; from the end of September to the beginning of December, the Bundesbank sold some DM 19 000 million worth of foreign currency on the foreign exchange market. France registered substantial returns of capital, after a sluggish period due to the uncertainty surrounding the parity of the D-mark.

The direct effects of the parity changes on the other countries of the Community appear to be marginal, the only exception being the movement of capital to the Benelux countries, where there was a heavy inflow of foreign exchange after the DM revaluation.

II. Economic outlook and problems

1. *General survey*

The parity changes decided upon in Germany and France have made it easier for the two countries to achieve certain basic economic aims without placing major difficulties in the way of the other Community countries. The revaluation of the mark is likely to curb the upward thrust of domestic prices in 1970 and contribute to a reduction of the heavy surplus on current account. The devaluation of the French franc holds out hopes of a progressive improvement of France's external balance during the year.

The economic trend in almost all Community countries is currently characterized by a rise in aggregate demand that is unduly sharp when compared with the limited possibilities for an expansion of overall production.

Only in France does there appear to be hope, as a result of the rigorous measures adopted in the second half of 1969, of a slowdown in the expansion of domestic demand. In the other countries, household spending on consumption is likely to rise as rapidly as at present, if not faster. Even if investment plans, which continue to expand sharply in most countries, were revised downwards, the execution of orders already on hand would by itself ensure that the very lively investment activity of enterprises would be maintained in the months ahead.

The scale of the prospective imbalances hampers action (which from every point of view is indispensable) to curb the vigorous and widespread upward thrust of production costs.

The difficulties inherent in the internal economic situation of the Community must—as has already been pointed out in the Commission's previous memorandum—be assessed in the light of the uncertainties surrounding the trend of world economic activity in 1970.

In the United States, the expansion of demand has slowed down considerably. In the third quarter of 1969, the annual growth rate of private consumers' expenditure in terms of value fell to 6%, compared with 8% in the first quarter, and fixed investment by the private sector dropped to 3.2%, against 16.8% in the first quarter (seasonally adjusted figures). The result was a very slow but steady decline in industrial production (2% between July and November 1969) and a tendency for unemployment to go up (the rate rose from 3.3% in the first quarter of 1969 to 3.7% in the third quarter of 1969). As, however, the upward thrust of prices does not yet appear to be easing, the auhorities are considering the maintenance of a rigid money and credit policy as well as of an extremely strict budget policy that is calculated to produce a substantial surplus on the Federal budget. In the circumstances, economic activity in the United States must be expected to cool down in the course of 1970 and this would entail a decline in imports. The chief points of uncertainty are the vigour and the duration of the slowdown. The main impact on world trade is probably to be expected for the second half of 1970.

In 1970 numerous other industrial countries will no doubt find themselves compelled to reinforce the measures they have already taken to combat the upward thrust of prices and avoid balance-of-payments difficulties. An exception is Great Britain, where the substantial improvements in the balance of payments in 1969, coupled with the favourable outlook for the first half of 1970, will no doubt make it possible to refrain from tightening the restrictions on the expansion of domestic demand and imports, despite substantial repayment of foreign debts.

All in all, the trend of visible trade between the industrial countries threatens to lose more and more of its vigour in the course of 1970. The Community may therefore fail to bring its inflationary strains sufficiently under control if external influences on demand should threaten to affect the pace of economic activity—as is likely to happen in the second half of 1970.

Persistence of the strong rise in prices and costs and a considerable deterioration in the current account would then make it almost impossible to change the line of short-term economic policy. For such a situation to be avoided, it is for the present indispensable to give priority to the removal of the imbalance between supply and demand. Its early elimination is of great importance, as the rise in costs and its impact on prices may even then persist for some time.

As internal and external equilibrium is gradually being restored by means of co-ordinated measures, action should also be taken not only to free the movement of goods and capital between Community countries as rapidly as possible from the obstacles introduced in the past few years, but indeed to provide fresh stimuli for their movement.

2. *Outlook and problems in the Member States*

In Germany, consumption and private investment will expand rapidly. The effects of revaluation, on the other hand, will take a comparatively long time to make themselves fully felt, and so will not suffice to dampen the rise in overall demand and prices speedily enough. It is important that Germany should rapidly return to a reasonable price trend compatible with the maintenance of satisfactory economic growth. If the excessive inflationary tendencies were to persist, it would sooner or later be necessary to apply a policy of very rigorous restraint. The stagnation of the German economy which might ensue would have a severe impact on the Community as a whole. The consequences would be all the more serious if, as may happen, they coincide with a slowdown in external demand. Today the German authorities have more room for manœuvre to avoid such a situation, since revaluation has reduced the conflict that had existed between the twin aims of domestic equilibrium and external equilibrium.

In France, the budgetary and monetary measures taken in the past few months will have a dampening effect on demand and on domestic liquidity; they will help to put the current account on a sound footing, inasmuch as the dampening effect will reinforce the switch of domestic supply into exports, already encouraged by the price advantages gained through devaluation of the franc. The heavy demands made on the production apparatus, which are likely to persist for some months even in 1970, the seeds of additional inflationary tendencies contained in devaluation, and the danger of a slackening of export demand in the second half of 1970 suggest, however, that France's external equilibrium can be consolidated only by way of a rapid return to economic equilibrium at home. Unless the expansion of domestic demand is rapidly curbed, the precarious external situation will substantially narrow the room for manœuvre when the French economy is to be steered into a new phase of lasting growth.

In Italy, there is increasing evidence of strains, following a comparatively balanced first half of the year. The upward thrust of prices has become distinctly steeper; labour disputes have led to stoppages of substantial proportions. Considerable wage increases have been awarded, and the overall balance of payments now shows a sizable deficit. Although production elasticity in Italy continues to be larger than in the other Member States, several factors such as the rise in wages, the appreciable increase in welfare payments, and the growth of excess demand as a result of the strikes promise a very sharp expansion of domestic demand for the second half of 1970. In the circumstances there is a great danger of reciprocal action which could add to existing strains and touch off a wage and price spiral.

In the Netherlands, where the pressure on resources may ease as a result of developments in the export sector, the conditions for economic equilibrium at home will nevertheless remain precarious in 1970. Private consumers' expenditure in particular will still rise appreciably. Disinflation of the economy is all the more important as it is one of the conditions which both sides of industry wish to see fulfilled if they are to participate in measures to moderate the rise in incomes.

In the Belgo-Luxembourg Economic Union, overall demand will continue to expand, even though exports, particularly those to non-member countries, can be expected to slow down.

In Belgium, demand will also receive very lively stimuli from private consumers' expenditure and corporate investment, with the result that during the greater part of the year the pace of economic growth will be largely determined by the availability of production capacity. The need to moderate the pressure of domestic demand as 1970 advances is evidently all the greater as the system of tax on value added is to be introduced on 1 January 1971.

In Luxembourg, where the decision to introduce the TVA system from the beginning of 1970 was maintained, it would seem urgently necessary to ensure a slowdown in the expansion of consumption and building investment, in view of the higher prices that are being paid for imports, particularly from Germany.

III. Guidelines for short-term economic policy

The economic outlook outlined above shows the need for disinflation in all Member States and the advisability of rapid action. This is the only way of returning to a sound economic situation without falling into stagnation or recession. Energetic measures, concentrated on the first half of 1970, are called for to ensure that in the longer term there is not a slowdown in economic growth accompanied by persistent increases in costs and prices against a precarious international background.

Efforts to expand production capacities, encourage increased labour mobility, recruit more foreign labour and switch resources to the most productive sectors are very useful in the present circumstances but can in the short term make only a comparatively limited contribution to the dampening of inflationary strains.

The emphasis must therefore be placed on those instruments which will serve to dampen the expansion of domestic demand.

(a) First of all, the finance policy of the public authorities will have to contribute energetically to limiting the expansion of demand in the months ahead. In this context the Commission draws attention to the fact that in its Memorandum of 9 July 1969 it had already stressed that "the budgets for 1970 should provide, if economic developments in the country concerned so require, not only for a distinct slowdown in the growth of expenditure but also for measures in the field of direct taxation, for the possible withdrawal of tax incentives to investment, and for a change in certain indirect taxes". Although in their budgets for 1970 most Member States have included measures to limit the growth of expenditure, these may not prove to be sufficient. The handling of expenditure should therefore be further tightened. Part of the funds shown in the budget could be temporarily frozen and held till the economic situation allowed of their use. As there is a danger that restrictive measures could fall mainly on capital expenditure, which is often more flexible than ordinary expenditure, care should be taken to ensure that the savings made do not compromise medium-term economic development too severely.

On the revenue side, no further tax reliefs can be advocated. Should the expenditure planned under the budget still provide unduly vigorous stimuli, an increase in rates of taxation, preferably direct taxation, should not be ruled out.

A rigorous budget policy should be pursued, not only by the central government but also by all other public authorities.

The budgets should at all events be implemented in such a way that in the first half of the year taxes are collected faster than before and the rate of spending slowed down.

It is also desirable that the cash transactions of the public authorities should where possible mop up a certain amount of domestic liquidity. Where there are still budget deficits, these should as far as possible be financed through long-term borrowing, even if the floating of public loans entails a certain upward thrust of interest rates on the capital market. There is at all events a case for measures to consolidate public indebtedness. Consideration should be given to absorption of liquidity through repayment of debts contracted with the central bank or foreign creditors, or through deposits with the central bank.

(b) In the course of 1969, money and credit policy was given a sharply restrictive bias in all Community countries. The effects of this policy, which generally take longer to make themselves felt than those of budget policy, should come out more strongly in 1970.

An easing of these restrictions cannot be contemplated at the moment. It should rather be one of the declared aims of money and credit policy to place strict limits during 1970 on the rise in the volume of money and quasi-money in circulation. In pursuing this aim, those responsible for credit policy should also take account of developments in government cash transactions and foreign exchange movements. Credit policy should be particularly stringent in countries where the external financial position is still precarious. In a number of cases this might imply a rise in interest rates, which in the present circumstances should not only be assessed in the light of the conditions obtaining on foreign money and capital markets, particularly the Eurocurrency market, but should also be considered a desirable complement to an overall stabilization policy.

The credit restrictions should be brought to bear more heavily on consumption expenditure and, in certain member countries, on construction, but publicly assisted residential construction must be maintained at a high level. Credit expansion in connection with investment or building plans, however, would also have to be carefully controlled, particularly in a business situation where inflationary strains are threatening to upset the distribution of the resources available for investment on the basis of genuine economic criteria.

(c) Encouragement of private saving must be an important instrument in the fight against inflation; it would help curb private consumption and the outflow of capital, and at the same time facilitate the non-inflationary financing of economic growth. The incentives offered should be fairly comprehensive, so as to rule out the possibility of a switch from one of the various forms of saving to another. The interest rates paid on savings deposits should be adjusted to the general rise in interest rates, for reasons of expediency as well as of fairness.

(d) To solve the problem which would be raised by the persistence of the strong rise in costs and prices at a time when economic activity is declining, it will also be necessary to use means other than those mentioned.

It is, for instance, desirable that the upward thrust of prices should be curbed by keener competition on the markets for goods and services. The rapid growth of visible trade between member countries and the reduction of the common external tariff in January 1970 make a major contribution in this context. Competition should in addition be intensified through other suitable means, particularly in the fields of resale price maintenance, the abuse of dominant positions on the market and the modernization of trading structures.

As the Commission emphasized in its Memorandum of 9 July 1969, the measures required to restore equilibrium will prove successful only if both sides of industry take an active part in the drawing up and implementation of an overall policy. It is therefore essential for governments to examine jointly with employers and workers the possibilities of increasing the various types of income and the impact this would have on the trend of prices. In this context it would also appear desirable to promote the various forms of formation of wealth by wage and salary earners.

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The Commission requests the Council to approve the guidelines set out above. This could enable the Community to get economic developments in 1970 more fully under control and facilitate pursuit of a medium-term policy which would ensure balanced economic growth from 1971 onwards, a policy which the Commission has already raised with the Council in another context.

Short-term Economic
Policy Committee

Brussels, 16 January 1970

Opinion of the Short-term Economic Policy Committee on the Economic Budgets for 1970

At its meeting of 17 December 1969, the Short-term Economic Policy Committee examined the economic situation in the Community at the end of 1969, the outlook for 1970 and related problems of short-term economic policy. The Committee based its survey on information contained in the economic budgets transmitted by Member Governments and in addition took account of the latest forecasts made by the Commission's services.

1. For the Community as a whole, 1969 was a year of high growth rates, but also one of monetary imbalances, which eventually led to parity changes, and of mounting inflationary pressure.

The real gross Community product rose by 7%, a rate never before achieved since the creation of the Common Market. However, for some time now production has been tending to expand more slowly; reserves of unutilized production capacities are quickly nearing exhaustion and the situation on the labour market is becoming very tight. Productivity gains, which were still very high at the beginning of the boom period, are now losing momentum. Prices kept increasing more and more steeply as the year went on, mainly under the pressure of growing demand accompanied by rising wage costs. In these circumstances the current external surplus of the Community contracted sharply.

2. In 1970, export demand is expected to slow down, though it is hard to tell at present to what extent and for how long it will do so. But internal demand should remain buoyant, especially during the first half of the year, and in most countries will probably be well in excess of the growth potential of domestic production. Productivity gains will slow down further and bottlenecks on the labour market will continue to increase in number. The gap between supply and potential demand is likely to cause a rapid rise of imports and prices, at least during the first half of 1970. Allowing for differences in degree from one country to another, the Community as a whole must, therefore, expect continuing inflationary pressure.

3. In the Committee's view the main policy priority should be a drive to overcome inflationary tendencies and prevent the economy from overheating. A concerted attack should be easier now that conflicts of aims both within countries and with respect to the re-establishment of internal balance in the Community as a whole are less severe.

In view of the danger that world economic conditions may begin to deteriorate sharply before the Community has got inflation under control, the measures adopted should be measures that take effect quickly and that can, where appropriate, be reversed easily. In this way it should be possible to avoid the combination of unduly sharp curtailment of growth with a continuing rise of costs.

4. The Committee believes that stringent budgetary policy, both on the expenditure and on the revenue side, will be required in order to hold back the expansion of overall demand in sufficient measure and to create favourable conditions for a return to internal balance. To the extent possible, budget deficits should be financed without recourse to the money market.

Given the need for measures that "bite" quickly and that can be reversed, countries still expecting high budget deficits would be well advised to introduce disinflationary tax increases. For the rest, budget management in the course of the year should be so arranged as to concentrate restrictive effects chiefly in the early months of the year. In addition, some of the original appropriations might temporarily be frozen.

All Member States took restrictive monetary measures in the course of 1969. The Committee feels that this policy line should be maintained for the time being, and in some cases even strengthened. However, allowance must be made in this connection for the restrictive influences deriving from any outflow of foreign exchange.

The fight against rising prices should be supported by incomes policy, promotion of saving and encouragement of competition, as well as by other measures.

5. As regards Italy, the Committee noted that current inflationary tendencies already constituted a serious threat and were still gaining in strength.

While current monetary and credit policy seemed to meet the requirements of the situation, the Committee felt that insufficient use was still being made of other stabilizing policy instruments. This applies especially to budget policy, for the 1970 budget, if implemented and financed according to present plans, is too expansionary. Failure to make adequate use of other economic policy instruments and almost exclusive reliance on monetary and credit policy might discourage investment and impair growth prospects.

In Belgium, any increase in current inflationary pressures appears all the more dangerous as it would worsen the economic climate for the introduction of the tax on value added (TVA) on 1 January 1971 and thus seriously compromise the prospects of a return to equilibrium. The Committee noted that the measures announced by the Belgian authorities late in November were a step in the right direction, but did not feel confident that the tightening of restrictions, especially in budget policy, went far enough to meet current requirements, or that the restrictive measures would take effect quickly enough.

In Luxembourg, the economy is moving towards considerable price rises by its own impetus and because of special factors such as the TVA and the revaluation of the mark. The Committee examined the stabilization programme now in hand and noted with interest the Government's efforts to slow down the rise in the cost of living.

In the Netherlands, production potential will still be under heavy pressure in 1970 and the demand-restricting policy introduced as early as the end of 1968 should be continued; particular care should be taken to make sure that the rise of budgetary expenditure does not exceed the limits laid down. It is all the more important to control the price rise as this is one of the conditions which must be fulfilled if both workers and employers are to co-operate in getting the economy back on a sound footing, a policy which has prospects of success only if it is backed by employers and employed alike.

In France the last few months brought signs of an improvement in the economic and financial situation. There was striking evidence of this in foreign trade, where the beneficial effects of devaluation on French exports were reinforced by continuing vigorous growth in major importing countries. There are signs that the expansion of domestic demand for consumer goods is losing momentum, but none as yet of any easing of pressure on factors of production; the price trend is still definitely rising. In these circumstances monetary, credit and budget restraint must be maintained if the improvement now under way is to be consolidated in the course of 1970.

In Germany the revaluation will no doubt ease economic strain, but this may well take time. Revaluation as a check on demand is being reinforced by developments in the monetary and credit fields. As a result of the heavy outflow of foreign exchange since revaluation, the market forces are already exerting heavy pressure on bank liquidity. Public finance should be deployed in early 1970, as in the past, to contain overall demand. Speedy action is all the more necessary since, if prices go on rising, the German economy might later enter a phase of stagnation harmful for the Community as a whole.

Trends in industrial labour costs

A. *Introduction: methods*

Every year since 1962 the Commission's Quarterly Surveys on the economic situation in the Community have included an Annex showing the trends of compensation of employees per head, productivity of labour, labour costs per unit of gross value added at constant prices, and the implicit price index for gross value added in industry (including construction), not only in the member countries but also in the United States and the United Kingdom.

The aggregates in this survey have been defined and calculated as follows:

Compensation of employees is defined as wages, salaries and social insurance contributions. For Belgium, however, separate figures corresponding to this definition are still not available for compensation of employees broken down by economic sectors; in this case, therefore, the index given by the Banque Nationale de Belgique for the wage bill has been used, corrected by the addition of the average figure for employers' social insurance contributions. It should be pointed out that this approximation probably understates the true trend of wages in Belgian industry. The figures for labour costs in Belgian industry therefore have to be treated with even more caution than those for the other countries.

In Italy and the United Kingdom, no market-price figures are published for gross value added at constant prices, broken down by economic sectors; for these countries, therefore, factor-cost data have been used. The prices taken as a basis for calculating gross value added at constant prices are those of 1963 in all cases except the United States, for which the prices used are still those of 1958.

It would have been better to use the trend of compensation of employees and gross value added at constant prices per hour worked, but this could not be done because the statistics on the number of hours worked in the Community countries are incomplete. Consequently, these two items could only be calculated per employee. This makes it more difficult to interpret the graphs, especially the results for the last few years, during which the number of hours actually worked has changed considerably in most of the countries.

Labour costs per unit of gross value added at constant prices were calculated by dividing the index of the wage bill by the index of gross value added at constant prices. These figures can also be obtained by dividing the wage bill per person employed by gross value added per person employed.

As last year, the survey again gives figures for the trend in labour costs adjusted for changes in official exchange rates. These figures are of special interest, given the intervening devaluation of sterling and the French franc, and the revaluation of the DM. Except for 1969, these calculations are based on the rate of exchange of the national currencies concerned in relation to the US dollar, as given by the SOEC in its publications on external trade. For 1969 the new parities were applied pro rata, for France as of 10 August and for Germany as of 1 October.

The implicit price index shows the extent to which the trend in value added at current prices differs from the trend at constant prices.

For Belgium, gross value added at current and at constant prices, as well as the implicit price index for the period 1958 to 1965 were calculated on the basis of figures given by the SOEC in its publication on National Accounts 1958-1967. For the period 1965 to 1968 the SOEC made available sets of figures corrected by the Belgian National Statistical Institute.

For all countries covered in this annex, the 1969 figures rest wholly or partly on estimates.

The following should be said about the significance of the series used here.

As far as possible the data have been taken from national accounts, in order to ensure a sufficient degree of international comparability. In this connection, however, it should be remembered that, while *trends* in the indices are internationally comparable, the absolute figures are not. This qualification is all the more important in that even the relationship between the various levels in the base year 1958 is not necessarily "correct".

Use of the national accounts meant that only annual figures could be used. Changes in the course of the year are only partly reflected in the annual figures concerned and also affect the results for the following year. This makes it more difficult to judge short-term trends, in particular.

The concept of value added differs from that of industrial production as generally applied in calculating the monthly indices of industrial production.

This difference between value added and industrial production (as used for production indices) appears most clearly in the implicit price index for gross value added. In this index, two essential factors affecting actual market prices are left out of account, namely, firm-to-firm supplies within industry and supplies from other sectors, including abroad. The trend of the implicit price index therefore differs from the trend of market prices, to an extent which varies from country to country, since the proportion of value added in industrial output also varies.

Compensation of employees in industry does not include all wages contained in the market prices, i.e. it excludes wages paid in respect of goods and services supplied to industry by other domestic sectors.

These remarks should show that the series which follow must be used cautiously. They are not internationally comparable as they stand, and their development in time is different from that of series whose data are based not on value added but on gross production.

B. *Developments in 1969*[1]

In 1969, the trend of labour costs per unit of gross value added (at constant prices) expressed in national currencies was unfavourable in the European Economic Community. The estimated average rise was much the same in all member countries. It ranged between 2.5 and 3%, after a general decline of labour costs in 1968 everywhere except in France.

Compensation of employees per head generally rose a good deal more steeply than in 1968. The increases were 10.5% in Germany (1968: 7.2%), 12.5% in France (1968: 12.5%), 7% in Italy (1968: 5.5%), 10% in the Netherlands (1968: 9%) and 9% in Belgium (1968: 5.8%). The high figure for France is largely explained by the heavy wage increases in the middle of 1968; in the course of 1969 wages rose much less.

The increase in production per employee was held back more severely last year by the high degree to which factors of production were already utilized. This is particularly evident in the annual figures for Germany and the Netherlands, where last year's increase of 7% compares with 9.1 and 9.7% respectively, in 1968. In France, gross value added per employee increased rather more (9.5%), thanks almost exclusively to the fact that the 1968 figure (5.7%) was so low as a result of the heavy production losses during the strikes in May and June 1968.

In Italy, production per employee rose much less in 1969 (4.5%) than in 1968 (6.8%). The reason is that much production was lost during the labour conflicts in the second half of 1969. In Belgium, the 1969 increase in gross value added per employee (6%) almost matched the 1968 figure (6.4%).

As regards the trend of labour costs per unit of gross value added in Germany, it must be emphasized that the overall 1969 increase of 3% in DM (5% after adjustment for parity changes) is in no way representative of the situation at the end of 1969, since these figures only partially reflect the considerable wage increases since the autumn of 1969 and the

[1] The calculation of the figures on which the graphs are based was completed on 10 March.

effects of the DM revaluation. In assessing the influence of the trend in labour costs on the international competitiveness of German industry, it should also be remembered that the 4% border tax on exports introduced in November and the equivalent tax relief on imports were abolished in October.

For a more accurate assessment of the trend of labour costs per unit of gross value added in France, it should be emphasized that the 4-5% payroll tax, of which no account was taken in the graphs, was abolished with effect from 1 December 1968. For the rest, as in Germany, the end-year situation is different from the picture conveyed by the annual figures, since the latter are only partially adjusted for devaluation.

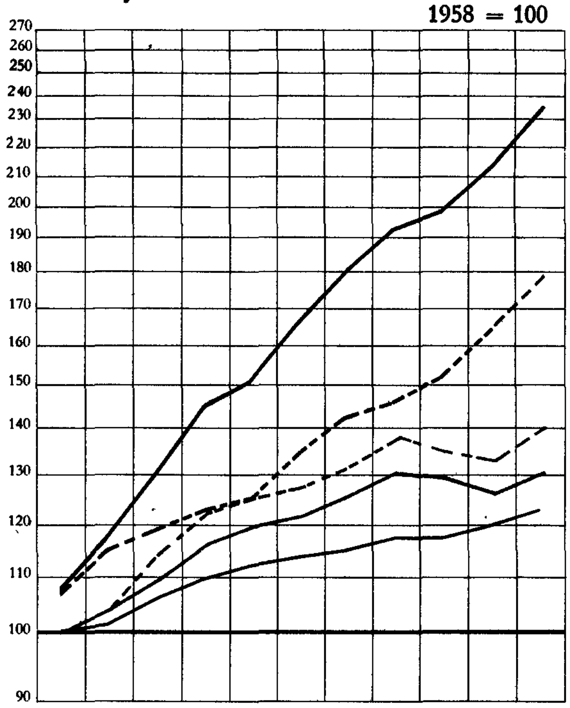
In the non-member countries covered here, as in the Member States, the trend of labour costs per unit of gross value added (at constant prices) was noticeably less favourable last year than in 1968.

In the United States compensation per employee rose by nearly as much (6.5%) in 1969 as in 1968 (6.8%). But under the impact of slower economic growth, production per employee increased much less (2.5%) in 1969 than in 1968 (4.5%). As a result, there was a distinct deterioration in the trend of labour costs per unit of gross value added, which rose by 4% in 1969 compared with 2.2% in 1968.

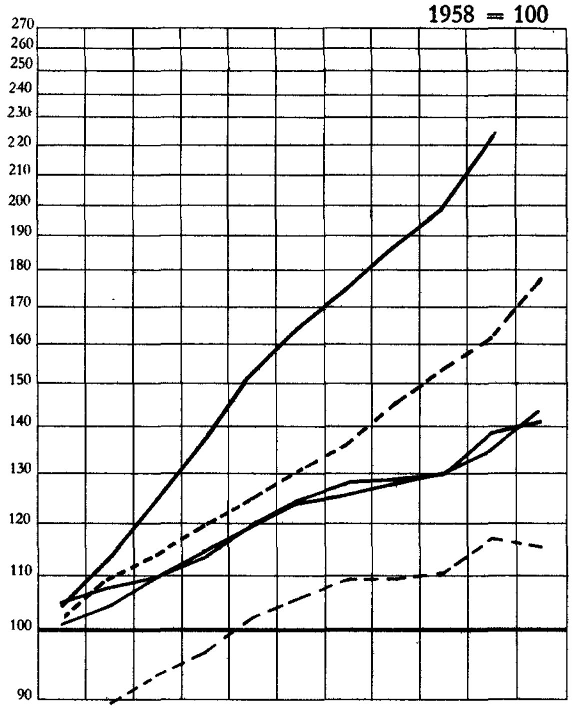
In the United Kingdom, compensation per employee rose a little less in 1969 (8%) than in 1968 (9.1%). But production growth slowed down appreciably and there was a drop in the number of persons employed. Production per employee rose by 4% in 1969, as against 7.4% in 1968. Labour costs per unit of gross value added (at constant prices) hence rose by 3.5% (1968: 1.4%).

LABOUR COSTS IN INDUSTRY

Germany

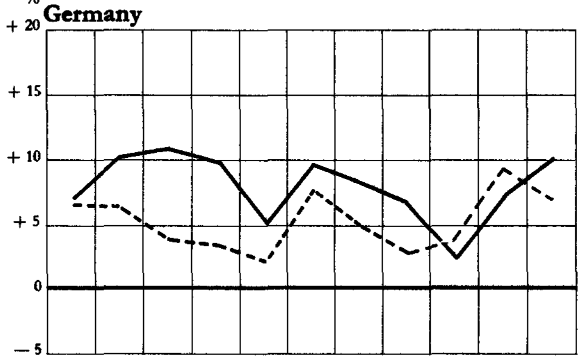


France



% change on preceding year

Germany



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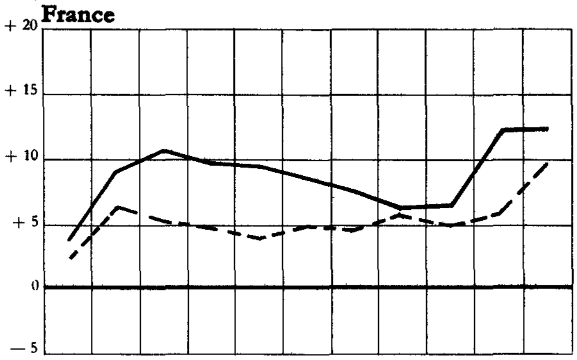

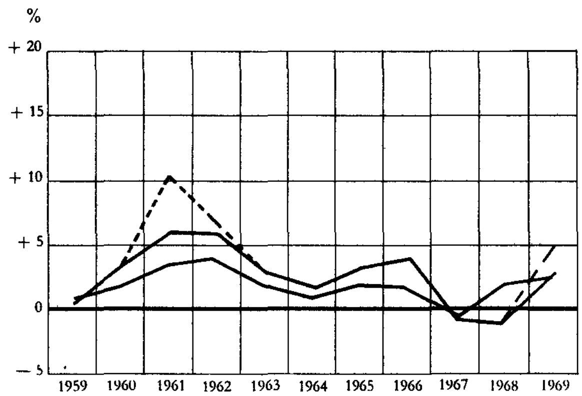

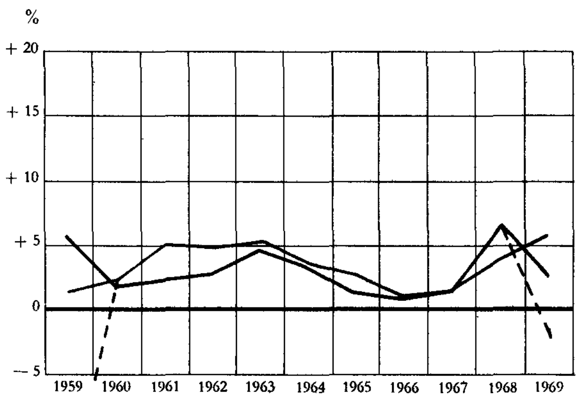

——— *Income from employment per head*
-------- *Gross value added (constant prices) per employee*
——— *Labour costs per unit of gross value added (at constant prices)*
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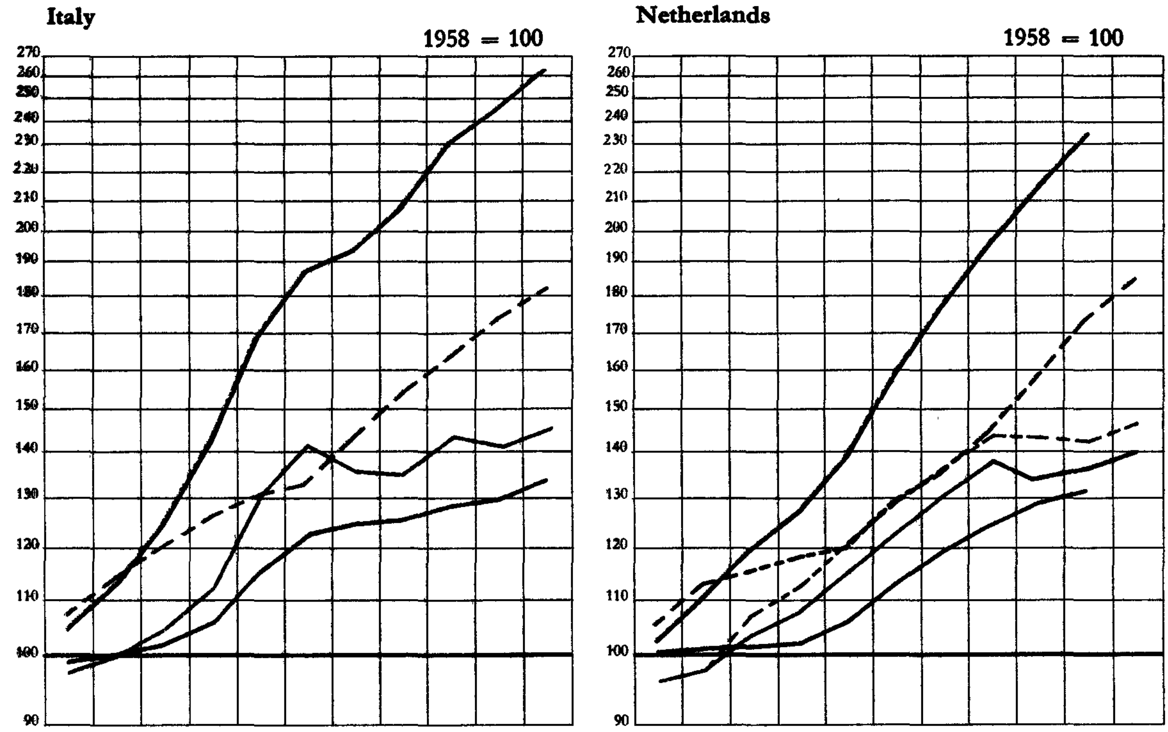
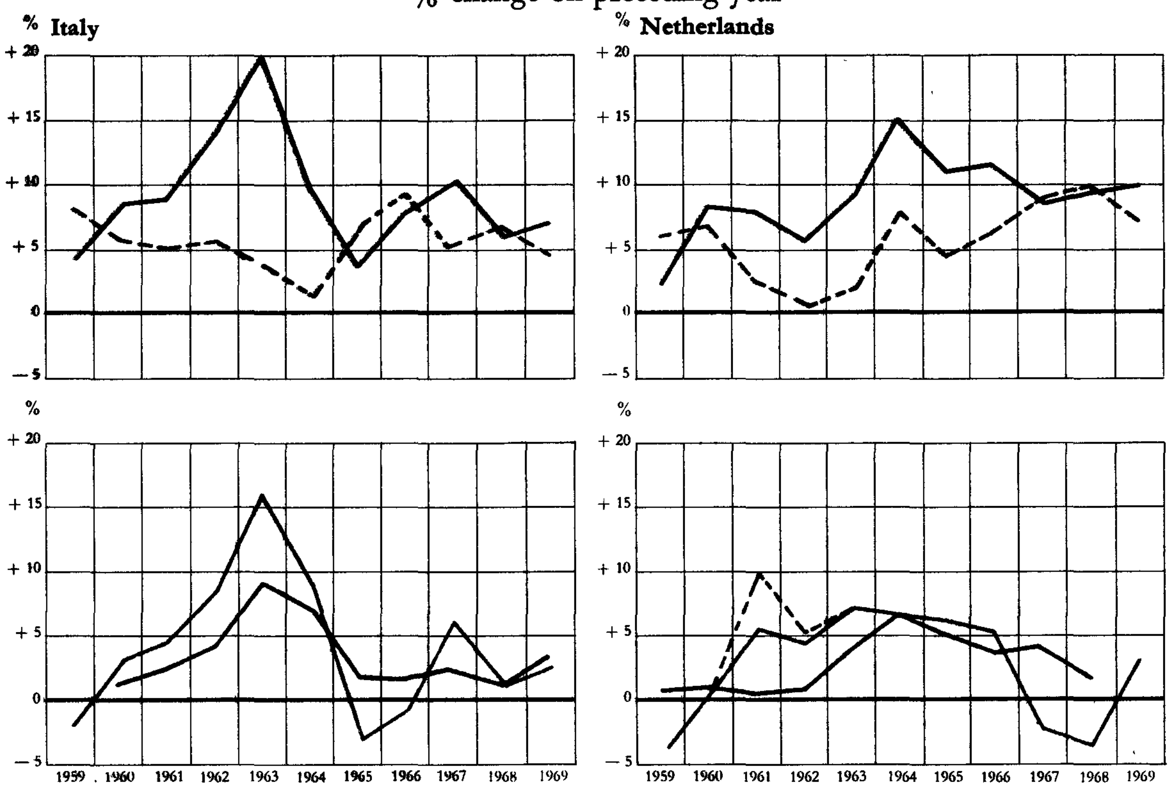
——— *Impliciti price index of gross value added*

LABOUR COSTS IN INDUSTRY



% change on preceding year



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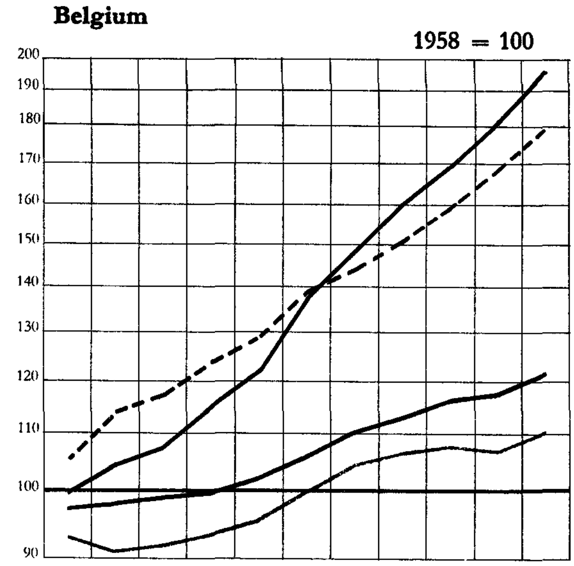
LABOUR COSTS IN INDUSTRY



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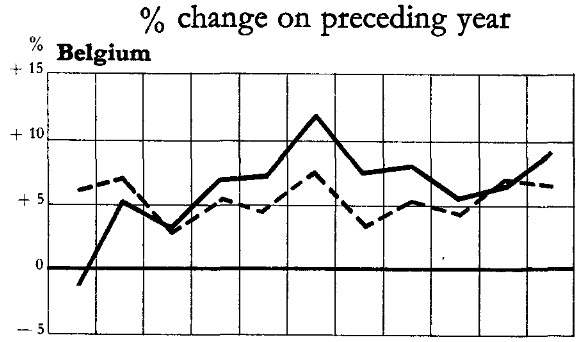

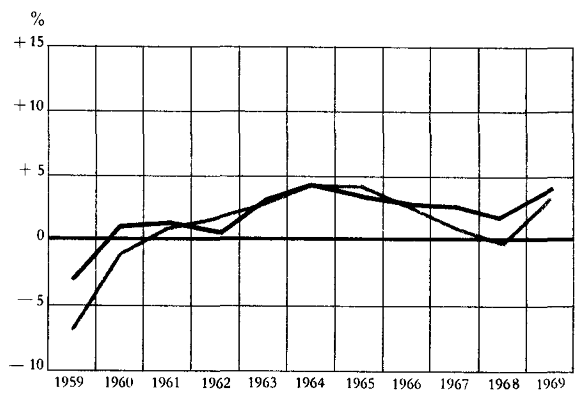

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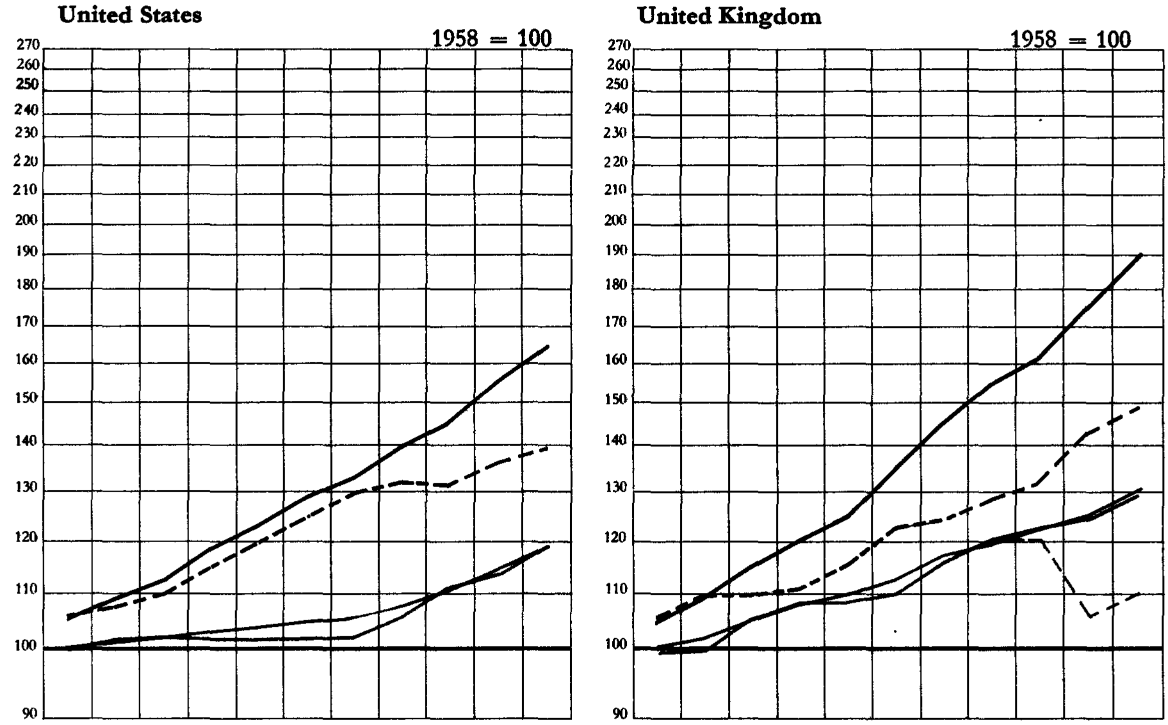

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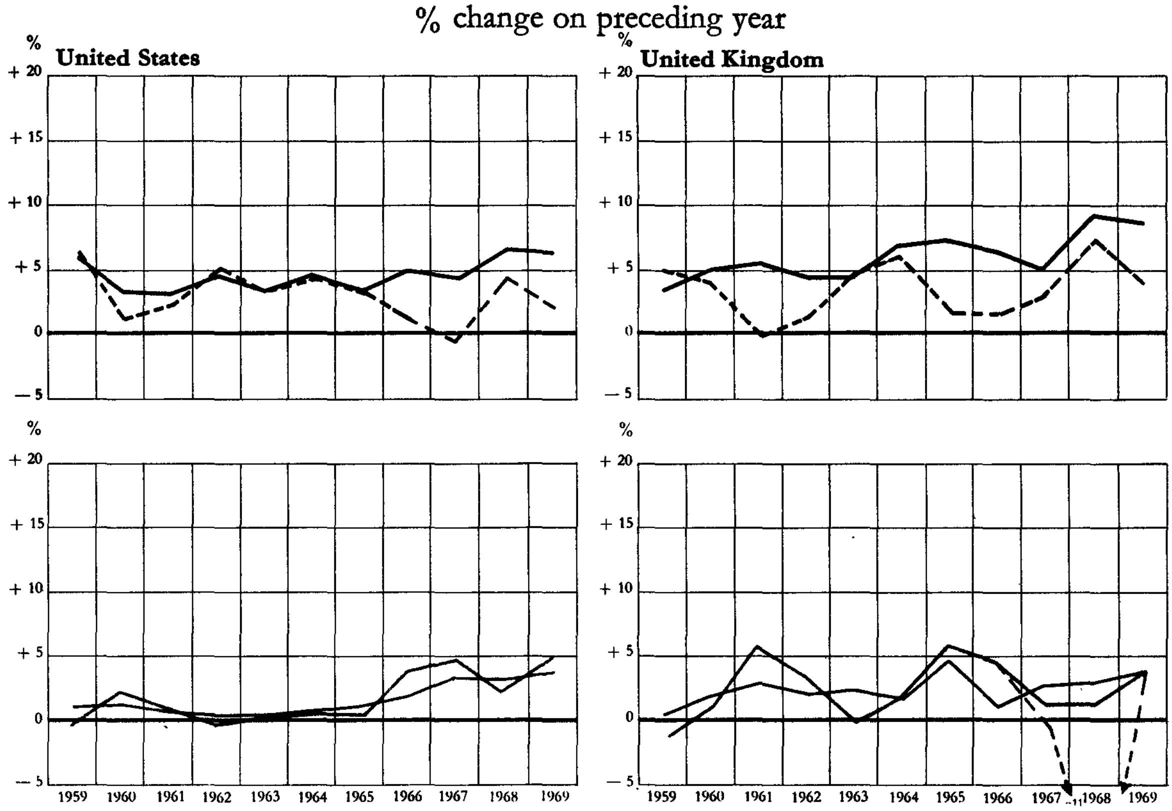

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