

**European
Economic
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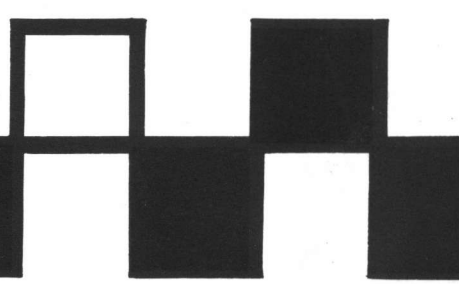


**Directorate-
General
for Economic
and Financial
Affairs**

**The economic situation
in the Community**

4

1966



Quarterly survey

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

COMMISSION

The Economic Situation in the Community

DECEMBER 1966

Contents

	<i>Page</i>
I. The overall situation	3
A. <i>Balance-sheet for 1966</i>	9
1. The world economic situation in 1966	9
2. Demand	11
3. Production	16
4. Balance of the markets	20
B. <i>Outlook for 1967</i>	28
C. <i>Economic policy</i>	35
Annex	
Council Recommendation of 22 December 1966 to the Member States on the guidelines for short-term economic policies in 1967	41
II. The situation in each of the Community countries	49
A. <i>Federal Republic of Germany</i>	51
1. Balance-sheet for 1966	51
2. Outlook for 1967	59
B. <i>France</i>	69
1. Balance-sheet for 1966	69
2. Outlook for 1967	76
C. <i>Italy</i>	85
1. Balance-sheet for 1966	85
2. Outlook for 1967	92
D. <i>The Netherlands</i>	101
1. Balance-sheet for 1966	102
2. Outlook for 1967	109
E. <i>B.L.E.U.</i>	119
Belgium	119
1. Balance-sheet for 1966	119
2. Outlook for 1967	126
Grand Duchy of Luxembourg	135
1. Balance-sheet for 1966	135
2. Outlook for 1967	140
Graphs and economic indicators	
1. Community trade	13
2. Economic indicators (graphs and tables)	
a) Community	45
b) Federal Republic of Germany	65
c) France	81
d) Italy	97
e) Netherlands	115
f) Belgium	131
g) Grand Duchy of Luxembourg	143
3. Businessmen's views on the industrial situation	8
a) Federal Republic of Germany	53
b) France	71
c) Italy	87
d) Netherlands	103
e) Belgium	121
f) Grand Duchy of Luxembourg	137

Note :

This Survey was completed around mid-December 1966. 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, No. 12-1966 of the "Graphs and Notes on the Economic Situation in the Community" can usefully complete the information supplied here.

I. THE OVERALL SITUATION

While the pattern of development differed from one member country to another, in the Community as a whole the expansion of economic activity has again been brisk in 1966. The real gross Community product is almost 4.5 % higher than in 1965, when in turn it was some 4 % up on the previous year.

Since 1958, then, the real gross Community product has grown by some 52 %, whereas in the United States the increase over the same period was about 44 %, and in the United Kingdom 30 %.

The year-to-year growth of total demand in money terms was much the same as in 1965, with a slight shift of emphasis among the main components: external demand rose less strongly, but internal demand somewhat more vigorously, than in 1965.

The expansion in the aggregate value of visible exports from the Community (as defined for the foreign trade statistics) declined from 12 % in 1965 to slightly less than 9 % in 1966. Exports to the United States again increased extraordinarily fast, but the growth of deliveries to EFTA and to the developing countries was appreciably weaker than from 1964 to 1965.

Gross fixed investment in the Community continued to rise at the same rates as before (value 6 %, volume 3.5 %). The increase in capital expenditure on building was somewhat lower than in the previous year to 1965, while investment by enterprises in plant and machinery rose somewhat more vigorously than in the previous year; its upward movement was stronger than before in France and Italy, while in Germany on the other hand there were even signs of a downward trend in the second half of the year. Stockbuilding provided much the same stimulus to growth as a year earlier.

Total consumer expenditure in the Community has probably increased at slightly higher pace than before. In most member countries the expansion of public current expenditure on goods and services remained very vigorous; nevertheless there may have been a slight slowdown for the Community as a whole on account of the somewhat quieter trend in Germany and in Italy. Private consumers' expenditure by contrast will probably have risen somewhat faster than before, i.e. by about 8 % in terms of value and approximately 4.5 % in terms of volume, following rises of 7.6 % and 4.2 % in 1965. In France and Italy the rise was more rapid, and especially in Germany it was slower, than in the previous year.

Including this estimated figure for 1966, private consumption in real terms has risen since 1958 by some 50 % (some 38 % per head of population).

The growth of private consumers' demand from 1965 to 1966 reflects first and foremost the change that has occurred in the disposable income of households. In Italy and France this went up perceptibly faster than in the previous year, mainly because the total number of hours worked responded to the improvement in business activity; in the other Community countries there was a more or less marked—but on the whole fairly moderate—slowdown in expansion.

Supply within the Community was as a rule sufficiently flexible to follow the rise in overall demand. Industrial production expanded faster than from 1964 to 1965; its year-to-year growth (as defined for the index of the Statistical Office of the European Communities) will probably have been 5 %, compared with 4.5 % in 1965—and this will have brought the total rise in output since 1958 to no less than 67 %.

However, the growth rates of industrial production in 1966 showed greater deviations from the Community average than in 1965, because of the divergent economic trends in the individual countries.

In the services sector, value added continued to expand at about the same rate as before. The rise in agricultural production, however, has flattened out distinctly, particularly as a result of a relatively modest grain crop.

On the Community's labour markets, the situation tended in the main to ease slightly; in the second half of the year the tendency gathered strength in Germany and in the Netherlands, but this does not mean that in the two countries concerned shortages of labour are yet a thing of the past. As the year advanced there were signs of a slight tendency towards a reduction of unemployment in Italy—the only country with a considerable number out of work; on the average for the year, however, the level of unemployment in that country was still a little higher than in 1966.

Imports from non-member countries rose more in 1966 than in 1965. The expansion of visible imports probably reached some 6 % by volume and 7.8 % in value, compared with 5 % and 6.5 % in 1965. These figures for the whole year, however, do not reveal the fluctuations that occurred in the month-to-month figures, i.e. a vigorous rise in the second half of 1965 and the first months of 1966, which then levelled off largely because the slowdown in demand from Germany outweighed the faster increase of France's and Italy's imports.

Visible trade between the Community countries continued to expand very vigorously, but since the spring it too has been losing momentum. This was reflected in the growth figure for the year; from 1964 to 1965 the increase in value (on the basis of imports) had been 13.5 %; it probably amounted to some 12 % from 1965 to 1966. While France and Italy expanded their imports from other Community countries at a faster pace, there was a more significant slowdown in corresponding imports by other member countries, in particular Germany.

The upward pressure on prices persisted. It gained in strength during the first half of the year, when there was marked excess demand in some member countries—the gain being partly, it is true, due to special influences of a temporary nature (the price of vegetables), to measures of tax and wage policy and to rent increases; it was particularly strong in the Netherlands, but in Germany and Belgium too it was very appreciable. With the disappearance of the special influences there was some flattening out; the upward trend in the seasonally adjusted figures continued, though less vigorously than before. In France, the rise in prices was relatively modest throughout the year, though in the end it totalled 3 %; in Italy there was even very extensive stabilization, at least up to the flood catastrophe in November.

The trend in exports and imports outlined above suggests that in 1966 the Community's visible trade balance should have closed with a slightly smaller deficit than in 1965 (on the basis of the foreign trade statistics, an estimated 1 400 million u.a. ⁽¹⁾ instead of 1 500 million u.a.). The seasonally adjusted figures tended to deteriorate until spring 1966, but later there was a distinct recovery, largely because of the improvement on the visible trade account of the Federal Republic of Germany.

Largely as a result of this, the surplus on current account appears to have risen once again in 1966, while the available—but so far particularly incomplete—information on the capital transactions account hardly suggests that any great surplus will be achieved. During the first eleven months of 1966 the gross gold and foreign exchange reserves of the monetary authorities in the Community countries rose by 310 million u.a. At the same time the net foreign exchange position of the

⁽¹⁾ 1 u.a. = 1 unit of account = 0.888671 gm of fine gold = US \$1 at the official rate of exchange.

commercial banks continued to improve, but probably less strongly than in the previous year.

The economic expansion of the Community is likely to slow down somewhat in 1967, with both external and internal demand losing momentum.

In external demand, the very strong stimuli so far provided by sales to the United States may weaken somewhat; this, coupled with a more or less pronounced stagnation of imports by the United Kingdom, would reduce the pace at which Community exports have been rising.

The expansion of internal demand may be affected by a slight decline in the growth of investment by enterprises. In Germany these outlays on investment can even be expected to continue falling in absolute terms—at least for part of the year—and there may also be a decline in the Netherlands. Despite a continued vigorous upswing in France and in Italy, and perhaps also a somewhat faster pace of growth in Belgium, the expansion of investment by enterprises is then likely to be weaker for the Community as a whole than it was from 1965 to 1966.

It can also be assumed that total expenditure on consumption will grow at a somewhat reduced rate, which will probably be due entirely to a more or less distinct slowing of the tempo at which private consumers' expenditure is expanding in Germany and in the Benelux countries.

As far as the prospective development of supply is concerned, there may be a stronger expansion of agricultural production in 1967 than in 1966, provided the weather is normal. Industrial production as a whole can be expected to rise at an only slightly reduced pace, with very modest growth particularly in Germany, a slowdown in expansion in the Netherlands and high growth rates in France and Italy.

Allowing for all factors that can so far be assessed clearly, the gross Community product is at present expected to rise by about 4 % in 1967.

Imports from non-member countries will for a while yet continue to be affected by the slowdown in economic activity in some member countries, particularly in Germany. On the other hand, certain special factors which tend to have an inhibitory effect (for instance, government imports into Germany and agricultural imports) will disappear, and as the year advances stockbuilding may once again exert a greater pull on imports. Overall, the Community's trade balance may be expected to show a further limited improvement in 1967.

Although the trend of supply and demand in the Community as a whole will in fact help to reduce the upward thrust of prices, allowance must still be made for the effects of the upward thrust that has already been affecting costs—and which is likely to persist, at least in attenuated form. In 1967 there will probably be once again a fairly distinct rise in the consumer price level.

The outlook for 1967 reveals in some member countries the effects of inflationary trends which have been tolerated during the past few years or which have been combated by too one-sided a set of economic policy instruments. There have consequently been price and cost increases on the one hand, coupled on the other with signs of a more or less distinct decline in investment and a considerable slowdown in economic growth. In these countries budget policy in particular should be tightened up with a view to steadying prices and costs and facilitating the financing of investment; concurrently the policy of containing credit could and should be relaxed or applied in a still more supple manner than hitherto. Any premature return to a short-term policy of general expansion would soon conjure up the spectre of fresh inflationary trends. Care will have to be taken in Italy and France to ensure that the current upswing of business activity in these two countries does not again end in imbalance.

A. Balance-sheet for 1966

1. The world economic situation in 1966

In 1966, the impetus given to the Community's economy by business trends in the outside world was rather less strong than in 1965. The average advance in the gross national product of the industrial non-member countries may, indeed, have been almost as rapid as in 1965, notwithstanding considerably greater differences between one country and another; but this time a larger number of the Community's main trading partners are to be found among the group of economies where demand was rising at a relatively modest pace.

In the United States, however, overall domestic demand continued to expand very briskly. Thus public expenditure proved to be particularly dynamic, owing not least to the more rapid rise in defence expenditure. Although credit markets stiffened increasingly until well into the autumn and the capital goods industries experienced growing difficulty over deliveries, enterprises continued to increase their expenditure on fixed assets substantially, partly as a result of the indirect influence of the appreciably higher demand for armaments; according to the latest surveys, their spending on fixed assets may prove to have been 17 % higher in value than in the previous year, compared with an increase of 15.7 % in 1965. Private consumers' expenditure also continued to rise; in the course of the year, however, it showed some signs of weakening—particularly spending on consumer durables—this was no doubt largely the result of the tax measures taken at the beginning of the year and of increases in social security contributions. Expenditure on residential construction showed a marked tendency to fall, the main reason for which was, it would seem, that funds for investment were in short supply and therefore cost more than before. Lastly, stockbuilding slackened quite perceptibly in the second half of the year—obviously owing to the disposal of stocks of finished consumer goods that had been accumulated involuntarily, and also to the tendency for raw material prices to move if anything downwards.

The gross national product of the United States may have risen by just on 6 % in real terms in 1966 compared with 1965—about as rapidly as in the previous year; in money terms, however, the increase was 9 % in 1966, as against 7.8 % in 1965, because of the upward trend in prices. Owing to considerable advances in productivity, industrial output, which will have risen at least 9 %, achieved a higher rate of growth than in the previous year, in spite of capacities being over-stretched and the shortage of skilled manpower becoming more acute.

Compared with the previous year, at least, the "inflationary gap" between overall demand and domestic supply widened, with the result that prices rose faster than before (at the retail stage they were about 3 % higher than in 1965) and imports again rose appreciably. This was the main reason for a further decline in the export surplus. Nevertheless, there appears to have been no significant increase in the overall balance-of-payments deficit as compared with 1965. Net exports of private capital did in fact decrease because of the growing scarcity of liquid funds on the American money and capital markets and the consequent considerable rise in interest rates, and because of the

programmes for voluntary limitation of capital outflows from the banks and of exports by enterprises of capital for investment abroad; in addition, there were some exceptional inflows of official funds—items such as advance repayments of loans by France and Italy.

In the United Kingdom, economic activity was influenced by the previous demand and cost inflation and by the consequent deterioration in the balance of payments; the restrictive policy intensified by the Budget for 1966/67, and even more by the measures adopted in July 1966, also had an effect. The result has been that among the components of demand, expenditure on fixed assets has been showing an underlying tendency to decline since the spring. Furthermore, the previously very brisk expansion of private consumers' expenditure slackened more and more rapidly as the decline in employment and the wage-freeze, also announced in July, came to be reflected in a considerably slower growth of incomes. The ensuing check to the growth of domestic demand—for only public expenditure showed a marked tendency to rise notwithstanding a fresh decision to limit public expenditure—was accompanied, in the second half of the year, by a perceptible slackening in the upward movement of prices; it should however be noted that this slackening was to some extent the result of direct action on the part of the authorities or of the possibility that such action might be taken should prices be raised.

With industrial output continuing to stagnate, the United Kingdom's real gross national product appears to be only about 1 % higher than in 1965. In the course of the year, the trend in the balance of payments changed for the better. Much of this improvement was due to the fact that the growth of imports levelled off, not only because purchases were held back pending the removal of the import surcharge at the end of November but also because the excessively high level of domestic demand was reduced.

In most of the other industrial countries outside the Community, economic growth continued at a slower pace, the degree of slackening varying from country to country. Thus the generally restrictive short-term economic policies pursued by the continental EFTA countries had fairly considerable repercussions, although the expansionary way in which the public authorities handled expenditure in some of them made it more difficult to combat inflationary tendencies, since the strains resulting from the imbalance between supply and demand still did not ease sufficiently. The business trend in the United Kingdom may also have acted as a brake on the economies of the other EFTA countries. It may have had the same effect, although to a lesser extent, on Canada—where the authorities, in view of the clear signs that supply was becoming less elastic, decided to reinforce the measures to restrict demand. In Japan, on the other hand, the upswing in economic activity continued throughout 1966.

World market prices of raw materials and semi-finished goods have fallen slightly since the spring, but mainly as a result of the elimination of certain extraneous factors which had been disturbing markets; in spite of this, the economic expansion of the industrialized countries—which, if the Community countries are included, has on the whole been hardly any less than before—appears to have been such as to assure the developing countries of a considerable increase in their export earnings. At all events, as far as it is possible to judge from the statistics available, the developing countries' foreign exchange reserves continued to rise in 1966, and this has clearly resulted in a perceptible increase, since the spring, in their propensity to import.

2. Demand

With world economic activity showing a generally rather less expansionary trend, the growth of exports from the Community to non-member countries was slower than in 1965. To judge by customs returns, the rise in visible exports may have been just on 9 % in value and about 8 % by volume, against corresponding increases of 12 % and 11 % a year before.

This means that the Community's visible exports again rose faster—although not very much faster—than world trade in general (excluding intra-Community trade), which should prove to have been about 7 % up on 1965, when it had advanced 8 % on 1964. The reason for this is probably to be found in the structure of supply in the member countries. At international level, it was in investment—particularly in the demand for capital goods on the part of the United States and, as the year went on, also on the part of the developing countries—that there was relatively most expansion, and this favoured a category of goods, that accounts for a large part of the Community's exports.

Visible exports from Community to non-member countries
(% change in values on preceding year)

	1965		1966			
	million u.a. (1)	%	1st quarter	2nd quarter	3rd quarter	Full year (5)
To all non-member countries :	27 079	+ 12	+ 7.5	+ 10.5	+ 8.5	+ 9
of which :						
To industrial countries (2)	17 612	+ 12.5	+ 9	+ 10.5	+ 7.5	+ 9
including :						
United States	3 425	+ 20	+ 22	+ 18.5	+ 20	+ 20
EFTA : total	9 604	+ 8.5	+ 5.5	+ 6.5	+ 3	+ 4
: United Kingdom	2 367	+ 3.5	+ 18	+ 12.5	+ 6	+ 9
To developing countries (3)	7 501	+ 9	+ 0.5	+ 8.5	+ 8	+ 5
including :						
Associated overseas countries and territories	1 733	+ 5	— 3	— 3	— 1	— 2
To other areas (4)	1 966	+ 19	+ 20	+ 20.5	+ 21.5	+ 21

Source : Statistical Office of the European Communities.

(1) 1 u.a. = 1 unit of account = 0.888671 gm. of fine gold = US \$1 at the official rate of exchange.

(2) Class 1 of the Standard Country Classification for Foreign Trade Statistics of the EEC.

(3) 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.

(5) Commission estimates.

The Community's sales to the United States again exhibited an exceptionally rapid rate of growth—hardly any less rapid than in the previous year. Deliveries to the EFTA countries, on the other hand, showed no more than a moderate increase; exports to the United Kingdom were again appreciably higher than in 1965, however, although there was a tendency for them to level off towards the end of 1966. Lastly, the revival in exports to the developing countries, which began in the spring, was not sufficient to ensure the same rate of growth for the year as a whole as for 1965. One of the reasons for this was certainly the weakness in purchases from the Community by the associated overseas countries and territories in the first half of 1966.

In contrast to demand from abroad, demand within the Community should have risen rather more strongly in the full year 1966 than in 1965, although there were signs that as the year wore on, and especially in the last six months the month-to-month figures were rising less rapidly.

Thus gross fixed asset formation may well have gone up by 6 % in value and 3.5 % by volume in 1966, compared with increases of 5.8 % and 3.3 % respectively for 1965. Its expansion slackened perceptibly in the Federal Republic of Germany but this was more than offset by a faster rate of increase in the Netherlands, Belgium and above all Italy, where after a decline that lasted into 1965 capital expenditure has revived considerably.

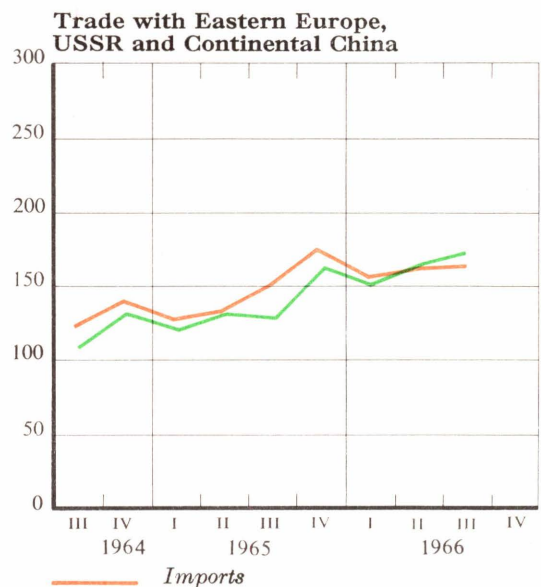
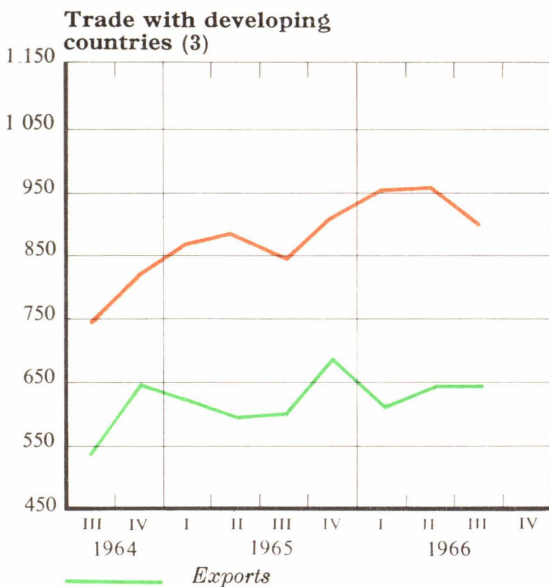
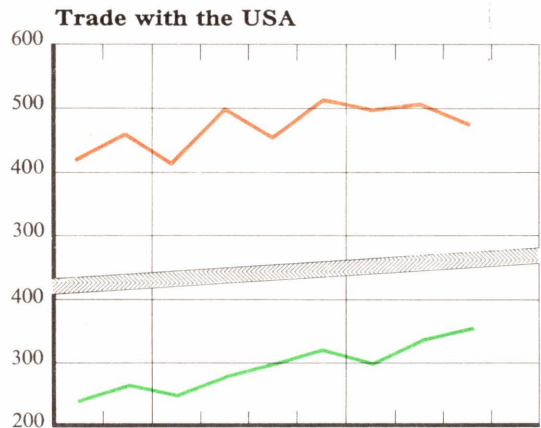
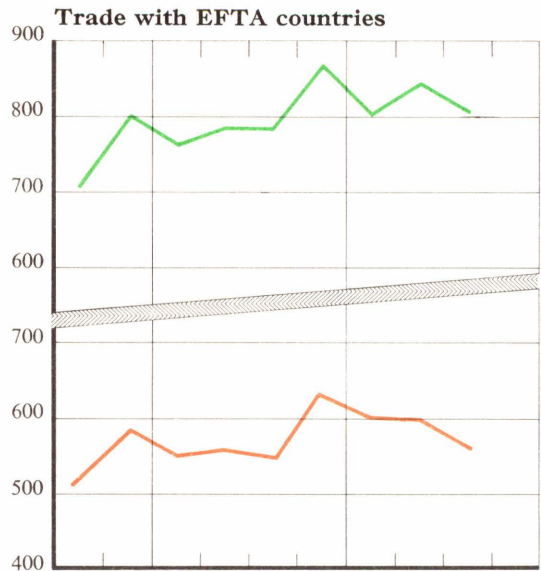
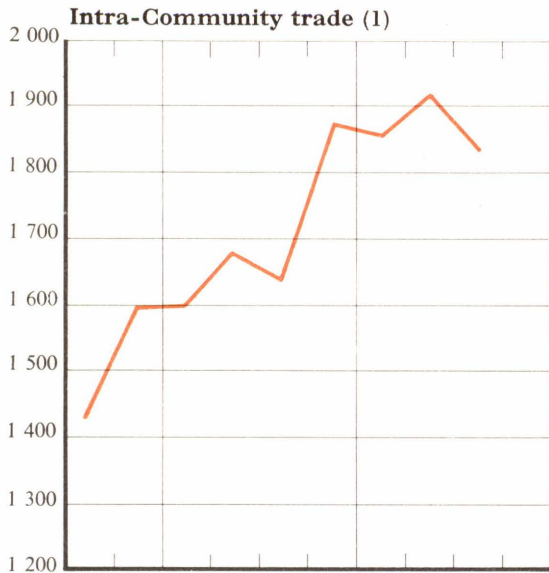
Expenditure on building and construction went up by about the same amount as in 1965. After having been on the whole extraordinarily rapid at the beginning of the year, the increase under this head tended to slacken in the Federal Republic of Germany and in France, and later on in the Netherlands as well. In France, the tendency was confined to residential construction and was occasioned by changes in the arrangements for financing and by a drop in effective demand, as indicated by the large number of dwellings left unsold; but in the Federal Republic of Germany, and to a lesser extent in the Netherlands, this slackening was mainly due to the tightness of the capital market, high interest rates, and certain attempts to save made by the public authorities. In Italy, investment in the form of construction went up slightly in 1966, after having declined persistently until 1965; the recovery appears to have been mainly due to the vigorous expansion in industrial building. Housing in that country was, on the other hand, not even able to maintain the already low level of 1965, although a tendency to recover became apparent in the spring and has been maintained since. In Belgium, too, there was a rather more distinct rise in expenditure on construction than in 1965; but its growth was inhibited by various factors, chief amongst them being a rather hesitant trend in expenditure on housing.

In contrast to this, investment by enterprises in plant and machinery rose rather more briskly in the Community as a whole than in 1965. It went up faster than before in France, and made a distinct recovery in Italy. In Belgium, too, this class of investment again showed a certain dynamism, which was, however, almost exclusively due to the execution of extensive investment programmes by foreign firms. Lastly, in the Netherlands, enterprises may have increased their investment in plant and machinery more

COMMUNITY TRADE

Monthly averages

In million u. a. *



(1) According to import returns.

(2) A.O.S. : Associated Overseas States (overseas departments, countries and territories).

(3) According to GATT classification : non-industrialized regions other than A.O.S.

* 1 unit of account = 0.888671 gramme of fine gold.

rapidly than in the previous year, but partly because of exceptional factors, such as purchases of aircraft and ships; moreover, a tendency for such investment to slacken became apparent as the year went on. In the Federal Republic of Germany, there was even a marked decline in the second half of the year as compared with the first; but here, too, expenditure on plant and machinery showed an increase for the year as a whole, compared with the already very high level of 1965.

Investment by the public authorities, which in the Community as a whole had been increasing at a substantial pace, seems to have been affected by restrictive measures and difficulties connected with financing. Its strong upward movement continued in France, and in Belgium its growth may have been even more vigorous in 1966 than in the previous year. In Italy the rise in the value of public works was at any rate greater than in 1965. In the Federal Republic of Germany, however, this type of expenditure slowed down perceptibly.

On the whole, stockbuilding probably contributed to the rise in overall demand to about the same, fairly modest, extent as in 1965. In the Federal Republic of Germany, the difficulty of finding finance certainly necessitated greater efforts to rationalize the stocking of raw materials; in addition managements here—and also in the Benelux countries—found it necessary to adapt stocks to the slower rate of production. But this development is likely to have been more or less cancelled out by the effects which the more rapid advance in industrial activity in France and Italy had on the formation of stocks. Moreover, stocks of finished goods appear to have risen no less rapidly than in the previous year. In the countries where the growth of final demand has slackened, dealers will certainly not always have trimmed their stocks accordingly, whereas in countries where a vigorous upsurge of business activity is taking place, that is, in France and Italy, the upward trend in stocks has been one of the factors leading to faster expansion.

The growth of consumer expenditure may have been almost as great in 1966 as in 1965. Public current expenditure on goods and services may well have risen a little less strongly in the Federal Republic of Germany and in Italy; but the increase nevertheless remained very substantial in most Community countries—mainly because of higher wages and salaries in the public sector.

Private consumers' expenditure in the Community also advanced at about the same pace as in 1965—about 8 %. As the increase in the index of consumer prices (as defined for the national accounts) was of about the same order as in the previous year, the growth rate by volume also remained about the same—almost 4.5 %.

In 1966, the Community's population went up by about 1 %, and real consumption per head by nearly 3.5 %. In marked contrast to the previous year, the increase was greatest in Italy and France—4.5 % and 4 % respectively, as against about 2.5—3 % in the other Community countries.

In France and Italy the month-to-month figures for private consumption tended to rise more rapidly, but in the Federal Republic of Germany their advance became distinctly slower in the second half of the year. In the Netherlands and Belgium, the short-term trend was distorted by fortuitous factors: at the beginning of 1966 the level of

consumption in those two countries was relatively low, after a rush to buy consumer goods towards the end of the previous year, due to the announcement that taxes would be raised in January 1966. In the second quarter, there was a temporary recovery, but this was followed later by a fresh slackening in the pace of increase.

The trend in private consumers' expenditure mainly reflected the changes in disposable household incomes, but changes in the savings ratio also played a part. Comparing one year with another, the savings ratio appears to have dropped in Italy and even more in the Federal Republic of Germany; in Belgium, on the other hand, it went up again, after having been affected in 1965 by the wave of purchases made in anticipation of higher taxes.

The increase in the gross wages bill slowed down in the Federal Republic of Germany and—less noticeably—in Belgium; this was due almost entirely to developments which took place in the second half of the year. In the Netherlands, too, wage-earners' incomes did not go up as much as in 1965, although the 12 % increase in that country was again substantially higher than in most of the other member countries. In France and Italy, on the other hand, disposable incomes rose appreciably faster than in 1965, owing to the improvement in the business situation.

The pattern of expenditure on consumption showed no substantial changes in the Community as a whole, despite signs that a slightly higher proportion of the total was spent on services and consumer durables. The number of new registrations of passenger cars rose by about 8 %, as against 9.4 % in 1965. Sales of these vehicles went up more rapidly than before in France and Italy; in the Federal Republic of Germany and in Belgium, they were only slightly higher than in 1965, and in the Netherlands they were considerably lower.

3. Production

Internal supply probably grew somewhat faster in 1966 than in 1965. In the Community as a whole it was primarily determined by the development of overall demand; in almost all member countries the elasticity of production was fairly high.

The pace at which industrial output advanced was even appreciably faster than in 1965. As defined for the index produced by the Statistical Office of the European Communities (this excludes construction and the food, beverages and tobacco industries), it will have been some 5.5 % up, compared with only 4.4 % between 1964 and 1965. As the year advanced, however, the upward trend flattened out appreciably, particularly from May onwards. Compared in each case with the preceding quarter, the rise in the index—adjusted for seasonal and fortuitous variations—was about 2 % in the first quarter, 1 % in the second and a good 0.5 % in the third; at the end of the year there may again have been some acceleration. The tendency for expansion to slow down was distinct in Germany and in B.L.E.U., less pronounced in the Netherlands, hardly noticeable in France and non-existent in Italy, where growth even gathered momentum. The figures for the full year were influenced in varying degree by these trends.

Industrial production in the Community ⁽¹⁾
(% change on preceding year)

	1964	1965	1966 ⁽²⁾
Federal Republic of Germany	+ 9.0	+ 6.1	+ 2.5
France	+ 7.1	+ 1.5	+ 7.5
Italy	+ 1.4	+ 4.4	+ 12.0
Netherlands	+ 9.7	+ 7.0	+ 7.0
Belgium	+ 7.2	+ 1.8	+ 2.0
Grand Duchy of Luxembourg	+ 10.3	+ 0.8	— 3.5
Community total	+ 7.1	+ 4.4	+ 5.5

(1) Industrial production as defined by the Statistical Office of the European Communities, i.e. excluding construction and the food, beverages and tobacco industries.

(2) Commission estimates.

As was to be expected, these differences in the figures for the year are to a considerable extent due to developments in the capital goods sector. In Germany, activity in this field was particularly slack because of the easing in domestic demand; output in the mechanical engineering industry was lower in absolute terms than in 1965, and the metal-working industry as a whole registered little growth. Nor was the trend in B.L.E.U. much more favourable. In France and Italy, however, these industries benefited considerably from the renewed expansion of investment outlays by enterprises, although in Italy the results were at times affected by strikes. The output of commercial vehicles in the Community probably went up some 5 % as a result of considerable advances in Italy, France and the Netherlands, which more than offset the decline in Germany.

Developments followed an essentially more consistent—but by and large also uninspiring—trend in mining and the basic materials industries of the member countries. This applies in particular to coal mining where output in the Community as a whole dropped 6 %, despite an increase in pithead stocks of more than 15 %. Production of iron and steel was relatively slack except in Italy, where it rose considerably as the Taranto steelworks approached full capacity. The total figure for the Community remained at much the same level as in the previous year. However, with economic activity gathering momentum in France and in Italy, the chemical industry as a whole increased its production somewhat faster than in 1965, continuing its structural expansion within the Community.

The most vigorous contribution to the growth of industrial production in 1966 came from the consumer goods sector, where activity speeded up appreciably. The output

of passenger cars in the Community, for instance, was 10 % higher than in 1965, when it had increased only 6 % on 1964. The rise was attributable mainly to increased domestic demand in France and Italy. Even in the textile industry production expanded by almost 10 % in the Community as a whole, compared with a decline of some 4 % in 1965. The output of the other consumer goods industries, such as leather and paper, also went up considerably.

The output of the building and construction sector probably rose only at the same rather modest rate as in 1965. After the winter lull, activity picked up again unusually soon, so that the first half of the year showed a very high output; but as the year advanced there was a tendency for production to slow down as a result of the trend followed by expenditure on investment in building.

The contribution to gross domestic product made by the services sectors of the various countries will have risen by much the same amount as between 1964 and 1965. The figure for retail trading was boosted by the considerable increase in private consumption; expansion is likely to have been even more vigorous in the branches connected with the tourist trade; and the expansion of output among the manufacturing industries contributed in no small measure to the buoyancy of branches connected with transport; its influence on the overall situation in this sector was, however, notably dampened by the weakness of production in some basic materials industries.

Agricultural production appears to be the only sector whose contribution to the growth of overall supply from within the Community was considerably smaller in 1966 than in 1965, as certain major crops did rather badly in comparison with the unusually high harvests of the previous year. The total production of cereals, for instance, dropped by 4 % in the Community, the sharpest fall (13 %) being in wheat. The production of sugar beet and wine declined, largely because of relatively modest crops in France. Potato production, however, was probably above the 1965 level in most Community countries except France. There was a distinct further advance in livestock production, aided by the rapid rise in beef output which resulted from the larger numbers of cattle reared in the Community in recent years.

All in all the real gross Community product should prove to have been almost 4.5 % higher than in 1966, following increases of a good 4 % in 1965 and of some 5.5 % in 1964. Italy and France recorded the sharpest increase (both 5.5 %); this was appreciably in excess of the rather modest expansion registered in 1965. There was however a distinct slowdown in Germany, where growth was only 3 % (as against 4.6 % in 1965), while in the Netherlands (4.5 % instead of 5.4 %) and in Belgium (3 % following 3.3 %) the loss of momentum was less marked. The economic growth of Luxembourg, as reflected in the gross national product, continued to be weak (between 1.5 % and 2 %).

After declining slightly in 1965, the total number of persons gainfully employed in the Community may have decreased somewhat further in 1966. On the one hand, the total labour force appears to have been much the same as in 1965; in some member countries at any rate its growth was smaller than in the previous year, while in Italy

there was again some contraction; the monthly averages of unemployed persons, on the other hand, were slightly higher than in 1965.

With internal production expanding somewhat more than in 1965 and the total number of persons gainfully employed even declining somewhat in the Community, the advances in overall productivity (in terms of real gross value added per person gainfully employed) were somewhat greater than in 1965.

In 1966, the average number of persons in paid employment over the year was—as in 1965—only slightly higher than in the previous year. A somewhat more vigorous growth in France was largely offset by a slowdown in Germany and in Belgium and a slight decline in Italy. Seasonally adjusted, the number of persons employed in Italy, especially in industry, increased somewhat as the year advanced, while in Germany there was a certain decline, particularly in the second half of the year.

The number of self-employed persons in the Community, most of them in agriculture, probably continued to decline slightly in 1966.

The total number of hours worked by persons in paid employment was probably somewhat higher in 1966 than in 1965, when it had dropped distinctly below the 1964 figure. The tendency to shorten the agreed working week was on the whole somewhat weaker, and in addition there were fewer sectors than in the previous year where the annual holiday was lengthened. In France and even more in Italy the revival of business activity, particularly in industry, led during most of the year to a considerably longer working week per person employed. The effects of this tendency on the total number of hours worked in the Community as a whole were not fully offset by a tendency for hours worked to contract in some other member countries, particularly Germany, from about the middle of the year, or by a slight further reduction in the hours worked in some industries faced with structural difficulties.

The number of unemployed, which was already up in 1965, was slightly higher in 1966. This development is reflected not only in the Community figures for the full year but also—apart from Italy—in the seasonally adjusted manpower figures for 1966. In most Community countries the number of persons seeking work tended to rise, and the number of unfilled vacancies registered with the labour exchanges showed, after adjustment, a tendency to fall. In France, however, the upswing of economic activity was quite distinctly reflected in the trend of unfilled vacancies. If the number of unemployed in this country tended to rise, this was largely due to a perceptible increase in the labour force—partly a result of greatly increased net immigration—and perhaps also to the quieter tone in housing. As the year advanced, unemployment in Italy showed signs of declining.

In spite of the tendency for pressure to ease, the labour markets in most Community countries, particularly Germany and the Netherlands, were in 1966 still short of manpower, at least up to the middle of autumn. The number of unfilled vacancies was still considerably greater than the number of unemployed.

4. Balance of the markets

Imports of goods and services from non-member countries rose quite considerably in 1966. Visible imports probably expanded 6 % in terms of volume and 8 % in terms of value (as shown in the customs returns), or somewhat faster than in 1965 (5 % and 6.5 %).

The higher figure for imports is, however, partly accounted for by the difference between the level reached before the end of 1965 and the average level throughout the year; it conceals the fact that in the course of 1966 the trend flattened out. Since spring 1966 the trend of Community imports has reflected the quieter tone of business activity in several member countries, particularly in Germany, less notably in the B.L.E.U. This was only partly offset by a further rapid expansion of imports by France and Italy. In addition there were movements connected with the stock cycle and, as a special factor, a substantial reduction of Germany's imports of defence material.

Visible imports from non-member countries
(Value and % change on preceding year)

Source	1965		1966			
	million u.a. (1)	%	1st quarter	2nd quarter	3rd quarter	Full year (5)
All non-member countries	28 562	+ 6.5	+ 13.5	+ 8.5	+ 5.5	+ 8
of which :						
Industrial countries (2)	16 216	+ 5	+ 15	+ 7	+ 4.5	+ 8
including :						
United States	5 687	+ 4.5	+ 20	+ 2	+ 4	+ 7.5
EFTA	6 893	+ 4.5	+ 9	+ 7	+ 4	+ 6
United Kingdom	2 605	+ 1	+ 9.5	+ 5	+ 5	+ 7
Developing countries (3)	10 522	+ 7	+ 10	+ 9	+ 6.5	+ 7
including :						
Associated overseas countries and territories	2 046	— 0.5	+ 9	+ 12.5	+ 17	+ 13
Central and South America	2 615	+ 6	+ 4.5	+ 7.5	+ 0.5	+ 3
Other areas (4)	1 824	+ 18	+ 24.5	+ 21.5	+ 11	+ 18

Source : Statistical Office of the European Communities.

(1) 1 u.a. = 1 unit of account = 0.888671 gm. of fine gold = US \$1 at the official rate of exchange.

(2) Class 1 of the Standard Country Classification for Foreign Trade Statistics of the EEC.

(3) 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 sources.

(5) Commission forecasts.

The slackening of demand for imports into the Community was most evident in the purchases of raw materials and semi-manufactures; for the Community as a whole these registered only a slight advance on 1965. In addition, food imports by member countries in 1966 were affected by the rather good harvest in 1965, particularly grain; consequently they will probably have risen less than in the previous year. Finally, the slowdown in investment activity, particularly in Germany, the leading importer of investment goods, had an appreciable dampening effect on imports of plant and machinery into the Community. It was almost only purchases of consumer goods that registered a brisk rise, mainly a result of the vigorous expansion of demand from France and Italy.

The restraint in demand for raw materials and the relatively weak growth of agricultural imports into member countries were particularly noticeable in the trend of Community imports from developing countries. Only imports from associated overseas countries and territories showed a distinct recovery, which was mainly attributable to an increase in purchases by France. Imports of finished goods and especially of plant and machinery were influenced both by the slower expansion of demand in this sector, with its inevitable impact on goods from industrialized non-member countries, and by certain supply factors in some supplier countries. The perceptible slowdown in the growth of imports from the United States, for instance, can be explained in part by the lively expansion of domestic demand in that country; similarly, the persistent inflationary trend in most EFTA countries had a retarding effect on the expansion of exports from that group of countries. The progressive slowdown of domestic demand in the United Kingdom, on the other hand, enabled exports to the Community to recover distinctly.

Intra-Community trade again expanded vigorously in 1966. The value of visible trade is likely to have increased by 12 % (on the basis of customs returns), following an increase of 13.5 % in 1965. The slight decline in growth is attributable to the fact that the very lively expansion in the early months of the year, which was certainly due in part to the effects of the reductions in internal duties that became effective on 1 January—was followed in spring by a perceptible slowdown in the rate of economic growth, itself largely a result of the weakening of economic activity in Germany. After expanding briskly in 1965 and having been primarily responsible for the vigorous growth of intra-Community trade, Germany experienced a marked slackening of business activity as the year 1966 advanced. Consequently, Germany's imports from other member countries—after having increased by 31 % in 1965—will in 1966 probably have been at very much the same level as in 1965. At the same time the growth of imports by B.L.E.U. was also weaker than in 1965, while imports by the Netherlands have also shown signs of growing somewhat more slowly since the beginning of autumn. French and Italian imports from Community countries, on the other hand, continued to increase at a rapid pace; although however they will probably have been 21 % and 25 % higher than in 1965, this will not have entirely offset the damping effect on overall intra-Community trade produced by the trend of imports into other member countries.

On the exports side, expansion of demand from France and Italy was largely responsible for an increase in Germany's exports to the other Community countries of

about 16 %, compared with the 6.6 % of 1965. French and Italian exports to other Community countries have shown a distinct tendency to slacken since spring, but because of the lively rise in their mutual trade their exports again registered a vigorous expansion for the full year. Owing in part to a number of special factors, but in part also to the quieter demand for imports in Germany, the growth of exports from the Benelux countries to other member countries was rather modest.

As in previous years, intra-Community trade played an important role both as a stimulant to expansion and as an element contributing to balanced economic activity in the member countries. It was in particular for Germany that trade between the member countries proved to be a stimulant to expansion; it provided an increasing measure of support when business activity was otherwise inclined to lose momentum. It has also been a factor that has contributed to stabilization or the maintenance of stability particularly in France, Italy and the Netherlands, where the accelerated rise in imports from other Community countries improved overall supply and so made it possible to avoid or reduce inflationary pressures.

This aspect of intra-Community trade is also reflected in the balance of trade between each member country and the remaining Community countries. In Germany, for instance, the previously considerable deterioration in the balance of intra-Community trade, which had led to a heavy deficit in 1965, was followed by a very appreciable improvement in 1966 (of the order of some 650 million u.a.). In contrast to this, the faster increase in French and Italian imports and the quieter trend of their exports were accompanied by a distinct tendency for their trade balances to deteriorate; in Italy, however, this deterioration has so far been fairly limited, as sales to France in particular have still registered a lively growth despite the generally quieter trend. Italy's trade with other Community countries will probably still show a considerable surplus for the whole of 1966. The trade balances of the Benelux countries were in the main unchanged : B.L.E.U. trade with the rest of the Community again produced a large surplus, despite a slight tendency to deteriorate in the course of the year. The Netherlands' deficit, on the other hand, was again about as heavy as in 1965.

In 1966 the general price level in the Community again showed a perceptible overall increase, comparable with that of 1965. The index of consumer prices (as defined for the national accounts) showed an increase of 3.5 % for the full year.

From mid-year, however, the upward trend of prices has—according to the consumer price indices in the various countries—shown signs of flattening out in those countries (Germany and Benelux) where till then the increase had been steepest.

The quite vigorous increase of prices in the Community, which persisted despite the slackening in the expansion of demand in most member countries and despite the generally satisfactory balance between supply and demand in France and Italy, is due

mainly to the passing on of previous and fresh increases in cost, which in turn were in very large measure a sequel to the previous state of severe imbalance. This development was clearest in the Benelux countries and—though to a less marked extent—in Germany. In addition, world prices for certain imported raw materials and semi-manufactures were, for the year as a whole, higher than in 1965 and therefore helped to push prices up. Lastly, considerable influence was exerted by “autonomous” factors making for price rises, such as increases in indirect taxation, the cost of public utilities, rents, and agricultural prices.

Rise in consumer prices
(as defined for the national accounts)

% change on preceding year

	1964	1965	1966 (1)
Federal Republic of Germany	2.4	3.3	3.5
France	3.4	2.6	3
Italy	6.0	4.0	2.5
Netherlands	6.4	3.8	6
Belgium	3.3	4.5	4.5
Grand Duchy of Luxembourg	4	4	4
Community as a whole	3.7	3.3	3.5

(1) Commission estimates.

In the Community as a whole, wage costs per unit of output again rose considerably in 1966, if somewhat less vigorously than in the previous year.

As in 1965, the rise in wage costs per unit of output for the year as a whole will probably have been strongest in the Netherlands and in Belgium, again principally owing to a particularly sharp rise in wages. Italy showed the smallest increase, as in this country the productivity of labour, especially in industry, advanced perceptibly while the rate at which wages were expanding slackened.

In the industrial field, the prices for some basic materials and semi-manufactures displayed a tendency to weaken, mainly as a result of the structurally unfavourable market situation, but partly also because of the quieter trend of business activity in Germany and the Benelux countries. In Germany, the upward movement of prices for industrial finished goods also slackened. In Belgium there was a similar development in wholesale prices, but in retail prices no levelling off is yet to be seen. Although in the

Netherlands too the upward movement of prices has slackened somewhat in various branches of industry, it would be premature to speak of any generally perceptible easing. The hitherto rather feeble reaction of prices in the Netherlands and in Belgium to this tendency for pressures to ease may be due to the scale of wage increases in these countries having been far greater than, for example, in Germany. In Italy price increases have been within very narrow limits. In France, too, the prices of industrial products have risen but little, although the pace accelerated slightly as the year advanced.

Apart from Italy, prices for services in the Community as a whole rose very considerably. Agricultural prices also continued to rise. Among crop products it was mainly the prices for items that depend on the weather (potatoes, fruit and vegetables) which at times contributed to an upward movement of the general price level. Owing to poor crops in 1965 and to bad weather early in the following year, the prices of these products rose vigorously in the first half of 1966 but declined again appreciably in summer, mainly because harvests were better than in 1965. Towards the end of the year the price of certain crop products again tended to move upwards. Price trends for livestock products varied fairly considerably from one country to another. Pigmeat prices, for instance, reached a much higher average for the year—following a distinct rise in the second half of 1965, a slight decline thereafter and a fresh increase in the second half of 1966. Prices for beef developed more favourably; the upward trend that had been typical throughout the Community since 1963 came more or less to a standstill as the year 1966 advanced.

In spring 1966 there was an improvement in the Community's balance of visible trade, which had been deteriorating from the second quarter of 1965 on. As a result of the fairly vigorous pace at which exports to non-member countries were again rising and of the reduced impact of imports, the deficit fell considerably as the year progressed; at an estimated 1 400 million u.a. for the full year 1966, it will probably have been even somewhat lower than in 1965 (some 1 500 million u.a.).

The current balance of payments was largely marked by these trade results, and the surplus may well have again been slightly higher than in the previous year. According to the—still very incomplete—information available, capital movements between the Community and non-member countries are no longer likely to show an appreciable surplus. This is in part attributable to the considerable special payments by Community countries, in particular the advance repayments of debts by France and Italy; at the same time, the inflow of private capital is likely to have declined, mainly as a result of measures taken by the United States and the United Kingdom in the fields of short-term economic, credit and balance-of-payment policies.

The gross gold and foreign exchange reserves of the member countries' monetary authorities increased by almost 310 million u.a. from the end of December 1965 to the end of November 1966, against a decline of 300 million u.a. in the corresponding period of the previous year. During the same period, the net foreign exchange position of the commercial banks again showed a substantial if somewhat smaller improvement than from the end of December 1964 to the end of November 1965.

All in all, transactions with non-member countries in 1966 had an expansionary effect on internal liquidity in the Community. The pattern, however, depended on the time of the year and was different in each member country. In Germany, for instance, transactions with non-member countries still tended to reduce liquidity in the first half of the year; later, the progressive improvement of the balance of payments gradually led once more to an increase. In France, and to a lesser degree in Italy also, the situation developed in the opposite direction as the year advanced; in both countries, however, and particularly in Italy, the supply of money still benefited considerably from the balance-of-payments situation. In the Benelux countries, on the other hand, this same factor tended to reduce liquidity almost throughout the year.

The cash operations of the public authorities and the methods adopted for financing the deficits increased domestic liquidity in almost all member countries, but more particularly in Belgium and the Netherlands, and to a far greater extent than in 1965. In France and Italy, too, the cash operations of the public authorities did much to increase liquidity, in contrast to what happened in 1965, especially in France; in Italy, however, this increase was largely offset by a vigorous expansion of official calls on the capital market, especially in autumn.

The expansion of bank lending to business and private customers slackened somewhat in Germany and—even less distinctly—in the Benelux countries; this was mainly due to the reduction of bank liquidity caused by the balance-of-payments deficits, by the fact that the banks had already lent more generously, and also to the measures of credit restriction, which in some cases were tightened up. A partial exception was Germany, where the restrictions were in effect relaxed during the second half of the year, inasmuch as the expansionary effects of the improvement in the balance of payments were not offset by correspondingly more severe measures of restraint. On the other hand credit expansion accelerated vigorously in Italy and even more in France, countries where credit policy was applied on fairly flexible lines.

Until the summer of 1966 the capital markets of most member countries were under increasing pressures; interest rates and yields rose considerably, especially on the bond markets. The sharpest rise occurred in Germany, but in the Netherlands, too, interest rates soared; the trend in B.L.E.U. was quieter; on the French and Italian capital markets interest rates remained during the first half of the year relatively low and in the main steady.

As the year advanced, these trends began to change everywhere except in Belgium, where interest rates still had some leeway to make up and investment activity was rising if anything a little faster than before. In Germany and the Netherlands the advances registered in the earlier part of the year came to a halt, and in Germany there was even some actual decline. In Italy and France, on the other hand, rates started to harden more or less distinctly.

The differences observed between groups of countries and from one period to another reflected variations in investment activity and in the impact of the balance-of-payments situation of each country; the increasing shortage of available funds and higher interest rates also reflected the deteriorating relationship—which has assumed an almost structural character—between current income and current expenditure in enterprises (the result of wage inflation) and in the public sector (caused by the scale of expenditure on items that contribute directly or indirectly to the expansion of private consumption); at the same time the propensity to invest was in both sectors high or still rising. In addition there was strong demand from American firms and banks—much of it directed to the Euro-dollar market, which has become very attractive to banks in the member countries. This help to keep interest rates high (in Germany) or to put them up (in Italy and France). Finally, direct links between firms and credit institutions in the two groups of countries also helped towards aligning interest rates in the Community (which has in fact meant increases in Italy and France rather than reductions elsewhere).

Demand for and supply of goods and services

	1964 ⁽¹⁾	1965 ⁽¹⁾		1966 ⁽⁴⁾		1967 ⁽⁵⁾
	At current prices in '000 million u.a. ⁽²⁾	% change on preceding year ⁽³⁾				
		Volume	Value	Volume	Value	Volume
Gross fixed asset formation	65.6	+ 3.5	+ 6.0	+ 3.5	+ 6	+ 3
Public current expenditure on goods and services	39.7	+ 4.4	+ 9.8	+ 3	+ 8.5	+ 4
Private consumers' expenditure	169.1	+ 4.2	+ 7.6	+ 4.5	+ 8	+ 4
Gross Community product	279.2	+ 4.1	+ 7.6	+ 4.5	+ 8	+ 4
Balance exports ⁽⁶⁾ less imports ⁽⁶⁾ (in '000 million u.a. current prices)	+ 1.4		+ 2.8		+ 3.5	+ 4.0

⁽¹⁾ Source : Statistical Office of the European Communities : national accounts from 1955 to 1965.

⁽²⁾ 1 u.a. = 1 unit of account = 0.888671 gm. of fine gold = US \$1 at official exchange rate.

⁽³⁾ Community aggregates based on official exchange parities.

⁽⁴⁾ Commission estimates.

⁽⁵⁾ Commission forecasts.

⁽⁶⁾ 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.

On the equity markets, prices maintained their distinct downward trend throughout the year, particularly in those countries (Germany, Benelux) where the prospects for expansion were deteriorating and the pressure on profit margins continued unabated; investors preferred the more attractive fixed-interest securities, while the unfavourable trend on the New York stock exchange and considerable sales by non-resident shareholders had a depressing effect on prices.

B. Outlook for 1967

The expansion of nominal overall demand in the Community between 1966 and 1967 will doubtless be slightly weaker than that between 1965 and 1966; both internal and external demand will probably be less vigorous.

World business trends will in all probability be quieter in 1967 than in the preceding year. The main ground for this conjecture is that economic expansion in the United States may lose momentum during the year. Elasticity of production will probably decrease; American experts estimate the limit for non-inflationary expansion of the gross national product at about 4 %, compared with an increase from 1965 to 1966 which was probably 6 %. In order to keep the expansion of nominal overall demand within the bounds of this feasible growth rate, steps additional to the braking measures already resorted to (mainly concerning industrial investment) will perhaps have to be taken. Indeed, the rise in capital expenditure by enterprises now seems to be becoming somewhat more moderate and there are even downward tendencies in housing construction. Government expenditure is rising very steeply, however, and since a spate of wage increases is also to be expected in 1967, this could result in acceleration of the increase in private consumers' expenditure.

However that may be, it would be cautious to anticipate that the increase both in national product and nominal demand during 1967 will be smaller than in 1966—though a continuation of excess demand and price increases is also to be expected. The result of this would be that the imports of the United States again rise steeply, though not so rapidly as between 1965 and 1966.

In the United Kingdom, as a result of cyclical factors and the anti-inflationary measures taken to correct the balance of payments, practically no substantial increase in domestic demand can be expected in 1967. Expenditure by enterprises on plant and machinery will no doubt fall off, although the shortage of liquidity available to enterprises, which was a restraining factor in the previous year, should be attenuated for several reasons such as refunds and premium payments under the selective employment tax, the initial payments of subsidies voted at the beginning of 1966 for productive investments and the effects of the anticipated improvement in the balance of payments. Other government incentives to investment which seem to be under consideration can hardly exert any substantial influence on the results for 1967. The weakness of industrial investment will probably further reduce the rise in household incomes by bringing down the level of employment and further impeding pay rises, with the result that private consumers' expenditure will show no significant increase. This is likely to be so even if public expenditure continues, largely owing to an increase in transfer and subsidy payments, to expand appreciably despite the planned limitation of public investment. Demand from abroad—coupled with increased pressure to export owing to the weakness of home demand—should provide a comparatively strong stimulus.

Since the effects of the various elements in total demand may approximately balance each other, the real gross national product of the United Kingdom can be expected to show little if any increase in 1967 over 1966. In these circumstances and in spite of the cancellation of the import surcharge on semi-finished and finished goods, no significant increase in imports can be foreseen.

The growth of demand in the other EFTA countries will no doubt be impaired to a certain extent by the developments in the United Kingdom outlined above. However, in most of these countries, domestic factors, especially the growth of government expenditure and of income from wages that can be expected everywhere, may outweigh both the United Kingdom's influence and the waning impact of their own restrictive fiscal and credit policy, in fact they may even cause demand as a whole to accelerate slightly again. This should push up imports into these countries, especially as their elasticity of production still appears by and large to be limited, while prices and costs are increasing fairly considerably.

Although world demand for raw materials and semi-finished goods will probably rise less in 1967 than in 1966, the slowdown should not be such as to cause steep falls in prices. There is little likelihood, therefore, of a substantial decline in the export earnings of the developing countries. Moreover, as there has been a relatively large increase in the foreign exchange reserves of these countries, we may expect a noteworthy rise in their imports, which in fact began in the second half of 1966.

The world economic outlook for 1967—which, moreover, is also to be considered in the light of the prospects for the economic development of the Community outlined below—suggests a slight fall-off in the growth of external demand (in terms of actual exports of goods and services to non-member countries). The Community will certainly again be able to increase its exports considerably. On the one hand the supply of goods for export is sufficiently elastic quantitatively speaking; in the Federal Republic of Germany, especially, the urge to export should even become still greater, owing to the calmer domestic business climate. On the other, in view of the upward trend of costs in most industrialized non-member countries apart from the United Kingdom, there is no reason to suppose there will be any deterioration in the Community's ability to compete on world markets.

With all these factors taken into account, the increase in visible exports from the Community to non-member countries in 1967 may be estimated at about 8 % (in value) compared with about 9 % in 1966.

The Community's internal demand in money terms should also rise less than in 1966.

Gross fixed asset formation may increase in 1967 by about 5.5 % in value and 3 % by volume, compared with 6 % and 3.5 % respectively in 1966.

The slackening in the growth rate should be particularly evident in investment by enterprises in plant and machinery. In the Federal Republic of Germany this will

continue to decline, at least during a part of the year. There are various reasons for expecting a reversal of the trend, such as the continuing need for rationalization, the vigorous expansion of exports and the effects of high surpluses on current transactions, perhaps also a relaxation of monetary and credit policy, the easier situation that is expected to develop on the capital and money markets, and further steeply rising government expenditure; but it is impossible to say as yet when the turning point will be reached. In any case it may be assumed that in the Federal Republic of Germany a revival of the propensity to invest would scarcely come early enough to influence significantly the actual investment results of the year 1967. A slowing down of investment trends seems to be expected in the Netherlands as well, and this could mean quasi-stagnation in the annual figure for investment expenditure by enterprises. Investment on plant and machinery should again rise in Belgium, however, with further investments by new (mostly foreign) firms playing the chief part in this process. Finally the distinct upswing in expenditure on capital goods may be expected to continue in France and Italy. But this upward trend in France and Italy, and the more moderate rise in Belgium, will not be strong enough to outweigh, in the overall growth figure for the Community, the slowdown that will occur in the Federal Republic of Germany and in the Netherlands.

As for investment in building, expenditure on residential construction may expand more vigorously than in 1966, especially in Italy, where the recovery which began in 1966 may establish itself more firmly and become a distinct upswing. In France the difficulties caused in the changeover from one financing system to another may become progressively less acute and, in line with the general trend of incomes, some revival in effective demand for housing during the year can definitely be forecast. In Belgium the trend of building starts in recent months and the policy of expansion in the field of publicly assisted housing suggest that expenditure in this sector will rise somewhat more sharply in 1967 than in 1966. On the other hand, in view of the most recent trend of building starts and the backlog of orders in the Federal Republic of Germany, some falling off can probably be expected in expenditure on housing, while in the Netherlands there is little likelihood of any growth in this sector.

The same applies to industrial building in these two countries, whereas the prospects for expansion of this type of building in the rest of the Community can be considered fairly favourable.

In the Community as a whole public works will increase less rapidly than in the previous year. Growth for the full year must be expected to be somewhat greater in France, Italy and Belgium than it was in 1966, but there will probably be some weakness in the Federal Republic of Germany and a distinct loss of momentum in the Netherlands.

Investment in stocks is unlikely to provide any very powerful stimulus. In particular, the exceptionally high wave of stock-building noted in France during the previous year may gradually subside, and investment in stocks will in this country come more and more into line with the expansion of industrial production. Moreover, the very modest forecasts made for the expansion of demand in the Federal Republic of Germany and the Benelux countries will certainly incline businessmen towards caution over their

stocks of raw materials and semi-finished goods, although the reduction of stocks of imported raw materials in the Netherlands may be reversed in 1967. The reduction in stocks of finished goods, particularly those held by dealers, which is now depressing production in the Federal Republic of Germany, may come to an end. Moreover, a further brisk build-up of stocks of finished goods is to be expected in Italy and France because of the upswing in business trends and production.

The expansion of total expenditure on consumption should be smaller in 1967 than it was in 1966. However, from what is now known of draft budgets, it is to be expected that public current expenditure on goods and services will increase about as quickly as in the previous year. Some slackening of the still rapid rate of increase must definitely be expected in the Netherlands, Belgium and Italy if the budget estimates are not exceeded, but a speed-up is probable in the Federal Republic of Germany (connected in particular with a vigorous increase in defence expenditure) and in France.

Private consumers' expenditure should, on the other hand, increase less vigorously in 1967 than in 1966. Its growth is now estimated at about 7.5 % in value and about 4 % in volume. Thus the growth of consumption in the Community, in both value and volume, is likely to be a little smaller than during the past three years.

Trends in private consumers' expenditure in Community countries should vary more in 1967 than in 1966—partly because of the differences in business climate, but also partly because of the 1966 trends and their arithmetical effects on the annual figures. Private consumers' expenditure will certainly rise again sharply in France and Italy (by 9—9.5 % in value and by 5.5—6.5 % by volume). In the other member countries, growth for the full year—over 1966—and in the month-to-month figures should both be down more or less considerably—most in the Federal Republic of Germany and least in the Netherlands, where a 8.5 % increase for the year is still expected. There will scarcely be any perceptible slackening in the increase by volume in Belgium either.

These forecasts are chiefly based on the expected trend in disposable household incomes. Particularly in the Federal Republic of Germany, and to a much smaller extent in the Benelux countries, there should be a less marked rise in wage rates than in 1966 and some local cases of stagnation in the level of employment. Nevertheless the increase in transfer incomes will continue almost unabated and an additional growth factor in the Netherlands will be the cut in direct taxation now planned for the middle of the year. On the other hand, consumers in the Federal Republic of Germany and the Netherlands may be more cautious owing to the change in the business climate, and this would be reflected in an increase in household savings ratios. In contrast, in France and Italy a further marked increase in disposable incomes can be expected for cyclical reasons, accompanied in particular by what may well be a faster rise in total wages and salaries, due in part to a fairly distinct recovery in the pace at which employment will rise.

Community supply should adapt itself without appreciable difficulty to the expansion of internal demand, especially as elasticity of production will be fairly high in all member countries.

Assuming normal weather conditions, agricultural output may rise more markedly in 1967 than in 1966, when the harvest had been fairly poor.

The increase in industrial output will probably be less than in 1966 and—according to the definition used for the Index of the Statistical Office of the European Communities, so excluding construction, foodstuffs, beverages and tobacco—will be little more than 5 %. The smallest advance should be in the Federal Republic of Germany and in Luxembourg where industrial output is unlikely to be significantly greater than in 1966. In Belgium, a growth rate of 2.5 % is expected, corresponding approximately to that of the previous year, and in the Netherlands industrial output may rise by 5 % compared with 7 % in 1966. In France growth for the year should in view of the high level of activity reached towards the end of 1966 amount to 6.5 % to 7 %, compared with 7.5 % in 1966, and in Italy it may even be once again around 12 %.

As in 1966, the greatest increases in production will probably be achieved in chemicals, oil and consumer durables, although the output of passenger cars and commercial vehicles will probably rise more slowly than in the previous year.

A further appreciable production increase can be expected in non-durable consumer goods as well, although in 1967 the textile industry will probably not be able to repeat its performance of the previous year (an estimated increase of 10 % over 1965).

For the moment there seems little prospect of any real improvement in coalmining or the iron and steel industry. Finally, growth in the production of capital goods should remain moderate in the Community as a whole. While progress can be expected in Italy and France, the output of the Federal Republic of Germany in this sector will, during part of 1967, be influenced more by the weakness of internal demand than by rising export orders.

The contribution of the building industry to the Community's gross domestic product will probably be somewhat larger in 1967 than in the previous year, especially in Italy, where the revival in residential construction that began during 1966 will probably be maintained and gain in strength, and in France, where a marked upward movement may set in during the year, in contrast to the present stagnation in this sector. In the Federal Republic of Germany, on the other hand, and even more in the Netherlands, it seems that little if any increase can be expected.

Value added by the services sector may advance slightly less than in 1966. In structurally expanding branches such as the tourist industry, there should be another very appreciable rise owing to the lengthening of holidays; on the other hand the growth of trade may slacken a little and the development of goods transport will be slowed down further by the structural decline of coalmining and by stagnation in the iron and steel industry.

In the light of all these assumptions it would at present appear that the Community's real gross product will rise by about 4 % in 1967, that is to say slightly less than in 1966 (when it was just short of 4.5 %).

In these circumstances the labour market may well experience a further, though moderate, rise in the number of persons employed, resulting from a small increase in the labour force and a very slight reduction in the number of unemployed. The average unemployment figure for the year should show a distinct decline in Italy, whereas in the Federal Republic of Germany and in the Benelux countries a certain increase in unemployment may well be expected.

The improvement in productivity throughout the Community in 1967 (in terms of gross value added per person employed) would thus be somewhat smaller than in the previous year.

The number of persons in paid employment, particularly those in industry, should rise in France and Italy, especially as in those countries there can hardly be any further considerable increase in weekly working hours per person employed, except perhaps in the construction sector. In the other member countries, particularly the Federal Republic of Germany and the Netherlands, the rather slow growth expected in production will certainly entail a slight decline both in the numbers employed in industry and in weekly working hours per employed person. The aggregate number of hours worked in the Community should show only a negligible increase on the previous year.

Although in the Federal Republic of Germany and the Benelux countries the labour market situation will tend to ease, shortage of manpower will probably persist, albeit to a lesser degree, in several sectors of the economy. Moreover it is not unlikely that during the year rather serious difficulties in recruiting skilled workers will again be experienced in France or perhaps even in Italy.

The Community's imports from non-member countries will continue to be influenced by the slacker business trend in certain member countries, especially the Federal Republic of Germany, and, particularly where finished goods are concerned, they will probably expand slowly. Since, moreover, replenishment of stocks of raw materials and semi-finished goods is not to be expected before the end of the year, the general trend of imports into the Community should weaken a little, notwithstanding the likelihood of another very marked rise in French and Italian purchases and the disappearance of special factors (such as the decline in German Federal Government imports) which impeded the growth of imports during 1966. The increase in goods exported to non-member countries in 1967 is unlikely to exceed 7 % in value.

Since the growth in the Community's exports will probably be only a little more pronounced than that of its imports, it is unlikely that its trade deficit with non-member countries will be significantly modified.

The quieter trend of economic activity in the Federal Republic of Germany and the expected decline in the growth of exports from the Netherlands are likely to inhibit notably the expansion of visible trade between member countries in 1967, although the persistently vigorous development of demand in France and Italy will doubtless stimulate expansion considerably. An increase in intra-Community trade of 9—10 % in value can be forecast for 1967 as against an increase of 12 % in 1966.

The prospects for supply and demand in the Community as a whole and in the individual member countries (see the country chapters that follow) suggest that the excess demand which was prevalent in much of the Community will to a great extent have disappeared. This would release forces that could do much towards stabilization of prices—were it not for the continued effects of cost increases and of the inflationary extension of government expenditure in recent years (effects which take the form of upward adjustments in the rates for public utilities, higher official charges, heavier indirect taxation and higher rents), and if only the upward movement of unit costs would cease at the same time as demand inflation. On this latter point, however, there is no room for optimism, especially where the total labour costs per unit of output borne by enterprises are concerned. In any case experience has shown that, owing to the time it takes managements and workers to react, or the period wage agreements may still have to run, inflation due to demand pull is usually followed by a cost-push phase even if the economic trend had meanwhile become fairly depressed—unless an incomes policy, including of course a wages policy, is applied with the necessary speed when excess demand disappears. In the case of the Community it is nevertheless possible that certain strains will persist in major sectors of the labour market on a scale that will vary from country to country and from one branch of industry to another, with the result that factors due to the balance between the supply and demand of manpower will continue to push up unit costs. In France and Italy, new factors of this kind could even arise within certain limits—apart from the fact that, in these countries too, the demand for commodities could already be exerting a pull on prices again. In Italy, moreover, certain repercussions of the flood disaster as well as various financial measures adopted largely as a result of that disaster which, like the proposed cancellation of the arrangement whereby the State met part of the cost of social benefits, add significantly to the costs falling upon enterprises.

For these reasons, the Commission does not expect any very distinct flattening of the upward trend of average consumer prices in the Community as a whole; according to the latest estimates, the consumer price index will still rise 3 % in 1967, compared with an increase of 3.5 % in 1966.

In the Federal Republic of Germany, in Belgium and to a lesser extent in the Netherlands, slackening in the growth of demand should set certain limits to the passing on of cost increases. In Belgium, too, the dwindling impact of the increase made in consumer taxes in January 1966 means that the year-to-year rise in prices should be somewhat lower. With regard to the Netherlands, there is still some uncertainty over the contemplated increase of indirect taxation. The rise in wage costs per unit of output, however, is in this country unlikely to fall below the previous year's increase by any substantial amount. The rise in prices should be somewhat smaller than before, but at some 4.5 % it is likely to be once again by far the highest in the upward movement of Community prices. In France and Italy prices are expected to show a slightly stronger upward trend than in 1966.

C. Economic policy

In the light of the outlook described above, those responsible for short-term economic policy in the Community are facing tasks that will be more than usually arduous because the forecasts—which at best can only be as sound as the assumptions on which they are based—are on this occasion especially uncertain. True, changes of trend have doubtless been forecast fairly accurately; but it is very difficult, if not impossible, to forecast with any precision the intensity of developments such as the slowdown or decline in investment by enterprises in the Federal Republic of Germany or in the Netherlands, because here psychological factors play a great part. These factors can be influenced not only by economic situations but also by political developments. It is clear that in the Federal Republic of Germany and in the Netherlands the events before the government crises—and the crises themselves—had and are still having effects that are hard to assess. In this context it should be pointed out that all prognostications are to some extent influenced by expectations as to the course of economic policy. Some of the assumptions made have not materialized, particularly as to the policy mix—the relative stress on budget policy and on monetary policy—recommended in the opinions rendered by the Commission, the Short-term Economic Policy Committee and the Monetary Committee.

All these factors caused enterprises, and perhaps also to a lesser extent consumers, to exercise greater restraint for a while than could be foreseen when the last survey of the economic situation was penned at the end of the summer holidays. While in the circumstances and on the assumptions of that time no stagnation, let alone recession, was to be expected in any member country, tendencies have in the meantime emerged, particularly in the Federal Republic of Germany, which have made a pause in economic growth much more probable.

It must be mentioned that even before the summer holidays the Commission submitted to the Council a proposal for a recommendation on short-term economic policy in the second half of 1966 and on the first measures to be taken for 1967. At that time, however, the Council was unable to deal with short-term economic policy and therefore could not bring its influence to bear on developments in 1966. A Council meeting was held on 20 December 1966, when short-term economic policy was discussed. The Commission had submitted a new proposal for a Council recommendation on this subject, which made allowance for the changed situation and set out the guidelines of the short-term economic policy to be envisaged for 1967. The proposal was adopted by the Council subject to certain amendments, and is given as an annex to this chapter.

What are the problems? First, the effects of inflationary developments on costs and prices are still being felt in the Benelux countries and to some extent in the Federal Republic of Germany too. At the same time signs are appearing, particularly in the latter country, of slacker trends in business activity which are having a direct impact on investment but are also having, indirectly, more and more effect on other factors of demand. These developments are typical of a “growth crisis” that is the logical result

of inflationary expansion in the past few years accompanied by an excessive rise in consumption and a relative reduction in *ex ante* saving both by public authorities and by enterprises. Against the background of these developments, the growth crisis has been aggravated by an economic policy which did not start to combat inflationary tendencies until too late and then almost entirely by means of a restrictive monetary policy, while budget policy had an expansionary effect, particularly upon consumption.

In contrast to this, France and Italy—member countries which passed through a more or less marked “growth crisis” in 1964/65—are experiencing a largely balanced upswing of economic activity. Although this trend is affected by damping influences from the economic situation in the other member countries, it is not impossible that 1967 may see new signs of overheating.

In view of these disparities, economic policy should vary to some extent from one country to another. In the first-mentioned group of countries the tendency for the rise in prices and unit costs to slacken must be reinforced and the efforts to stabilize them maintained—which means, of course, that these countries should not switch over too early to an expansionary economic policy in all fields, as this would inevitably inhibit the stabilizing of prices and unit costs and would in time start a new inflationary process. Alongside the stabilization drive action should be taken, especially in Germany but also in the Benelux countries, to support investment and ensure that it can once again grow steadily. In France and Italy every effort should be made to maintain economic balance and—in France—even to improve it further wherever possible.

The Community should continue to give high priority to the objective of stabilizing the price level—that is, of containing within narrow limits the rising trend of the indices. The extent to which the rise has been reduced so far is not impressive : to take the consumer price index as an example, the increase for the Community as a whole went down from 4 % in 1964 to 3.5 % in 1965 and in 1966, while a rate of 3 % is still to be expected for 1967—unless efforts are made to ensure satisfactory stabilization. These are particularly necessary in the Netherlands, with a prospective price increase of 4.5 %, and in Belgium, where almost 4 % is still expected; they are also called for in France, where the price increase (as defined above) has never dropped below 2.6 % even after the period of stabilization, and must be expected to reach almost 3.5 % in 1967. Even in the Federal Republic of Germany, which is experiencing a distinct slackening of economic activity, prices will probably be up again by 2.5 to 3 % for the full year.

There is therefore a danger that the rate of price increase will not come down sufficiently; the cause, in those countries where the price increase has been strongest so far, is not so much the way overall demand develops as past and current rises in costs. Although the situation on the labour markets of these countries can be expected to ease further, it is doubtful whether this alone will check the rise in unit costs—a prerequisite for price stabilization.

A threat could develop in the member countries concerned, particularly the Federal Republic of Germany, that too much unemployment could be “exported”—not only to

non-member countries but, unfortunately, also to a Community country (Italy), as in quite a number of sectors cuts in employment fall on foreign workers much more than on nationals. This would be contrary not only to the spirit of the Community but also to the interests of the countries concerned and of their enterprises, since clearly such exports of unemployment cannot fail to impede the slowdown in the upward movement of costs. Undoubtedly, therefore, employment policy should keep such tendencies firmly in check.

Moreover, unit costs could go on rising because of the slowness with which managements and workers, bemused by profit figures and other elements of a boom that is over, adjust their wage policies to the changed situation or, again, because current wage agreements may still have some time to run. This brings out the danger of concluding long-term wage agreements, reached under boom conditions, which provide for relatively high annual wage increases. Governments should endeavour to remedy this situation by beginning discussions with the employers and workers on a reasonable incomes policy. In these talks a true picture should be presented of the economic prospects, showing clearly that continually rising costs are not only an obstacle to price stabilization but can also bring the danger of a recession.

Finally, the proposed budget policy of these member countries for 1967—as far as it is already more or less settled or can be judged from foreseeable trends—still seems too expansionary where current expenditure neither directly nor indirectly applied to investment is concerned; certain sectors of demand would thus be kept in a state which would favour at least some increases in costs and prices. In addition there are increases in a number of indirect taxes or in the rates for certain public services, largely as a result of too sharp an expansion of expenditure on goods and services and on transfer payments in the past and of the heavier deficits to which they have led; while certain of these measures have a damping effect on overall demand, as elements affecting costs they are quite easily passed on in prices—especially when the increased revenue is promptly used in a way which stimulates demand.

In the circumstances it is to be recommended that in 1967 the Netherlands, Belgium and Luxembourg adopt a budget policy which will ensure that the relation of current income to the aggregate current expenditure of the public authorities is distinctly better than in 1966 and that the proportion of this expenditure to be financed by borrowing is therefore reduced. The foreseeable economic trends being as they are, this should be achieved primarily by cutting down the rate of increase of current expenditure which directly or indirectly contributes to consumption. Efforts in this direction have been made in Belgium, the Federal Republic of Germany and the Netherlands, but there seems to be a tendency not to place sufficient emphasis on the reduction of expenditure and prefer heavier taxation, and at the moment it cannot be predicted with certainty whether the overall effect on the demand for finance will be sufficient. It is in the Netherlands, if anywhere, that positive results appear likely; special efforts are being made there in view of the fact that the current balance of payments is also in deficit.

In any event, a policy aimed at improving the relation of aggregate current income to current expenditure in the public budgets would not only make it easier to finance the

growing volume of public investment but would also limit the calls made by the public authorities on the savings of other sectors.

Against this background the restrictions placed on credit could and should be relaxed. The first step that should be considered is perhaps a reduction in Bank rate in those member countries where bank liquidity has risen appreciably or is now rising as a result of balance-of-payments surpluses or because entrepreneurs are reluctant to make any great increase in their indebtedness when interest rates are so high.

However, this policy mix ought to be put into operation soon, while the incentive to invest offered by shortages of skilled labour, high wage and welfare costs, the increased pressure of competition, growth of exports, the long-term market prospects and investment programmes—particularly those of large enterprises—are still vigorous enough to allow the propensity to invest to pick up again as soon as internal and external financing conditions improve. Regional and local authorities at any rate would certainly not hesitate to take advantage of the improved financing possibilities.

It is evident from the economic outlook in the various countries that the need for early action to support investment is not equally pressing everywhere. It is clearest in the Federal Republic of Germany, less pronounced in the Netherlands, and still less in Belgium, where it will hardly be felt as long as foreign enterprises continue to make large-scale investments independently of the current situation, so that outlays on investment by enterprises as a whole gather momentum.

The short-term policy outlined above (applying particularly to budgets, labour market, (wages and credit), coupled with the slackening of investment and—at least in the Federal Republic of Germany—with the effects of increasing export surpluses, would considerably strengthen the downward trend of interest rates which is already becoming evident. This in turn would, at least in the longer run, encourage the propensity to invest and improve the chances for economic growth. If in the short term such a downward trend of interest rates were to elicit a widespread attitude of “wait and see”, if in other words borrowers hesitated because they were hoping for lower rates—which could even accentuate the tendency for industrial investment and residential construction to slacken—the situation might best be countered by temporary tax incentives (which would hardly affect tax revenue for 1967).

Lower interest rates in the Federal Republic of Germany and the Benelux countries would also promote the balance-of-payments equilibrium internationally. Of course this applies only if on the money and capital markets of major non-member countries interest rates are maintained at a high level, as they probably must be not only because of balance-of-payments deficits but also, in one of these countries, in order to bring internal inflationary pressures effectively under control.

But there are reasons internal to the Community which also call for the lowering of interest rates in the member countries mentioned. Moreover the interlocking of capital

and money markets, which has developed in spite of the many administrative obstacles that still exist, is already working in this direction.

In Italy and France the upturn of industrial investment still provides no cause for alarm. But the expansion of overall domestic demand in money terms is rather rapid, particularly in public current expenditure and private consumers' expenditure. Here therefore a more cautious budget policy is to be recommended, especially in view of the experience of the last few years. In France this would mean implementing the 1967 budget in such a way as to ensure that the balance stipulated in the Finance Act was really assured in 1967—unlike 1966 when, according to the estimates, there should be a slight deficit. Further measures would be involved, concerning in particular social insurance contributions and rates for public services, or else a reduction in the expansion of public current expenditure which is scheduled to increase at a higher rate in 1967. Further steps should perhaps also be taken to cut down the deficits of regional and local authorities.

In Italy, where 1966 showed a very large central government deficit (when expenditure voted outside the budget and to be financed directly from the capital market is included) and where a similar deficit must be expected for 1967—and here the increase in deficits is mainly due to a sharp expansion of expenditure on consumption—an attempt should be made, in implementing the budget, to reduce the deficit in 1967. In this process the pattern of expenditure would have to be changed in favour of a more productive use of resources. There should also be a further reduction in that part of the deficit which is financed by short-term borrowing. This will be all the more important if, as may well happen, supply in certain sectors has some difficulty in keeping up with demand following the flood catastrophe that struck several regions in Italy. In its plan for aid—which was very speedy, extensive and effective—the Government in fact provided for means of financing (primarily a general increase of direct taxation) which should not produce any great increase in the budget deficit for 1967.

So much for the main lines of the short-term economic policy the Commission considers appropriate in the present situation. It must however be stressed that speedy and effective action is called for. Otherwise the effects on economic growth of an unsuitable combination of the various instruments of policy would become more and more serious in some member countries and more and more difficult to overcome. This would not only affect those particular countries but, owing to the increasingly close economic interdependence developing in the Community, would have more or less serious repercussions on all member countries.

As the outlook is uncertain in several member countries, the instrument of policy should be and should remain particularly flexible in order to allow timely action to be taken at the first sign of untoward developments. In the event of a serious and general decline of economic activity in one or more member countries, there would probably be no immediate need for a fundamental change in the principles of the short-term economic policy outlined above. The automatic stabilization effect must however be allowed to play its part; a severe short-fall in tax revenue due to the downturn in business activity

should of course not be offset by large additional cuts in expenditure or by increases in taxation. If it were found that business activity needed further support, this should not take the form of increasing direct or indirect expenditure which contributes directly or indirectly to consumption, but should be brought about, if possible exclusively, by a judicious expansion of public investment. It can certainly be assumed that if there were a steep decline the money and capital markets would be sufficiently liquid to meet any calls for finance that stemmed from such action.

It must however be pointed out that at the moment neither the actual figures on the economic situation nor the economic outlook can in any way justify the pessimism which tends to spread through one or other of the member countries, often on a one-sided view, and as a result of generalizations drawn from the structural difficulties of this or that branch of the economy. The spread of pessimistic views may, however, itself act as a factor contributing to recession—and this should be avoided at all costs.

THE COUNCIL**Council Recommendation of 22 December 1966**

to the Member States
on the guidelines for short-term
economic policies in 1967

THE COUNCIL OF THE EUROPEAN ECONOMIC COMMUNITY,

Having regard to Article 103 of the Treaty setting up the European Economic Community,

Acting on a proposal of the Commission,

Recommends to the Member States that they should observe the following guidelines for their short-term economic policies in 1967 :

1. It is still one of the main objectives of short-term economic policy in the Community that the tendency for the general price level and unit costs to rise should be reduced considerably and as rapidly as possible.

In the Kingdom of Belgium, the Grand Duchy of Luxembourg and the Kingdom of the Netherlands particular importance attaches to this objective because in these countries the outlook for costs and prices is still in part determined by the excess demand which was until recently, or still is, a prominent feature of their economic development. If in the long run a policy intended to support economic growth is to be successful and is to offer the prospect of balanced advance, there must be a marked slowdown of the rise in unit costs and prices.

There has recently been a very distinct slackening of economic activity in Germany. Economic policy should aim at optimum growth and at stability.

In France and Italy economic activity has, after a temporary slowdown, picked up again, but there still are production factors which are not fully employed, while prices have shown distinctly less tendency to rise than in other Community countries or have been more or less stabilized. In both these countries, then, there are at present good grounds for not adopting a restrictive attitude towards domestic demand in money terms. It must, however, be ensured that this demand stays within limits compatible with the stabilization of prices and unit costs.

2. Net only in the interests of the drive to stabilize prices and unit costs, but also in order to reserve an adequate share of private savings for financing investment by enterprises and to allow for the requirements of financial policy brought to light by the work being done on medium-term economic policy, the Governments of the Kingdom of Belgium, of the Federal Republic of Germany and of the Grand Duchy of Luxembourg are recommended to make in 1967 an appreciable reduction of the aggregate cash deficit of their public authorities. In the Netherlands the deficit in the national budget should be kept, after due allowance for the proposals just submitted to Parliament by the Dutch Government, within the limits shown in the estimates for 1967.

If economic activity in the Federal Republic of Germany continues to slacken, it might prove necessary to support investment activity by additional spending. However, measures to this end should not be taken too early, and they should be so timed that excessive calls are not again made on the capital market.

3. For the purposes of this recommendation, a cash deficit is defined as that part of aggregate cash expenditure (excluding repayment of the public debt) by the public authorities (except social insurance institutions) which is not covered by current revenue but is financed by loans or other types of credit.

4. It is desirable that in implementing the 1967 budget the Government of the French Republic should ensure that no cash deficit develops and should intensify its efforts to limit the financing requirements of local authorities. Provision should in addition be made for the rapid use of the budget, in conjunction with other instruments of short-term economic policy, as a means of applying a brake if domestic demand in money terms should exceed the limits compatible with balanced economic growth.

5. The Government of the Italian Republic is recommended to take the measures needed for an appreciable reduction in the cash deficits of the public authorities in 1967.

6. In Member States where the public authorities as a whole are in deficit, the measures taken to reduce these deficits should be such that they have a stronger impact on private consumption than on gross fixed asset formation. In the Italian Republic, sharp action to brake the expansion of expenditure which contributes directly or indirectly to higher consumption would be particularly appropriate as the measures and expenditure which directly or indirectly promote investment ought to be stepped up.

7. The recommended reduction of deficits could be achieved either through measures making for a slowdown in the expansion of expenditure, or through measures to increase current revenue, in particular receipts from taxation, or through a combination of both types of measure. In this connection the Governments of the Member States will have, as part of the action they take to implement the common policies provided for in the Treaty, to make the necessary provisions for gradually increasing the rates of those public service enterprises which are heavily in deficit; these increases should be effected when the deficit cannot be eliminated by rationalization and should assure that the rates come closer to actual costs. By analogy, these considerations also apply to contributions to

the social insurance system where it is heavily and increasingly in deficit; the sale of assets held by the social insurance institutions should not be considered as an appropriate remedy.

8. All Member States should draw on domestic savings to finance the cash deficits of the public authorities. The Italian authorities should gradually reduce that part of the aggregate cash deficit of the public authorities which is financed through short-term borrowing, and should ensure that finance is obtained mainly out of domestic savings.

9. The above recommendations should be reviewed if economic activity shows a marked slowdown.

10. Once budget policy in the Benelux countries is guided by the requirements of short-term economic policy as set out in the above principles, there could be a corresponding relaxation—very desirable in view of the tendency for investment to weaken—of restraints on credit.

In the Federal Republic of Germany the measures in restraint of credit could be relaxed, this being done as part of an overall programme which aimed at both economic growth and stability and followed the guidelines of this recommendation.

In the French Republic and the Italian Republic, credit policy can doubtless remain flexible for the time being, but too rapid an expansion of credit should be avoided. If fresh signs of strain appeared in prices and costs, credit policy should again be tightened in good time.

11. All Member States should intensify their struggle against those restraints of competition which contribute to rising prices, and they should in general exercise a close supervision on the formation of prices on markets where competition is not sufficiently active. In addition it is advisable that, if fresh price strains should occur, they should also be combated by reducing intra-Community customs duties ahead of schedule and by reducing external customs duties—an expedient still open only to France and Italy—to the levels fixed in the common customs tariff. Lastly, Member States should also intensify their struggle against structural factors making for price increases, especially by stepping up action to rationalize the machinery of production and distribution and to increase the mobility of the factors of production—and more particularly of labour through improvements in vocational training and retraining.

12. While still maintaining the measures required for supervising prices, the French Republic should continue to relax the price freeze.

13. In order to promote price stability but also to increase the funds available for non-inflationary financing of investments, Member States are recommended to encourage private saving by appropriate measures.

14. For the sake of stabilizing prices and unit costs but also for promoting economic growth, the Governments of all Member States should intensify their efforts in connection

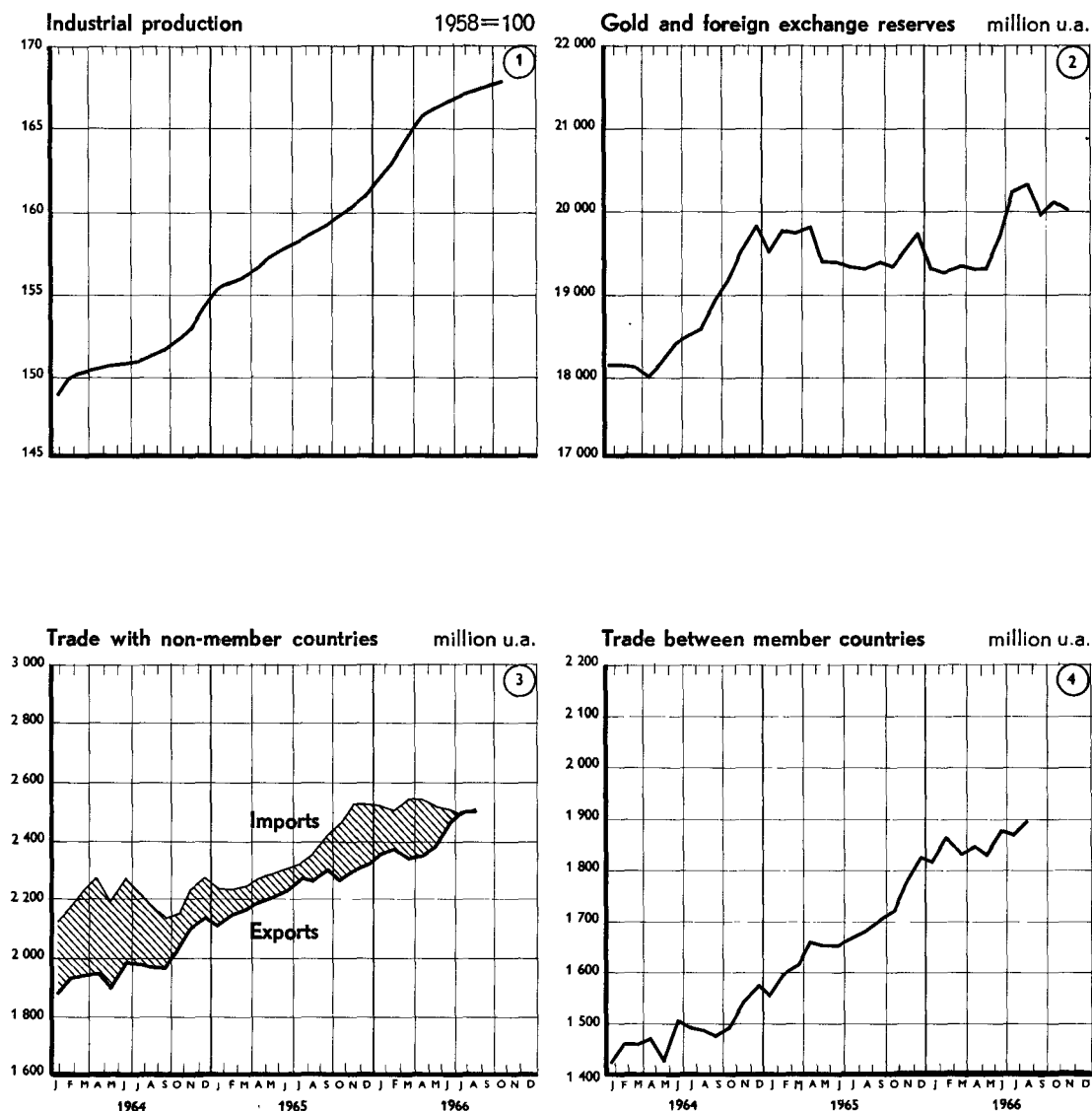
with incomes policy and should, by discussions with representatives of the major occupational groups, try to ensure a reduction of the gap which still exists between the trend of gross income per head in money terms and the trend in the output of goods and services per head in real terms. Here special attention should be paid to the wage trend in those member countries where profits and consequently saving by enterprises, and in turn their ability to finance investment from their own resources, have in the past few years declined sharply in absolute or in relative terms. This applies in particular to the Kingdoms of the Netherlands and of Belgium, the Federal Republic of Germany and the Grand Duchy of Luxembourg, that is, to those Member States where according to preliminary estimates comparing 1966 with 1965 the rise in the gross income per person in paid employment in money terms was at least double the rise in real gross national product per person in paid employment. The authorities of the French and Italian Republics are recommended to do everything in their power to ensure that in 1967 the total wages and salaries bill develops in step with the volume of production.

15. The recommendations addressed to Italy may need to be amended in order to allow for the situation resulting from the catastrophes which have struck a number of regions.

16. In implementing this recommendation, Member States should take any special measures needed to protect the economically weakest sections of the population.

17. At a meeting to be held in July 1967 on problems of short-term economic policy the Council will examine the progress made in the implementation of this recommendation.

ECONOMIC INDICATORS



NOTES:

Source: Statistical Office of the European Communities.

Graph 1. Trend curve; estimation established on the basis of indices adjusted by the SOEC for seasonal and fortuitous variations (excluding construction, food, beverages and tobacco).

Graph 2. Total gross reserves of gold and foreign exchange held by the monetary authorities of the Community countries at the end of each month.

Graph 3. Three-monthly moving averages of the seasonally adjusted value of exports to non-member countries (fob) and imports from these countries (cif), as shown in customs returns.

Graph 4. Three-monthly moving averages of the seasonally adjusted value of trade between EEC countries, as shown by customs returns for imports.

u.a.: one unit of account = 0.888671 gm. of fine gold = US \$1 at the official rate of exchange.

TABLE 1: Basic data (1965)

Total area ('000 sq. km.)	1 167.5
Total population ('000)	181 550
Density of population per sq. km.	156
Working population ('000)	74 650
Working population, breakdown by main sector (%)	
— Agriculture	18
— Industry	44
— Services	38

TABLE 2: Development of basic economic data

	% change by volume on preceding year							Volume indices (1958 = 100)	Contri- bution (in %) to GNP
	1959	1960	1961	1962	1963	1964	1965		
Gross Community product	5.1	7.7	5.4	5.6	4.4	5.8	4.1	145	—
Industrial production	6.3	11.9	6.9	5.8	5.2	7.1	4.4	158	—
Visible imports	5.1	20.5	6.0	11.3	10.2	6.9	5.0	185	—
Private consumers' expenditure	3.7	6.2	6.2	6.4	6.0	4.4	4.2	143	61
Gross fixed asset formation	8.3	10.3	10.1	7.2	5.3	8.4	3.5	167	23
Visible exports	12.5	11.1	3.0	1.0	3.8	9.3	11.0	164	—
Intra-Community visible trade	24.2	22.0	15.0	13.9	16.0	13.2	12.2	292	—
Gross product per capita	4.2	6.7	4.4	4.3	3.2	4.6	3.0	135	—

TABLE 3 : Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1958 = 100)	1964	147	152	156	156	159	155	143	121	154	159	164	157
	1965	154	159	157	163	164	164	147	128	162	167	171	166
	1966	162	166	170	174	174	175	158	134	169			
Imports from non-member countries (cif, million u.a.)	1964	2 288	2 186	2 237	2 381	2 192	2 320	2 254	1 886	2 085	2 270	2 238	2 460
	1965	2 243	2 090	2 422	2 363	2 380	2 352	2 404	2 156	2 386	2 443	2 558	2 754
	1966	2 516	2 367	2 782	2 525	2 563	2 622	2 418	2 308	2 605			
Exports to non-member countries (fob, million u.a.)	1964	1 891	1 878	1 959	2 038	1 866	2 036	2 053	1 731	2 030	2 252	2 113	2 291
	1965	1 940	2 064	2 414	2 172	2 249	2 192	2 348	1 997	2 239	2 380	2 367	2 649
	1966	2 153	2 179	2 567	2 372	2 451	2 502	2 506	2 226	2 460			
Balance of trade (million u.a.)	1964	- 397	- 308	- 278	- 342	- 326	- 288	- 201	- 155	- 55	- 18	- 125	- 169
	1965	- 303	- 26	- 7	- 196	- 131	- 160	- 56	- 159	- 97	- 63	- 191	- 105
	1966	- 363	- 188	- 215	- 153	- 112	- 120	+ 88	- 82	- 145			
Intra-Community trade (million u.a.)	1964	1 436	1 452	1 496	1 577	1 415	1 576	1 532	1 243	1 512	1 654	1 510	1 623
	1965	1 445	1 576	1 801	1 680	1 661	1 691	1 735	1 437	1 734	1 871	1 812	1 933
	1966	1 654	1 790	2 087	1 858	1 902	1 968	1 853	1 636	1 967			

NOTES

Source : Statistical Office of the European Communities.

Table 1

- Total population at mid-year.
- Population in employment at mid-year.

Table 2

- The final column of the table gives a % breakdown of GNP at market prices by main categories of expenditure. The calculation of the Community's GNP has been made on the basis of official rates of exchange.
- Industrial production: index of the Statistical Office of the European Communities, excluding construction, food, beverages and tobacco.
- Imports of goods (cif) from countries which are not members of the EEC, as shown by customs returns.
- Exports of goods (fob) to countries which are not members of the EEC, as shown by customs returns.
- Trade between EEC member countries, as shown by customs returns relating to imports.

Table 3

- See note to Table 2.
- Values in the last column of the table are expressed in million units of account. Conversion into units of account was effected at official exchange rates (1 unit of account = 0.888671 gm. of fine gold = US \$1 at the official rate of exchange).

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

A. Federal Republic of Germany

In the course of 1966 economic growth gradually lost momentum, and after the summer holidays there was even a slight decline in industrial production. In the early months of the year there was still considerable excess of demand, but subsequently one of the main components of domestic demand, the investment expenditure of enterprises, ceased to expand and even showed a slight tendency to decline; this in turn affected the trend of employment, the climate on the labour market and also private consumers' expenditure which, though it continued to rise, did so only at a slower pace.

Although the situation on the labour market eased more and more, the upward movement of costs persisted. The rise in the level of consumer prices accelerated further in the early months of 1966, was interrupted in summer by seasonal and special factors, but continued in autumn—although, as a result of the quieter demand situation, at a slower rate than previously.

It appears at present that, despite the decline in investment, which will probably continue for some time, there will in 1967 be a further, if relatively moderate, growth in real gross national product. The sustained and lively expansion of exports in particular may well lead to an appreciable improvement in the trade balance, which—by increasing the liquidity of the financial markets—might contribute to the support and eventually to the recovery of economic activity at home.

The present outlook can be said to provide a favourable setting for a resumption of balanced economic growth. But this calls for an economic policy which should be entirely focused on support of economic expansion and the stabilization of prices and costs. This policy should therefore aim not at stimulating expansion generally but, by restricting public expenditure on goods and services, at promoting price stabilization while leaving a greater share of the savings of the other sectors available for the financing of private investment. As budget policy is brought in line with these principles and there are signs that the trend of costs is being sufficiently stabilized, the restrictions on credit policy could and should be further eased.

1. Balance-sheet for 1966

In 1966 effective demand from abroad, in terms of exports of goods and services, grew much more rapidly than before. The acceleration was particularly pronounced in visible exports; for the third quarter their value, as shown in the foreign trade statistics, was no less than 15.3 % higher than a year earlier, and it appears that there was further acceleration in the fourth quarter. For the full year 1966, visible exports should be up by 13 % in terms of value and 11.5 % in terms of volume, compared with corresponding increases of 10.4 % and 8.6 % in 1965.

The main stimulus to exports came from the lively expansion of demand in certain other EEC countries, particularly Italy and France, and from an increase in the pull of demand from the United States. In addition, enterprises stepped up their export drive in hopes of offsetting the weaker trend of domestic orders by increased sales abroad.

Exports of services are also likely to have risen faster than in 1965. The expansion of total exports of goods and services (as defined for the national accounts) in 1966 is estimated at some 13 % in terms of value, following an increase of 9.1 % in 1965.

The growth of domestic demand has become distinctly slacker. This development goes back to the changed trend in gross fixed asset formation, where expansion slowed down distinctly in the early months of the year already, came gradually to a full stop and finally gave way to a decline. The extent of this weakening was more appreciable than had been forecast, on the basis of certain assumptions regarding economic policy, at the beginning of the year. The increasing shortage of funds for investment, due to the vigorous and uninterrupted growth of current expenditure by both public authorities and enterprises, to the after-effects of the deterioration in the balance of payments and to the curb on credit, proved to be considerably more acute than could have been foreseen.

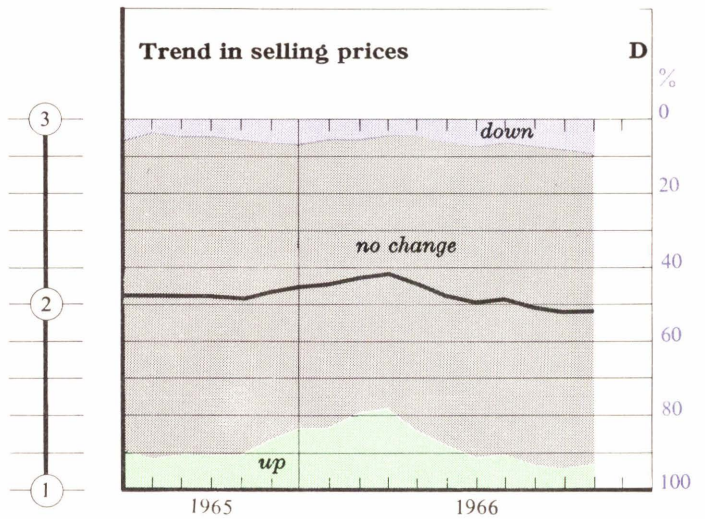
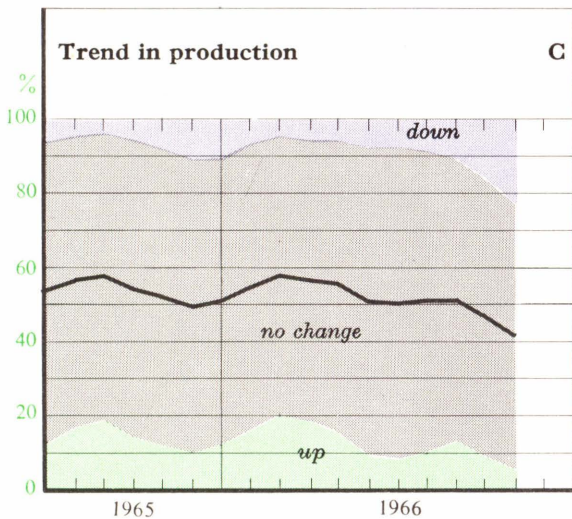
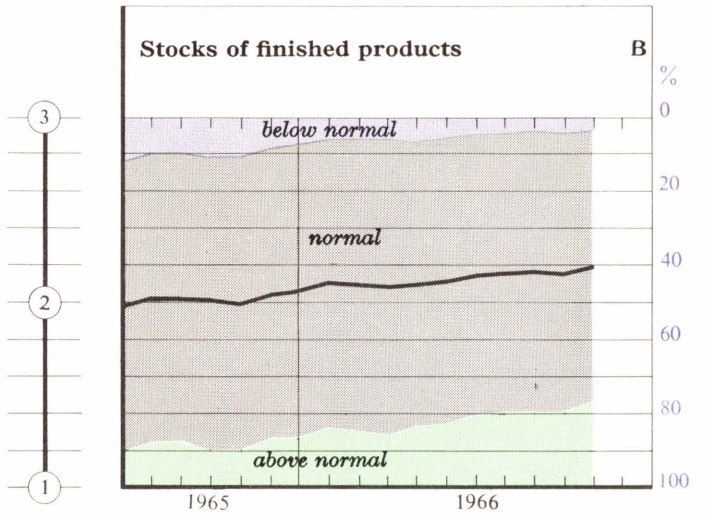
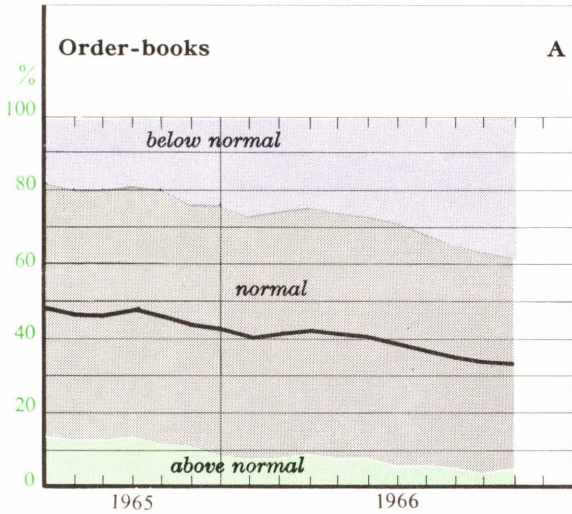
The weakening of investment activity was particularly marked in plant and machinery. In 1965 investment in this sector had risen by 13.8 %, the rise in 1966 is estimated at some 2 %.

In contrast to previous periods of reduced economic growth, when expenditure on building and construction had expanded steadily and as a rule vigorously, the growth of expenditure now slowed down in this field too, earlier indeed than in plant and machinery. Orders for new buildings even showed a decrease in 1966, which was strongest in the public sector; so far expenditure has not kept fully in step with this trend, mainly because the building industry had a backlog of orders which was largely worked off in 1966, but civil engineering and industrial building were distinctly affected. Though the output of housing has of late been growing less rapidly, the number of completions in 1966, estimated at 550 000 can still be looked upon as high when the changes, including structural changes, in the market situation are taken into consideration.

Investment in stocks seems to have been decidedly lower than in 1965. Industry trend to keep stocks as low as possible; the immediate reasons were financial and that the prices of raw materials and semi-manufactures on the world market were inclined to ease, but firms also wished to adapt themselves to the quieter trend of production. Dealers, particularly in the consumer goods sector, temporarily increased their stocks of finished goods, as it took some time to gear the amount of goods received to the changed situation. Later in the year the position was if anything reversed : the amount of goods received being below the level of sales.

The rate at which public current expenditure on goods and services expanded was again brisk in 1966. As far as the civil authorities are concerned, this was mainly due to an increase in wages and salaries and to improvements in the establishment tables.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

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

A very slight slowdown in the expansion of total public expenditure on goods and services was entirely due to the fact that the growth of military expenditure marked time, imports of defence material no longer being as high as in the previous years, when they had risen steeply.

The slackening in investment activity also caused the growth of private consumers' expenditure to level off, first slowly but then more and more distinctly. In the third quarter retail sales, which account for about half of all personal expenditure, were only 4.8 % above the figure of a year earlier. The easing was most marked in the demand for traditional consumer goods (textiles, clothing). In contrast to this, the expansion of spending on items that do not form part of retail trade, in particular expenditure on holidays, was as vigorous as ever.

All in all, private consumers' expenditure will probably have risen 7.5 % (value) in 1966, following an increase of 9.5 % in 1965. The expansion of consumption in real terms, however, amounted only to some 3.5 %, as consumer prices rose faster than before.

The quieter growth of private consumer demand stems exclusively from a slowdown in the expansion of incomes; the share of the disposable incomes of households put into savings has even declined.

The expansion of incomes from wages and salaries slackened, particularly in the second half of the year. In the full year 1966 the gross wages bill in the economy was probably only 7.5 % higher than in the previous year (1964 to 1965: + 10.5 %). The slowdown was mainly attributable to a decline in the growth of the number of workers in paid employment, to a reduction of overtime and of payment in excess of agreed rates, and finally to a more moderate rise in agreed wages. Income from property and entrepreneurship has probably risen only slightly. When it is remembered that, after a tax cut at the beginning of 1965, the effect of a progressive income tax scale will have made itself felt again in 1966 with full force and that income tax payments in part still referred to the year 1964, when earnings had been high, it is clear that the incidence of taxation contributed to a weaker expansion of disposable incomes.

The slower growth in the incomes of persons in paid employment was a result of the easier situation on the labour market, which from mid-year on was sufficiently marked to be reflected in the statistics, particularly in the number of unfilled vacancies. At the end of November there were only 319 000 such vacancies on the books of the labour exchanges. In addition, the number of unemployed increased in the autumn months; by the end of November the unemployment rate (unemployed as a proportion of the total number of wage and salary earners) had risen 1 %. There are therefore unmistakable signs of a trend towards better equilibrium.

The cooling of the economic climate has also affected the employment of foreign labour. In the first half of the year the number of foreign workers increased only slightly, and from the end of June to the end of September it actually fell, moving against the seasonal trend; after the end of the year the total is likely to fall considerably further.

The fall in the numbers employed in industry is also to some extent a reflection of the changed situation on the labour market; at not quite 1 %, it may have been about on the same scale as from 1962 to 1963, but while in 1963, a year when the situation on the labour market was easing, the building industry had been a major factor in maintaining the pressures on the labour market, in 1966 it too was cutting down on manpower.

The easing on the labour market followed an uneven pattern. Some branches of industry such as mechanical engineering, which had obviously been unable to find all the manpower needed, continued to increase their labour force well into 1966, in spite of a decline in production.

The supply of goods and services also showed a notable slackening in growth. An exception was agricultural production, which reacts little to changes in the level of business activity; here the trend was far better than in 1965; largely thanks to somewhat better weather, the grain harvest was up by some 5 %. Production of fruit and vegetables showed an even more marked increase. The output of livestock products was also distinctly higher than in 1965.

The expansion of industrial production, on the other hand, slackened more and more, and in autumn there were even signs of a slight decline. According to the Federal Statistical Office's index of production per working day, the rate of growth for the full year fell from 3.4 % and 3.2 % in the first and second quarters to 0.3 % in the third quarter. For the full year 1966 productivity may have advanced by a bare 2 %, compared with 5.6 % in 1965. The trend of production in the capital goods industry was distinctly weak; from mid-year on, output was markedly below the level of the corresponding period of the previous year. Even in the consumer goods industry, where the upward movement of production had been comparatively vigorous, expansion has slackened more and more since summer, particularly among the traditional consumer goods.

In the services sector the growth of value added will have slowed down far less. All in all, the gross national product at constant prices is still likely to have risen some 3 % in 1966, compared with 4.8 % in 1965.

The expansion of imports of goods and services—still very fast in 1965—declined sharply in 1966, tending to stagnate or even to move slightly downward. In the early months of the year, imports of capital goods and consumer goods were still rising rather vigorously, in spite of the already perceptible slackening in the pressure of excess demand. However, as internal economic activity eased more and more, commercial imports of finished goods showed a marked decline. Total imports of goods (as shown in the customs returns) may have increased even less than commercial imports—i.e. a little less than 3 % in terms of volume and some 4.5 % in terms of value, against increases of 17 % and 20 % in 1965. This was due in part to the considerable reduction in Government imports, in part to the fact that, thanks to the better harvests of 1965, agricultural imports rose at an appreciably lower rate than in the previous year. Finally, the change in managements' attitude to stocks had a damping effect on imports.

In 1966 the upward trend of prices gained in strength during the first quarter and part of the second, although the expansion of demand in money terms was already showing a distinct decline. On the supply side, there were temporary shortages of some goods (fruit, vegetables, potatoes), coupled with the effects of earlier and current cost increases. There was some stabilization in the summer as the prices of these foodstuffs went down; this was followed by a renewed tendency for prices to rise, rather less vigorously than before.

At the level of industrial production, the rise in prices reached a peak in March—April with a year-to-year rate of 2.3 %. Afterwards it flattened out distinctly and fell back to 1 % in October. Unlike 1965, producer prices in agriculture did not on the whole contribute to an upward movement of the overall price level. Owing to relatively good harvests, on the contrary, the vigorous price increase of the previous year was partly cancelled out; in October the prices of agricultural products were 5 % below the 1965 level.

In 1966 the upward trend of consumer prices was more pronounced than in 1965, in spite of the tendency for economic activity to level from the spring onwards and despite the more favourable trend of agricultural prices. If the price trend for food, beverages and tobacco is excluded, the cost-of-living index rose by some 4 % in 1966, following 3 % in 1965. Including food, the rise in the index is likely to be some 3.5 % compared with 3.4 % in 1965.

The slackening of imports and the accelerated growth of exports led to a substantial recovery in the balance of visible trade. For the first ten months of the year the foreign trade statistics showed a surplus of DM 5 300 million, compared with only DM 700 million for the same period of 1965. While in 1965 there had been a deficit of some DM 800 million on external account—as defined for the national accounts—the surplus for 1966 can be estimated at DM 5 600 million.

The current balance of payments improved distinctly. While in 1965 the period January-October had closed with a deficit of as much as DM 5 600 million, the adverse balance was reduced to a bare DM 1 000 million in the same period of 1966. This was attributable to the improvement in the trade account, to a services account which did not deteriorate further and to transfer payments that closed with a somewhat smaller deficit than in the previous year.

Capital transactions (excluding changes in the foreign exchange position of the commercial banks) showed a surplus of some DM 1 700 million in the first ten months of 1966; if allowance is made for the special payments made by the Bundesbank in 1966, mainly as a result of the increase in the IMF quota and the higher share in the capital of the World Bank, the surplus on capital transactions was as high as in the period from January to October 1965. The surplus on the remaining items of the balance of payments, which is mainly accounted for by capital transactions not shown in statistical returns, and which in the previous year had risen sharply owing to high foreign lending to German enterprises, is likely to have dropped appreciably.

As a result of these various trends, the overall balance of payments of 1966 was again in surplus after the deficit registered in 1965. The surplus of some DM 2 400 million produced in the first ten months was most evident in a substantial improvement of the net foreign exchange position of the commercial banks, while the net gold and foreign exchange reserves of the Bundesbank rose by DM 450 million. This picture is of course distorted by the window-dressing transactions of the commercial banks, which always influence the end-of-year figures (in this case end of December 1965) in favour of the official reserves. At the end of 1966, too, these reserves are likely to have risen again vigorously, at the expense of the net foreign exchange position of the commercial banks.

So far, the improvement in domestic liquidity has slowed down in 1966, despite increasingly expansionary influences emanating from foreign transactions. This is in part explained by the fact that the banks expanded their lending less markedly than a year previously. At DM 5 000 million in the first nine months, short-term advances to business and private customers, for instance, were no longer rising as vigorously as in the same period of 1965 (DM 5 600 million). Initially this was due to the insufficient liquidity of the banking system, but later there will probably have been an increasing distaste on the part of borrowers for expanding their indebtedness on the terms prevailing on the market and at a time when the prospects for sales and profits were relatively poor. Lastly, the cash transactions of the public authorities were still having a vigorous expansionary effect, even if this was less pronounced than in the previous year.

The liquidity of the banking system improved as the year advanced, mainly as a result of the increasingly expansionary effect of the balance of payments in a period of slackening credit expansion. Short-term interest rates, which had been rising sharply in the early part of the year and into the summer, dipped slightly in the closing months of the year.

The volume of new issues continued to decline on the security markets. Savings turned more and more to other types of investment and it was the bond market which was most affected by the marked caution of investors. In the first nine months of 1966 the net sales of fixed-interest bearing securities totalled only DM 3 800 million which was less than half as much as in the corresponding period of 1965. The new issues on the equity market were worth somewhat less than DM 2 200 million at current prices, only two thirds of the corresponding amount in the previous year. This trend on the recognized security markets was associated with correspondingly higher transactions on the "secondary markets" (e.g. the market for loans against borrowers' notes), which were not only called upon by enterprises but also, to an increasing extent, by the public authorities.

All in all, severe imbalance persisted on the bond market and interest rates rose till the beginning of autumn. Later there were signs of stabilization and towards the end of the year it was even possible to note a fairly distinct measure of recovery. This was mainly due to the fact that the banks increased their portfolios of securities again and that, as a result of the round table talks on capital market problems, the public authorities refrained from floating new issues.

Demand for and supply of goods and services

	1964 ⁽¹⁾	1965 ⁽¹⁾		1966 ⁽²⁾		1967 ⁽³⁾
	At current prices (in DM '000 million)	% change on preceding year				
		Volume ⁽⁵⁾	Value	Volume ⁽⁵⁾	Value	Volume ⁽⁵⁾
Exports ⁽⁴⁾	91.1	+ 7.1	+ 9.1	+ 11.5	+ 13	+ 8.5
Gross fixed asset formation	109.2	+ 6.5	+ 9.4	+ 1	+ 3.5	— 1.5
Public current expenditure on goods and services	61.7	+ 6.6	+ 12.7	+ 1	+ 6.5	+ 3.5
Private consumers' expenditure	232.9	+ 6.1	+ 9.5	+ 3.5	+ 7.5	+ 2
Gross national product	413.8	+ 4.8	+ 8.5	+ 3	+ 6.5	+ 2.5
Imports ⁽⁴⁾	91.9	+ 14.8	+ 17.5	+ 4	+ 6	+ 4

⁽¹⁾ Statistisches Bundesamt, Wirtschaft und Statistik, No. 9/1966.

⁽²⁾ Commission estimates.

⁽³⁾ Commission forecasts.

⁽⁴⁾ Goods, services and factor income.

⁽⁵⁾ At prices of the preceding year.

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.

2. Outlook for 1967

As the future course of economic and financial policy is still uncertain at the time this report is being penned, any forecast for 1967 will inevitably be subject to a great deal of qualification. It can, however, be expected that the weakening of economic activity in the Federal Republic of Germany will persist for a considerable part of the year.

The very weakness of the internal situation should help demand from abroad—in terms of actual exports of goods and services—to continue expanding vigorously and this in turn may eventually contribute to a recovery in the expansion of domestic demand. Both the level of business activity in Germany and the probable trend of demand for imports in important purchasing countries provide conditions in which visible exports can go on rising rapidly—at least for some while to come. This trend is likely to benefit in particular from the continuance of boom conditions in France and Italy. The ex-

pansion of demand in the United States and in the developing countries should also provide steady support. Even if the forecasts of some general slowing in the expansion of total world demand for imports prove to be correct, industry in the Federal Republic of Germany may manage to secure a larger share of the total thanks to an improvement in its ability to deliver.

After adjustment for seasonal variations, expenditure on gross fixed asset formation will no doubt tend to decline further in the early months of 1967. Fixed investment by enterprises is a case in point; the manufacturing enterprises covered by the latest Ifo survey on investment intentions plan to reduce their expenditure on investment by some 12 % in 1967. It cannot yet be predicted when this decline—which mainly affects investment in plant and machinery—will be reversed, as so much depends on the future course of economic policy.

There are none the less a number of positive factors : the substantial expenditure on capital replacements and the growing volume of investment in rationalization undertaken under the pressure of keener competition are, for instance, likely to set a lower limit to the fall in expenditure on investment. At the same time, the vigorous expansion of demand from abroad and the rather greater liquidity provided by the growing export surpluses will provide support for the propensity to invest and eventually stimulate it again. Lastly, it is at the present juncture quite on the cards that there may be an improvement in the terms on which finance for investment can be obtained.

However, even if the propensity to invest were to pick up again soon, this could have no effect on actual investment expenditure before the autumn at earliest.

Partly because of this trend in investment by enterprises, the expansion of expenditure on industrial building will probably continue to slacken for some time. Recently, the decline in orders seems to have become somewhat steeper in housing as well. Finally, the tendency for civil engineering on public account to weaken is also likely to continue.

Unless the budget estimates are changed substantially, public current expenditure on goods and services will continue to expand very vigorously in 1967, particularly as expenditure on defence will again rise at a faster pace, after slowing down in 1966.

Although the growth of private consumers' expenditure is likely to lose momentum, there may still be a perceptible increase over the 1966 figure. On the one hand, the progressive easing of the situation on the labour market will mean that the growth of incomes from wages and salaries will be more modest. The rise in the sums which the self-employed withdraw from their businesses will probably also remain weak for some time yet. On the other hand, transfer incomes will increase vigorously, and the savings ratio is unlikely to rise significantly.

The tendency for demand to slacken during the year may prove rather greater than the corresponding tendency in the figures for supply. The pressure on prices

resulting from keener competition will be an incentive for increasing the volume of sales; in addition, there are unlikely to be further bottlenecks in manpower to impede the expansion of production. Because of the pattern of imports and production, however, it must be expected that domestic production may grow more slowly than imports.

It is conceivable that production will pick up again in the course of 1967, but at present the Commission is taking a cautious line and estimating the growth of industrial production for the year at only about 1 %. Provided agricultural production develops normally, and when allowance is made for the fact that the contribution of the services sector will expand at any rate more vigorously than that of industry, the real gross national product may well grow by 2.5 % in 1967. This would be 1.5 percentage points less than assumed in the last Quarterly Survey. Like the authorities in Germany, the Commission has had to revise its forecasts for 1967. These forecasts had been based on certain assumptions regarding economic policy which—the crisis in domestic policy caused by these very problems having come to a head—retain at best only part of their validity. It is, moreover, always very difficult to forecast the extent and the tempo of a deceleration process in investment by enterprises, as it is in part the outcome of psychological factors which can be eliminated only by the economic and financial policy of the new Government.

Although visible imports are unlikely to expand very much faster than before, they may none the less increase in 1967, largely owing to a certain recovery in Government imports. Total imports of goods and services are even likely to grow distinctly faster than domestic production.

As a result of these trends in Germany's foreign trade, there will in 1967 be a further recovery in the trade balance (as defined for the national accounts), and the current balance of payments (including the balance of unrequited transactions) would close with its first surplus since 1964.

Despite the prospects of a better relationship between supply and demand and of a balanced situation on the labour markets, there will doubtless be for some time to come at least a tendency for prices to rise. As a result of the sluggish trend in production, unit costs must be expected to exert an upward pressure, and this may for a time gain in strength even if the rise in wages slows down; at the same time, the progress of productivity will slacken, at least temporarily, and unit costs may be forced up in some sectors where plant is working below capacity. In addition, there is the usual time-lag before changed conditions on the market influence the wage policy of both sides of industry and the price policy of managements. Finally, public utility charges and possibly indirect taxes on certain goods will be increased, as a reaction to the longer-term inflationary process and as a means of reducing the public authorities' deficits; rises in rents will also continue for some time yet.

This outlook certainly does not justify the premature return to a short-term policy aimed at general expansion. If, after an inflationary process tolerated over too long a period, prices and unit costs are to be stabilized and if serious dangers to longer-term economic growth are to be avoided some loss of growth must be accepted now. This

is not as serious as could be suggested by a formal comparison in which account is taken of earlier growth rates but no allowance is made for the fact that these high rates were reached only at the price of inflation; such a comparison also ignores the point that the current loss of growth involved belongs to a phase when economic forces are being redeployed and the pattern of the economy being modified in preparation for an early return to balanced growth that would in addition be on an adequate scale. It must, however, be pointed out that this sacrifice of growth could have been smaller if during the last economic upswing the various instruments of economic policy had not been combined in a way detrimental to economic growth.

Short-term policy must then be such that prices and unit costs are further stabilized and at the same time the conditions for growth are improved.

On the first point, the disappearance of excess demand brings to the fore the problem of controlling cost-push inflation, for experience shows that this type of inflation, continues for some time after demand-pull inflation has receded. It is clear that this control ought to be exercised mainly by applying, in close collaboration with both sides of industry, an incomes policy that should be adapted as rapidly as possible to all changes occurring in market conditions. Otherwise the upward movement of prices will continue and the risk of a recession conjured up or reinforced.

A wage policy more geared to productivity would already improve the conditions for growth, at least in relative terms. But this by itself is not sufficient. There is need for a change in the pattern of the whole of demand, and this cannot be brought about without an appropriate budget policy.

In conformity with the requirements of short-term economic policy, budget policy should be designed to ensure that the net aggregate financial deficit of all budgets is perceptibly lower than it was in 1966; this should be done either by placing a check on the expansion of public current expenditure or by taking measures to contain the growth of private consumers' expenditure, or both concurrently. This should allow for public saving, which has deteriorated seriously in the past few years, to be revised on a scale that would not only make it possible for the financial deficit to be reduced but for public investment to be increased at a satisfactory pace.

If the financing requirements of the public budgets—which in all probability will fall mainly on the capital markets—were reduced, the amount of private savings available to finance investment by enterprises would be increased. In addition credit policy could—and should—be eased distinctly as part of such a programme. At the moment there is still a very good chance that investors would take advantage of any such improvement in conditions. This would at the same time lead to increased production which would improve productivity by bringing free capacity into play and so contribute to the achievement of price stability.

It should be clear that on the broader view of this policy mix the proposal to reduce the deficits in the public budgets should not be considered as “pro-cyclical” in the

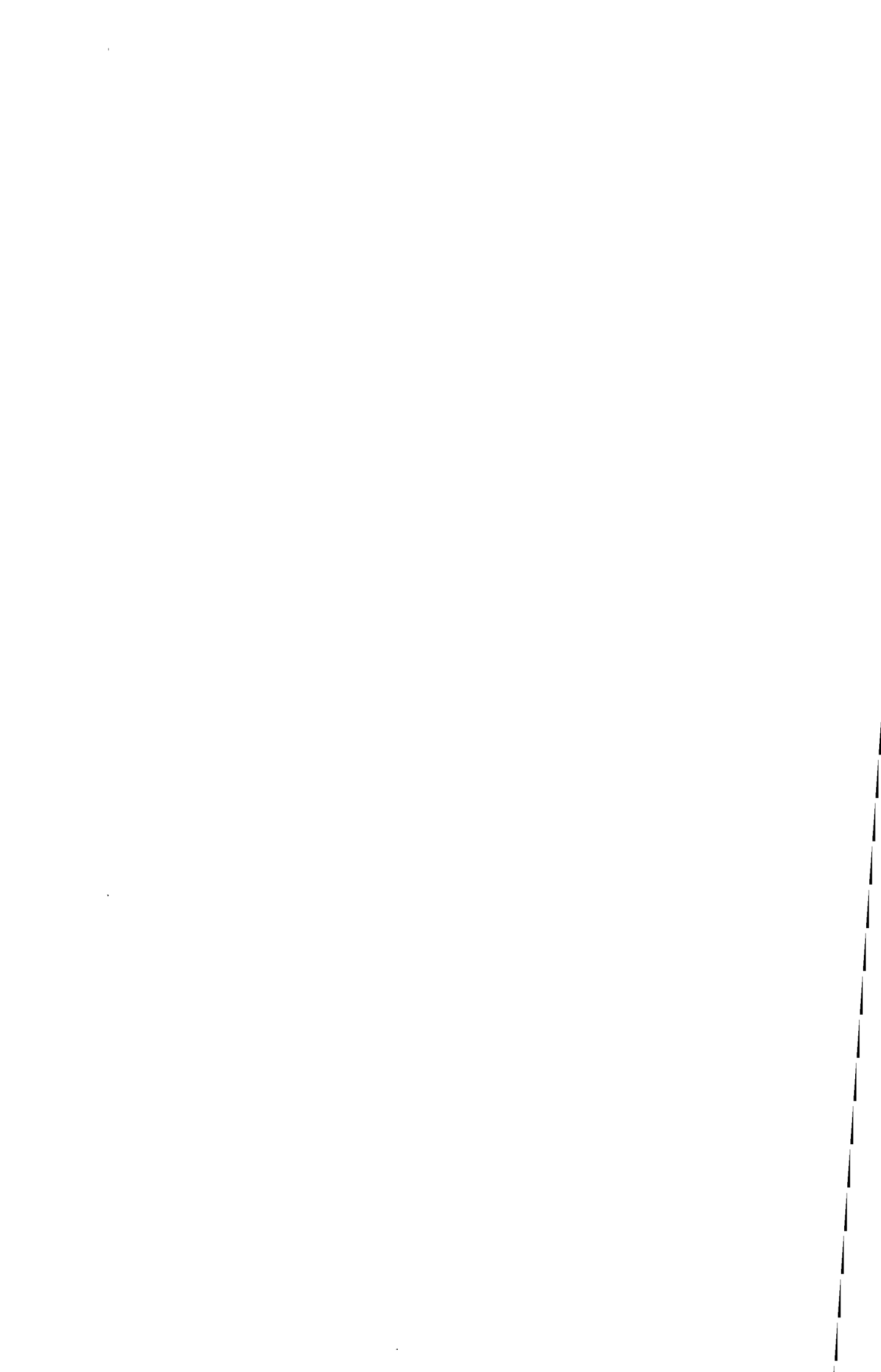
sense that it would further strengthen the slowdown of demand. It would have to be *ex ante* in character and be based on the assumption that gross national product will attain a certain rate of growth (say 5 %) in money terms. If a business setback threatened to compromise this rate seriously, the budget would have to play its role of automatic stabilizer—in other words any shortfall in receipts from taxation resulting from such a reduction ought not to be offset by a fresh cut in spending or by additional taxation. In these circumstances, with the deficit revealing a further deterioration in the economic situation, it would be possible and advisable to finance out of bank liquidity the part of the deficit due to the recession.

These suggestions on the general lines that should be followed in short-term economic policy are fully consonant with the gradual relaxation of certain restrictions on credit policy pending the measures expected in the field of public finance. One example of such relaxation is the decision not to maintain the time limit on the reduction in the minimum reserve ratios which was made in order to ease the seasonal pressures that occur at the end of the year.

By and large such a policy could—if the various elements are properly mixed—be sufficient to prevent any further weakening in the propensity to invest and later to help boost it again. However, if budgets are not very soon placed on a sound footing or if this aim is even abandoned completely, credit policy would sooner or later have to switch back to definitely expansionary lines in order to avoid a genuine recession and severe unemployment. This being so, it would also be advisable to carry out new public investment schemes, possibly financed by short-term borrowing. It can, however, already be predicted that in the latter case the next upswing of economic activity would very soon produce problems similar to the ones which prevailed from 1963 to 1965 and continued into the first half of 1966: a rapid increase in costs and prices, balance of payments deficits and, this time, the additional possibility of a lasting deterioration in Germany's ability to compete and consequently in the outlook for longer-term economic growth.

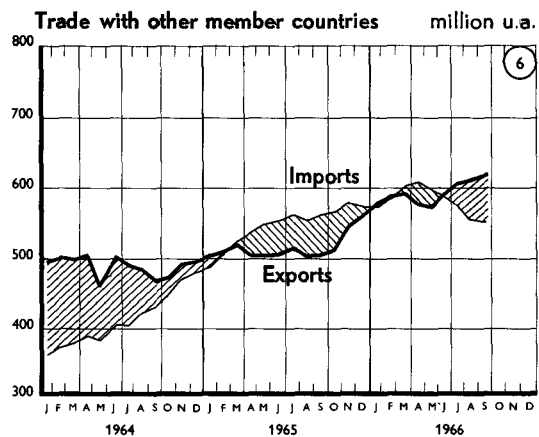
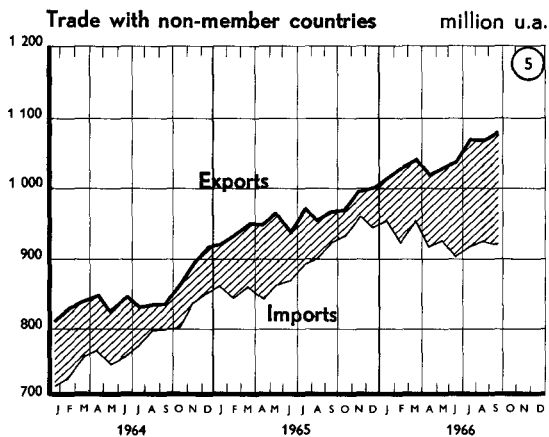
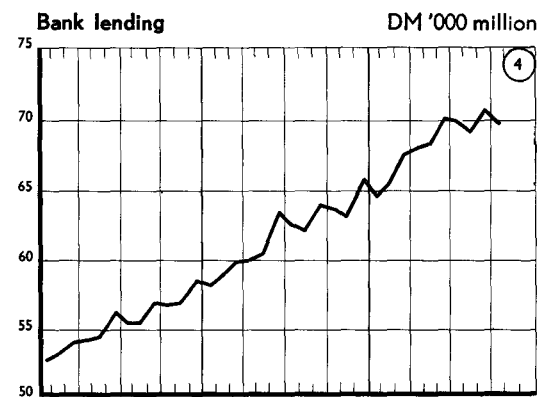
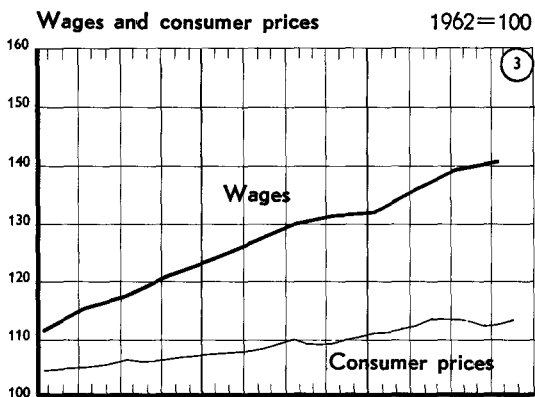
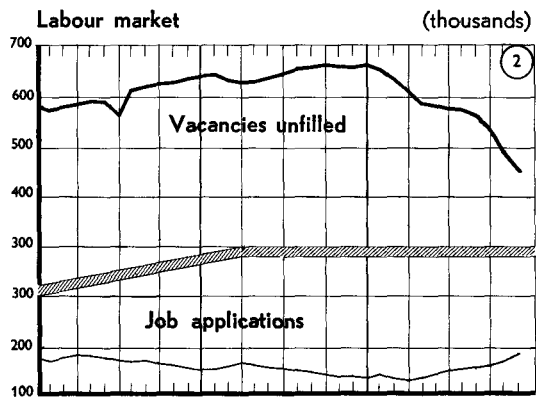
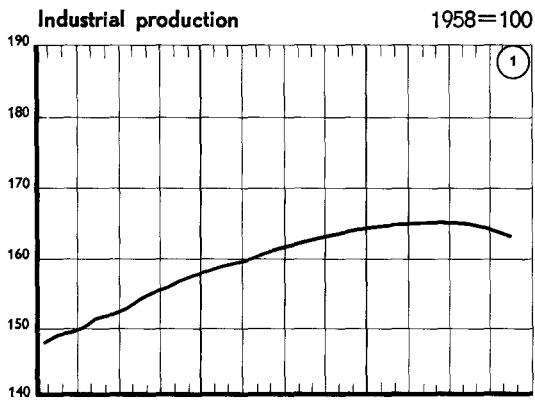
Note :

Since the Fourth Quarterly Survey is essentially a report on the whole year and is largely based on national accounts which include West Berlin, no special sections has been devoted to the economic situation in West Berlin. This follows the practice pursued in previous years. In the first three Quarterly Surveys of 1967 there will again be a section on West Berlin.



Federal Republic of Germany

ECONOMIC INDICATORS



NOTES:

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

Graph 1. Trend curve; estimation established on the basis of indices adjusted by the SOEC for seasonal and fortuitous variations (excluding construction, food, beverages and tobacco).

Graph 2. Series seasonally adjusted. Moving averages of 3 months.

Graph 3. Source: Statistisches Bundesamt. Cost-of-living index at middle of month; index of average hourly gross earnings in industry (including construction).

Graph 4. Short-term loans to business and private customers within the country.

Graphs 5 and 6. Series adjusted for seasonal and accidental variations (moving averages of 3 months). Exports fob, imports cif. Conversion at official exchange rates.

Federal Republic of Germany

TABLE 1: Basic data (1965)

Total area ('000 sq. km.)	248.5
Total population ('000)	59 012
Density of population per sq. km.	238
Working population ('000)	27 153
Working population, breakdown by main sector (%)	
— Agriculture	10.9
— Industry	48.7
of which : Construction	8.2
— Services	40.4
Percentage share of gross domestic product	
— Agriculture	5.9
— Industry	50.9
of which: Construction	8.2
— Services	43.2
Gross product per capita (DM)	7 605

**TABLE 2: Some elements of national product and expenditure
(annual rates of growth)**

	% change by volume on preceding year						Volume indices (1958 = 100)	Contri- bution (in %) to GNP
	1960	1961	1962	1963	1964	1965	1965	1965
Gross national product	8.8	5.4	4.2	3.3	6.6	4.6	147	—
Industrial production	10.7	6.3	4.5	2.7	8.5	5.7	157	—
Total imports	16.9	8.1	11.4	8.0	10.7	14.3	225	20.5
Private consumers' expenditure	6.9	6.8	5.9	2.9	5.3	6.3	147	56.9
Public current expenditure on goods and services	7.6	7.8	11.5	7.5	— 0.1	6.4	161	15.6
Gross fixed asset formation	11.3	9.4	5.9	2.9	11.8	6.5	178	26.5
Total exports	13.0	3.5	3.9	9.0	9.6	6.6	174	20.3
Gross national product per capita	7.7	4.0	2.8	2.2	5.3	3.3	135	—
Gross national product per person gainfully employed	7.0	4.0	3.4	3.0	6.2	3.9	139	—

Federal Republic of Germany

TABLE 3: Foreign trade (at current prices)

	% change on preceding year							Indices 1958 = 100	Million u.a.	% of the total
	1959	1960	1961	1962	1963	1964	1965			
Visible exports										
Total	11.3	16.4	11.1	4.5	10.2	10.9	10.3	203	17 892	100
Intra-EEC	13.5	23.3	19.6	20.9	20.8	8.4	6.7	262	6 306	35.2
To non-EEC countries	10.5	13.8	7.6	1.0	4.7	12.5	12.4	181	11 586	64.8
Exports of food, beverages and tobacco										
Total	11.2	9.3	4.3	7.3	16.0	20.5	25.0	238	435	2.4
Intra-EEC	13.7	10.2	1.0	8.1	23.9	22.1	22.6	254	166	0.9
To non-EEC countries	9.8	8.8	6.8	6.9	11.5	19.5	26.6	229	269	1.5
Exports of raw materials and manufactures										
Total	11.3	16.6	11.3	4.5	10.1	10.8	10.0	202	17 458	97.6
Intra-EEC	13.5	23.6	20.1	12.2	20.8	8.1	6.3	262	6 140	34.3
To non-EEC countries	10.5	13.9	7.6	0.9	4.6	12.3	12.1	180	11 318	63.3
Visible imports										
Total	15.2	19.2	8.3	12.2	6.0	12.2	19.6	237	17 472	100
Intra-EEC	29.8	22.9	13.3	16.6	8.7	17.4	30.7	351	6 660	38.1
From non-EEC countries	10.1	17.7	6.1	10.3	4.7	9.7	13.6	198	10 812	61.9
Imports of food, beverages and tobacco										
Total	15.2	4.1	7.9	20.1	- 8.3	8.3	21.6	188	3 651	20.9
Intra-EEC	25.2	13.9	15.3	15.9	- 0.0	9.3	28.0	268	1 349	7.7
From non-EEC countries	11.7	0.3	4.4	22.2	-12.2	7.8	18.1	160	2 302	13.2
Imports of raw materials and manufactures										
Total	15.1	24.6	8.4	9.9	10.7	13.3	19.0	255	13 821	79.1
Intra-EEC	31.4	26.0	12.5	16.3	11.5	19.7	31.3	381	5 311	30.4
From non-EEC countries	9.5	24.0	6.7	6.8	10.3	10.2	12.5	211	8 510	48.7

TABLE 4: Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.	
Industrial production (1958 = 100)	1964	134	141	148	148	158	151	142	137	153	159	166	155	
	1965	150	152	152	163	164	162	147	143	162	167	171	158	
	1966	151	156	162	168	167	168	153	144	162	166	169		
Total orders received (1958 = 100)	1964	160	164	171	185	165	178	177	154	181	192	185	179	
	1965	166	173	198	190	188	182	180	165	197	200	196	188	
	1966	173	178	216	193	193	188	176	170	192	193			
of which:														
	home orders	1964	153	158	168	182	163	174	177	153	179	190	181	172
		1965	161	167	193	188	185	173	176	164	196	193	192	177
1966		163	170	208	186	185	178	169	161	184	181			
foreign orders	1964	190	193	187	200	176	193	178	156	190	203	203	206	
	1965	187	195	222	199	201	200	198	173	206	210	214	233	
	1966	211	213	250	227	230	234	207	208	232	251			
Building: number of permits issued (DM '000 million)	1964	2.49	2.58	2.89	3.34	3.32	3.62	3.82	3.87	3.72	4.01	3.55	3.51	
	1965	2.88	2.61	3.25	3.61	4.04	3.85	4.45	4.39	4.27	4.17	3.81	3.77	
	1966	2.95	2.97	4.00	3.75	3.85	4.03	4.15	4.03	4.04	4.13			
Private consumers' expenditure: Retail turnover (1958 = 100)	1964	126	122	143	147	142	137	149	131	139	167	168	223	
	1965	134	129	154	170	156	150	167	143	155	179	195	241	
	1966	144	142	173	176	171	157	171	154	162	183			
Total visible imports (million u.a.)	1964	1 078	1 058	1 158	1 231	1 097	1 233	1 311	1 141	1 246	1 370	1 368	1 419	
	1965	1 331	1 247	1 492	1 396	1 479	1 484	1 509	1 375	1 542	1 566	1 584	1 606	
	1966	1 446	1 397	1 635	1 476	1 541	1 544	1 478	1 449	1 482	1 607	1 530		
Total visible exports (million u.a.)	1964	1 240	1 289	1 362	1 423	1 281	1 350	1 368	1 172	1 329	1 487	1 390	1 538	
	1965	1 364	1 353	1 627	1 397	1 544	1 407	1 535	1 297	1 481	1 583	1 557	1 768	
	1966	1 492	1 490	1 757	1 559	1 701	1 645	1 708	1 537	1 727	1 809	1 719		
Balance of trade (million u.a.)	1964	+ 162	+ 231	+ 204	+ 192	+ 184	+ 117	+ 57	+ 31	+ 83	+ 118	+ 22	+ 118	
	1965	+ 33	+ 106	+ 135	+ 1	+ 65	- 77	+ 26	- 77	- 62	+ 17	- 27	+ 162	
	1966	+ 46	+ 93	+ 72	+ 83	+ 160	+ 101	+ 230	+ 88	+ 246	+ 201	+ 189		
Official gold and foreign exchange reserves (million u.a.)	1964	7 012	7 206	7 114	6 968	6 921	7 153	7 049	7 024	7 059	7 052	6 944	6 969	
	1965	6 604	6 702	6 860	6 825	6 486	6 393	6 295	6 211	6 303	6 335	6 354	6 352	
	1966	6 190	6 139	6 150	6 072	5 974	6 193	6 441	6 433	6 454	6 616	6 652		
Money supply (DM '000 million)	1964	63.5	64.2	64.3	65.3	66.7	67.7	67.8	68.7	68.4	69.0	71.5	72.9	
	1965	69.4	70.4	70.1	71.4	73.3	74.0	74.1	74.2	74.2	75.1	77.5	78.4	
	1966	74.0	74.5	74.2	75.9	76.9	77.7	77.7	77.3	76.7	76.5			

Federal Republic of Germany

NOTES

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

Table 1

- Total population. Yearly average (estimate).
- Working population in employment. Yearly average. Source : Statistisches Bundesamt.
- Breakdown of gross domestic product at factor cost. (1964 figures.)

Table 2

- GNP in 1958 prices.
- Industrial production : value added at market prices.
- Total exports and imports : goods, services and factor income.

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 and manufactures (groups 2-9 CST).

Table 4

- Industrial production. Source : Statistisches Bundesamt. All industries, including construction, adjusted for varying length of months.
- New orders. Source : Statistisches Bundesamt. Value index manufacturing industry (excluding food).
- Construction. Source : Statistisches Bundesamt. Building permits, estimates of construction costs (excluding civil engineering).
- Private consumption. Source : Statistisches Bundesamt. Index of value of retail trade turnover.
- Exports fob, imports cif. Conversion at official exchange rates. Source : Statistisches Bundesamt.
- Official gold and foreign exchange reserves. Bundesbank's gross reserves of gold and convertible currency at end of month.
- Money supply. Notes and coin circulation, excluding cash holdings of credit institutions. Sight deposits of non-banks and of private residents (excluding public authorities' deposits with the Bundesbank). End-of-month figures.

B. France

The balance-sheet of the French economy for 1966 is on the whole very favourable. The rise in business activity continued; production, employment and incomes increased much more vigorously than a year before. The main stimulus was provided by an expansion of domestic demand, which gathered increasing momentum, chiefly because investment expenditure in the private sector was recovering after a year of rather hesitant growth, and also because expenditure by the public authorities was at times growing distinctly faster than a year earlier.

Economic activity, as measured by the increase in the real gross national product, was 5.5 % higher than in 1965, and continued to be fairly free from new difficulties. In the course of the year, however, developments in the business situation led to a slight upward trend in prices and a gradual reduction in the external surplus.

These tendencies may become more marked in 1967, since demand can be expected to go on increasing at a brisk pace—there may even be some slight acceleration—while the elasticity of domestic supply may decline. Utilization of technical capacity will rise, and on the labour market it will be increasingly difficult to find manpower with the right skills in the right places. The gross national product is nevertheless expected to increase by a further 5.5 % in 1967.

Any increased pressure on resources would inevitably be a serious threat to the achievement of balanced economic growth. Those responsible for policy must therefore seek to keep the expansion of domestic demand in money terms under control and at the same time to increase the elasticity of markets and the efficiency of the financing machinery by improving their structure.

1. Balance-sheet for 1966

By the end of 1966 business activity in France will be considerably higher than in the previous year. The economic advance, which gathered momentum again in the spring of 1965 after easing for a period, has continued and gained increasingly in depth.

The growth of exports was particularly strong at the beginning of the year and in early spring, though later in the year there was a marked slowdown as a result of an appreciable decrease in demand from important purchasing countries, particularly the Federal Republic of Germany, where business activity was slackening. At times exports to other Community countries even fell in absolute terms, and this was not fully offset by the more rapid expansion of exports to non-member countries, particularly those in Asia, Latin America and the European countries of the Eastern bloc.

Nevertheless, the value of visible exports for the full year 1966 should, to judge by customs returns, have risen 10 % (in 1965 the rise was 11.8 %). Since exports of services also increased considerably, the rate of increase for exports of goods and services combined (as defined for the national accounts, i.e. including factor income from abroad) will have been only slightly lower than that registered in 1965 (about 9.5 % by value, compared with 11.6 %). In view of the fact that appreciably higher prices were received for exports, the slackening of growth is more marked in the figure for total exports by volume (8 %, as compared with 10.9 % last year).

Internal demand, on the other hand, gained in strength as the year wore on. Here the rapid recovery in the propensity to invest of enterprises was undoubtedly the decisive factor.

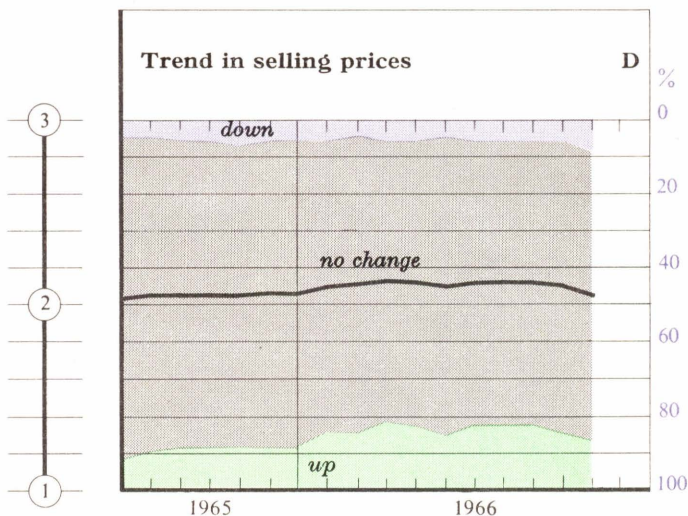
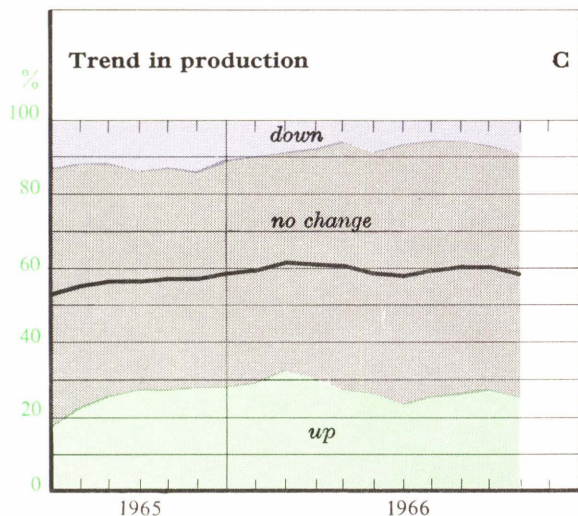
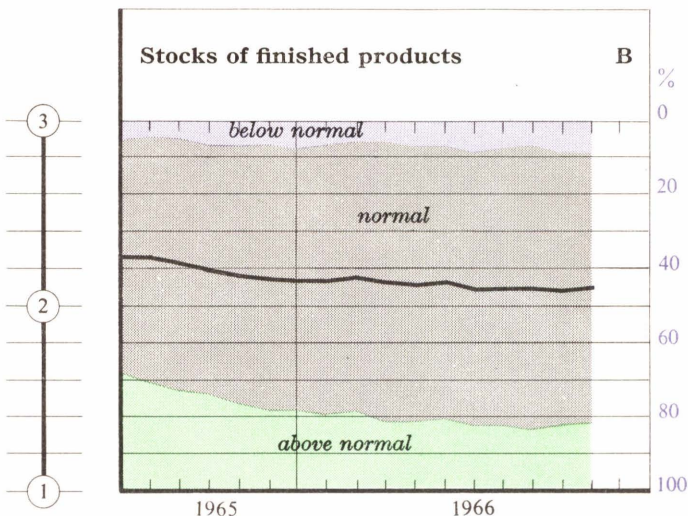
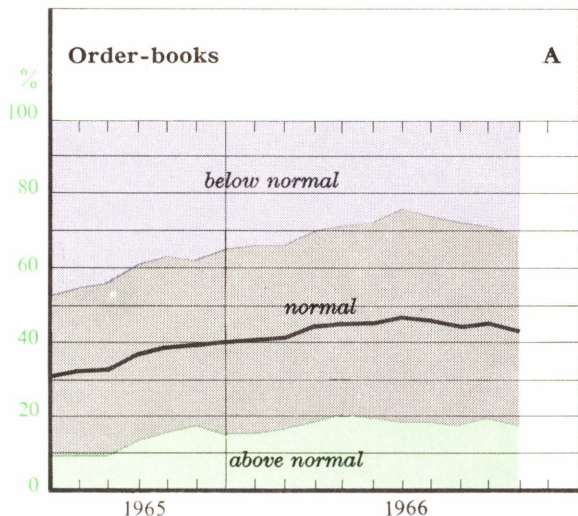
Private industry stepped up its gross fixed asset formation considerably in view of the increasingly full use being made of capacity and of the recovery occurring in the profits situation, and also because confidence was growing that the new advance in business activity would last a long while. An additional incentive was given by the introduction in February of a 10 % tax credit on the purchase of plant and machinery. For the full year productive investment by enterprises is likely to be at least 9.5 % in value (and approximately 7 % by volume) higher than in 1965, when it had been 4 % (and 2 %) higher than in the preceding year. Government investment expenditure continued its strong upward trend with an increase of almost 13 %. Investment in housing, however, slowed down sharply during the year. Delays that occurred at times in giving approval for housing financed from public funds, certain changes in the methods of financing, and a growing amount of completed but unsold dwellings in the privately financed sector kept the volume of new building projects well below the level reached in the previous year. All in all, the increase in gross fixed asset formation may prove to have been somewhat greater in 1966 than in 1965, rising to about 9 % (as compared with 8.4 %) at current prices or about 6 % (as compared with 5.3 %) at constant prices.

Stockbuilding also increased perceptibly during 1966, in response to the growing volume of production and the considerable expansion of final demand. This increase alone accounted for almost one percentage point in the growth of the gross national product in 1966.

Expenditure on consumption also increased the pull it exerts on production, though to a lesser extent than expenditure on investment. Public current expenditure on goods and services, especially outlay for wages and salaries in the public sector, rose more sharply than in 1965, because although there was little change in the modest increase of wage and salary rates (some 4 % per annum), a rise in the numbers employed particularly, in education, meant that outlay under this heading rose appreciably faster than in 1965. All told, the increase in public current expenditure should amount to some 8 % at current prices (4.8 % in 1965) or 4.5 % at constant prices (2.3 % in 1965).

Consumption by households increased at a slightly faster tempo as the year advanced, owing primarily to a marked increase in the rate at which incomes were expand-

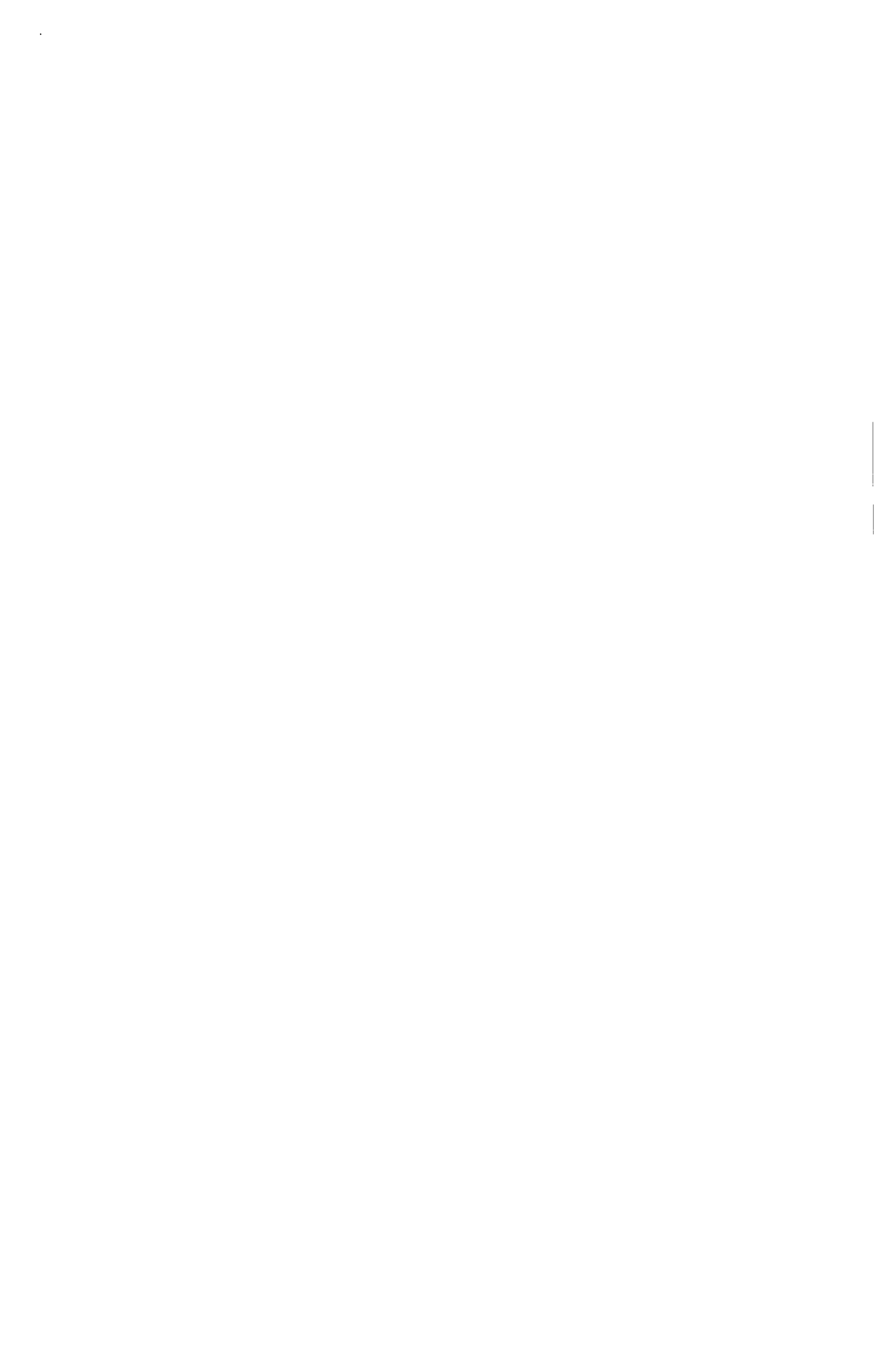
BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

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



ing. Incomes from wages and salaries rose more than in 1965 (about 8.5 %, against a bare 7 %). The increases in wage and salary rates were not much larger than before, but the total number of hours worked, which had been practically unchanged in 1965, increased substantially as a result of a lengthening in average hours per week and, from spring onwards, because of some expansion in numbers employed. At the same time, transfer incomes increased by at least as much as between 1964 and 1965 (9.5 %). Incomes of households derived from self-employment and property rose more sharply as a result of the general increase in business activity. The fact that gross incomes had to support a relatively lighter burden of direct taxation and of deductions for social services and that the savings ratio was slightly down on the previous year gave private consumption an additional impulse which should amount to a good 8 % in money terms or 5 % in real terms, compared with corresponding increases of 5.9 % and 3.2 % in 1965.

On the whole, supply showed a fair degree of elasticity in response to this rapid growth in demand.

Industrial production grew steadily during the year at almost the same rate as at the beginning of this new period of expansion—almost 2 % from quarter to quarter, according to the seasonally adjusted INSEE index (which excludes construction). The growth for the year may well turn out to be some 7.5 %, as against a mere 1.4 % in 1965. The building industry had a less satisfactory record during 1966, due to the fairly appreciable weakening of effective demand for new housing. However, the rapidly increasing demand from the public authorities and business meant that according to the INSEE index, output in this industry was some 5 % up—that is to say, virtually the same increase as in 1965 (5.6 %).

Agricultural production on the other hand is not likely to have risen much above the exceptionally high level of the previous year. While livestock production is up considerably on 1965, harvests have been much smaller owing to reduced acreage and unfavourable weather conditions.

Nevertheless the gross national product, which increased by 3.4 % from 1964 to 1965, may be up 5.5 % in 1966; here the sharp rise in net value added in the services sector was one factor of some significance.

This rather rapid growth of economic activity in general was made possible by a slightly more rapid increase in productivity (defined as the increase in real gross national product per man hour worked) and a distinct increase in the total number of hours worked; in the course of the year there was a perceptible rise in the demand for additional manpower, particularly from industry. Although on the whole the situation on the labour market was still fairly easy—the number of workers seeking employment showed a further slight tendency to grow—signs of strain were already recurring here and there. It is evident that the increased supply of manpower, due mainly to the high birth-rates of the post-war years, but in part also to the number of immigrants in 1966 having been considerably higher than in 1965, does not fully correspond to the particular requirements of either the various regions or of the various industries.

Domestic supply in 1966 was supplemented to a considerable extent by supplies from abroad. Imports of goods, which in the second half of 1965 had been pushed to an exceptionally high level because of the need to replenish stocks, continued to rise with practically unabated vigour in the months that followed; their total volume for the year may be estimated (on the basis of customs returns) to have been no less than 13.5 % higher than in 1965, after having risen as little as 0.8 % between 1964 and 1965. Moreover, imports of services grew considerably in 1966, so that total imports of goods and services (as defined for the national accounts) should show an increase of some 12 % in real terms and approximately 13.5 % in money terms (as against 3.6 % and 4.0 % in 1965).

The high elasticity of supply and a trend in costs which benefited from greatly improved productivity coupled with wage increases which were still fairly modest ensured that till well into the year prices remained relatively stable despite the rapid expansion of demand; in addition, the policy of direct price control was retained in principle, and was relaxed only for certain industrial products under "stability agreements"⁽¹⁾ or "programme agreements"⁽²⁾. Evidently, however, the phase of progressive stabilization of general price levels came to an end in autumn 1965 and has given way since spring 1966 to a slightly more pronounced upward movement. During the year the business situation gave rise to a slight tendency for prices to edge upwards, principally in clothing, consumer durables and personal services, and this tendency was reinforced by increases in the rates charged for public services. In addition, the rise in the price of certain agricultural commodities had a limited impact: for the year, average prices of goods and services for private consumption will probably have risen 3 % (against 2.6 % in 1965).

Since the spring of 1966 there has been a distinct deterioration in the balance on goods and services. In terms of national accounts, the surplus of 4 400 million recorded in 1965 may well have shrunk to below FF 2 500 million in 1966.

Since this contraction occurred mainly in trade with countries outside the franc area, the surplus on current account of the balance of payments was appreciably reduced. At the same time the surplus on capital account fell, because on balance the inflow of private capital was far smaller than in 1965—in part, no doubt, owing to the different rates of interest ruling abroad—and despite the fact that net official exports of capital were considerably lower than in the previous year. Official gold and foreign exchange reserves (gross) ceased to rise in the course of the year; in fact, there was even a slight contraction in the autumn, the first experienced for many years if exceptional transactions are left out of account. Total reserves including the change in net claims on the International Monetary Fund increased by only FF 2 200 million in the first eleven months of 1966, in comparison with a good FF 3 000 million increase in the corresponding period

(1) One-year agreements allowing enterprises and groups of enterprises to adjust the price of individual products in return for an undertaking not to exceed the previous average price of all the products manufactured by them.

(2) Five-year agreements under which enterprises or groups of enterprises are free to fix their own prices in return for certain undertakings on wages, investment exports, etc.

of 1965. In addition, the change in the net foreign exchange position of the commercial banks was on balance much less favourable than in the previous year.

Demand for and supply of goods and services

	1964 ⁽¹⁾	1965 ⁽¹⁾		1966 ⁽²⁾		1967 ⁽³⁾
	At current prices (in FF '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports ⁽⁴⁾	62.7	+ 10.9	+ 11.6	+ 8	+ 9.5	+ 6.5
Gross fixed asset formation	92.3	+ 5.3	+ 8.4	+ 6	+ 9	+ 7.5
Public current expenditure on goods and services	58.7	+ 2.3	+ 4.8	+ 4.5	+ 8	+ 5.5
Private consumers' expenditure	278.1	+ 3.2	+ 5.9	+ 5	+ 8	+ 5.5
Gross national product	435.2	+ 3.4	+ 6.0	+ 5.5	+ 8.5	+ 5.5
Imports ⁽⁴⁾	63.1	+ 3.6	+ 4.0	+ 12	+ 13.5	+ 10.5

⁽¹⁾ *Rapport sur les Comptes de la Nation de l'année 1965*, Ministère de l'Économie et des Finances, Paris.

⁽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.

Although the effect of external transactions on internal liquidity weakened appreciably during the year and faded entirely in the autumn months, internal liquidity maintained, and at times more than maintained its previous growth rate. Treasury operations will on balance have had a strongly expansionary effect; to take only one element, the execution of the national budget in the first nine months of the year led, because of a more rapid rise in expenditure, to a cash deficit ⁽¹⁾ of FF 3 100 million, against barely FF 1 200 for the corresponding period last year. By the end of 1966 it will presumably have been possible to reduce this deficit a little, but on balance the budget ⁽¹⁾ is unlikely to close, as it did in 1965, with a slight surplus of income, but with a quite

⁽¹⁾ Excluding repayment of debts.

considerable deficit of some FF 2 000 or 3 000 million. In addition, lending by the banks to business customers contributed considerably more to liquidity than in 1965; the amount of outstanding credit increased by almost FF 8 300 million (6.3 %) between the end of December 1965 and the end of September 1966—as compared with a mere FF 4 500 million (3.8 %) in the same period last year.

The money market was under pressure for almost the entire year. Call money rates rose appreciably despite massive intervention at times by the Central Bank and very flexible application of the regulations on minimum reserves. There was a clear upward trend in interest rates on the capital market too, due in part to the marked discrepancy between domestic interest rates and those ruling on foreign markets. A certain reluctance on the part of investors was apparent in sales of shares, while more fixed-interest securities were issued than in 1965 without undue difficulty (but only at higher rates of interest), mainly by the public authorities and by savings institutions under public law.

2. Outlook for 1967

At the moment all indicators and information regarding future developments point to the fact that the rise in business activity will continue in 1967; certain strains between the growth of demand and domestic resources could however become more evident, and the movement towards a more pronounced increase in prices that is already apparent could become more marked. The deterioration in the balance of payments will continue.

Domestic demand may well account for a larger part of expansion than has been the case so far. The prospects for increased demand from abroad are less promising at the moment owing to the persistent tendency for business activity to flatten out in some major purchasing countries. In the first half of 1967 at least, exports to other Community countries will be appreciably hampered by dampening influences. Despite this, the value of visible exports for the full year 1967 can be expected to increase by about 8.5 %; since the competitiveness of French industry is still high and improved financing facilities have been made available through extension of the export credit system the rapid expansion of sales to other parts of the world should continue, especially as the demand for imports from this quarter may continue to expand vigorously.

The effects which the slight slackening in the growth of demand from abroad will exert on production and employment should be at least offset by the higher rate at which domestic demand is likely to expand.

Gross fixed asset formation in particular is likely to rise more rapidly in the course of 1967 than in 1966, and its total growth for the year will also be greater; much of the advance will be due to investment by enterprises in construction and in plant and machinery. Rising sales and fuller utilization of capacity combined with growing profits and a

margin for self-financing which, as the stockbuilding programme drew to a close, is increasingly available for fixed asset formation, have led managements in the private sector to revise their investment plans upwards. This revision will probably lead to particularly large increases in expenditure on plant and machinery, as most of the orders placed before the end of 1966 (with an eye to the 10 % tax concession) will be filled during 1967. Furthermore, both the public enterprises and the central government have very extensive investment programmes; they expect to increase their expenditure by 9.5 % and 13.5 % respectively. Finally, there may well be a revival of activity in the housing sector in 1967 once certain administrative delays have been overcome and financing becomes easier as a result of a system of saving for building purposes introduced in 1966 and of the establishment of a mortgage bond market.

It has already been pointed out with regard to stockbuilding that stocks in industry—and probably in commerce also—have by now returned in most cases to their “normal” level; it seems likely therefore that in 1967 stocks will on the whole be increased only where this is necessary in order to meet the demands of current production and sales. Given normal harvests, stocks in agriculture should however increase much more vigorously than in 1966.

There should be a further slight acceleration of consumer expenditure in 1967. Even if there is no overstepping of the budgetary estimates—and this would imply a far more strict control of expenditure than was exercised in the past year—somewhat higher increases can be expected for public current expenditure on goods and services in 1967. In view of the probable development of incomes, a more lively expansion can be forecast for private consumption too.

Incomes from wages and salaries should show a more vigorous increase, principally because the total number of hours worked will rise faster than before, but also because wage and salary rates may be expected to react more distinctly to the increased demand for additional manpower. Furthermore transfer incomes will increase more than in 1966 as a result of social policy measures already introduced or planned. Finally, an increased expansion in personal incomes from self-employment and property may be expected, since agricultural incomes in particular may benefit appreciably from better harvests and higher prices and since the upward movement of interest rates noted in 1966 and the reform of the tax treatment of dividends adopted in 1965 should produce their full effect for the first time in 1967.

A further steady growth in domestic production can be expected to result from these developments among the several elements of demand. The pace of growth should, by and large, be much the same as in 1966, but the contribution made by each sector will vary depending as it does on the pattern of demand and the reserves of capacity available. There may for instance be a progressive slackening in the growth of industrial production as the year advances; more because of limitations imposed in certain fields by lack of technical capacity than by shortage of manpower. This will result in a greater backlog of orders and longer delivery dates. On the other hand, building output may increase appreciably more rapidly than in 1966. There may well be an acceleration of

demand for industrial building as firms find it more and more necessary to invest in expansion, and the demand for housing, which was decidedly poor in 1966, may be expected gradually to exert a greater influence on output once again.

The growth of industrial production may therefore be expected to be somewhat slower in 1967 than in 1966 (6.5 % against 7.5 %), the growth of building output a little faster (6 % against 5 %). Given normal weather conditions for agricultural production, and assuming that the services sector maintains its strong upward trend, a further 5.5 % increase in real gross national product can be forecast for 1967.

Growth at such a pace presupposes an accelerated rise in the total number of hours worked, since improvements in productivity (defined as increase in real gross national product per man hour worked) may tend if anything to tail off as the pressure on production capacity increases. Such a rise is not impossible. There is little scope for further lengthening of the working week; but the number of workers could increase more than in 1966. At the same time it must be pointed out that because of the frequent lack of training and the difficulty of getting available reserves of manpower to move from one area to another, this increase can probably be achieved only at the cost of greater tightness on the labour market.

In view of the possibly accelerated growth of overall demand in money terms and the tendency for domestic industrial production to become if anything less elastic, the vigorous demand for imports may be expected to continue. Foreign suppliers should be the better able to meet this demand because of the slowing of business activity in important industrial countries, especially in the Federal Republic of Germany; this will have left more capacity free to produce for export. Imports of finished industrial goods could therefore increase further. Even if at the same time imports of raw materials fall as stockbuilding comes gradually to an end, a 12 % increase in the total volume of visible imports can be expected for the year, almost as much as in 1966 (13.5 %).

In these circumstances, and even if it is assumed that the terms of trade continue to develop in favour of French industry, a continuous and fairly pronounced deterioration in the balance of trade can be expected. The external surplus (as defined for the national accounts) could be appreciably reduced and may even swing into deficit.

Despite this a fresh and rather more rapid increase may occur in the levels of prices. Entrepreneurs may well, in face of the lively growth in demand and the need to finance a growing volume of investment, be tempted not merely to pass on in the form of higher prices the higher costs attributable in the main to a heavier burden of wages and social charges, but also to widen their profit margins. Furthermore, structural factors are helping to push prices up in the services sector, quite apart from the fact that rates for public services are to be further increased and that rents are in any case climbing steadily. It can therefore be forecast that in 1967 the increase in price levels—based on prices of goods and services for private consumption—will be more than 3 % and may come close to 3.5 %, as compared with 3 % in 1966 and 2.6 % in 1965. Such a rate of increase—especially if it continues for any length of time—can hardly be reconciled with

the aim of balanced economic growth. The Fifth Plan in fact allowed for a mere 1.5 % price increase per year.

In these circumstances it would be advisable if short-term economic policy were such that the rise in prices were better contained and an appropriate measure of balanced economic growth ensured.

It is doubtful whether price policy measures such as the extension of direct price control to the services sector can provide a solution to this problem. Indeed it would seem preferable to return as quickly as possible to free price formation in the services sector. So far the danger of massive price increases is remote, and such a move would have the advantage of allowing the gross savings effected by enterprises to be better distributed between the various sectors.

To ensure that the supply of funds is sufficient and that they are correctly distributed will be one of the most important problems in 1967. Steps should be taken to facilitate a non-inflationary financing of the investments planned by industry which would appreciably increase the possibility of expanding production in the years ahead; these should include the possibility of covering a reasonable proportion of investments from subscribed capital and reserves. Furthermore, the amount of loan capital available should be increased by measures to promote saving by households and to improve the efficiency of the capital market, and available capital should be channelled to a greater extent towards productive investments.

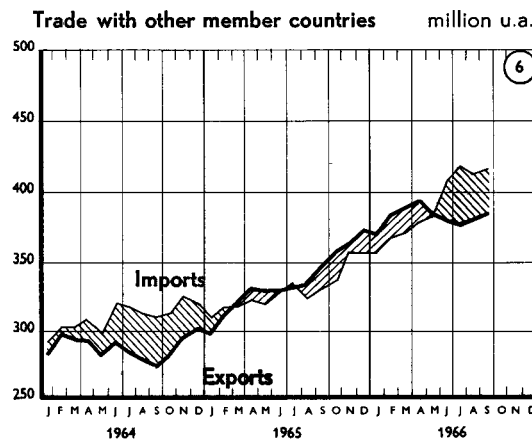
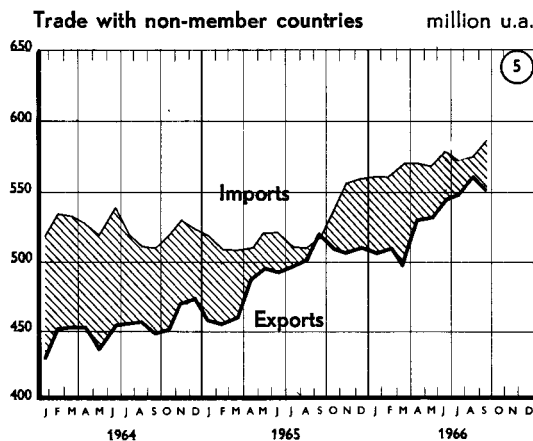
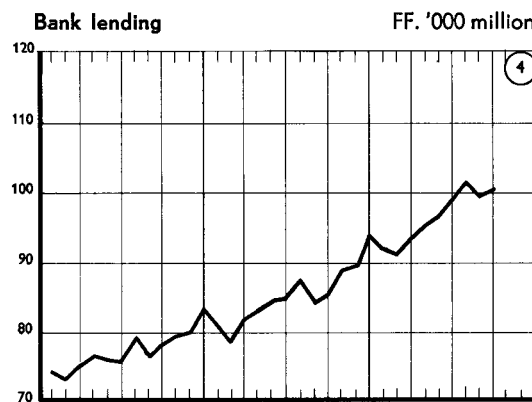
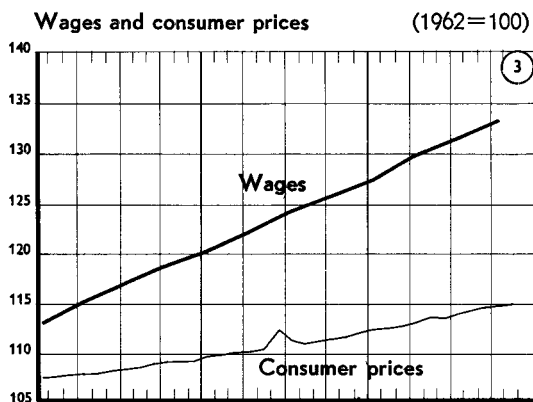
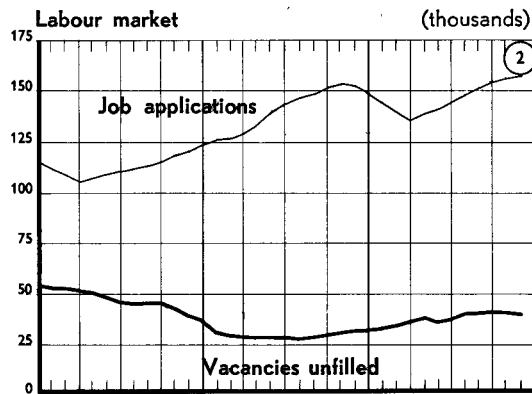
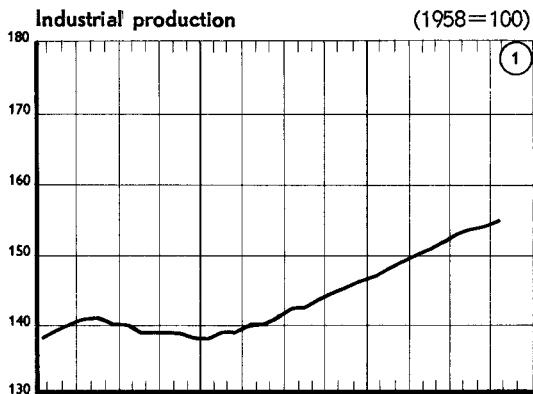
In this connection it is disturbing to note that the official forecasts for 1967 presented to Parliament with the Finance Act show that the income and expenditure of the public authorities, which showed a financial surplus in 1965 and balanced in 1966, will show a financial deficit of FF 1 500 million in 1967, and that the public authorities will be making corresponding calls on the savings of the other sectors of the economy.

A budget which did less than the present proposals to step up expenditures that contribute directly or indirectly to the growth of consumption would not only be of general assistance in containing the rise in prices but would leave more savings available for financing investment by enterprises. This in turn would slow down the growth of bank borrowing by enterprises and would make it that much easier for the monetary authorities to keep credit policy relatively flexible and interest rates relatively low. The monetary authorities cannot, in a period of strong economic expansion with a high rate of utilization of the factors of production, use credit expansion as an alternative to savings without inflationary tendencies sooner or later affecting costs and prices, perhaps even the external balance. Such a development would bring a speedy return to restrictive measures which would affect in particular the supply of credit and so have an injurious effect on the trend of productive investment by enterprises.

The support of short-term economic policy by an active structural policy which could permanently improve the elasticity of the economy seems more necessary in 1967 than ever before. During 1966 the Government has already implemented or laid the

foundations for a number of measures on these lines : there is the draft for a law on vocational training, to increase the supply of trained workers; the draft of a law on real estate, primarily intended to ensure the financing of local authority investments; regulations on the reform of banking and credit, which should ensure that the unduly large funds invested short-term can be channelled into long-term investment; and action to establish a mortgage bond market. Other measures would deal with the reform of the system of aids for industrial decentralization; increased export promotion and removal of the remaining restrictions on imports; and a fairly far-reaching liberalization of capital movements. An early and effective implementation of these various measures could help to create more favourable conditions for a balanced growth of the economy.

ECONOMIC INDICATORS



NOTES:

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

Graph 1. Trend curve; estimation established on the basis of indices adjusted by the SOEC for seasonal and fortuitous variations (excluding construction, food, beverages and tobacco).

Graph 2. Source: INSEE. Series seasonally adjusted. Moving averages of 3 months. End-of-month figures.

Graph 3. Source: INSEE. National index of consumer prices (259 items). Index of hourly wage rate, all activities, all regions.

Graph 4. Source: Conseil national du Cr dit. Short-term credits (up to 2 years) from monetary institutions to business and private customers — end-of-period figures.

Graphs 5 and 6. Series adjusted for seasonal and accidental variations (moving averages of 3 months). Exports fob, imports cif. Conversion at official exchange rates.

u.a. : one unit of account = 0.888761 gm. of fine gold = US \$1 at the official rate of exchange.

France

TABLE 1: Basic data (1965)

Total area ('000 sq. km.)	551.2
Total population ('000)	48 797
Density of population per sq. km.	88
Working population ('000)	19 642
Working population, breakdown by main sector (%)	
— Agriculture	17.3
— Industry	39.9
of which : Construction	9.4
— Services	42.8
Percentage share of gross domestic product	
— Agriculture	8
— Industry	46
of which: Construction	9
— Services	46
Gross product per capita (FF)	9 432

TABLE 2: Development of basic economic data

	% change by volume on preceding year							Volume indices (1958 = 100)	Contri- bution (in %) to GNP
	1959	1960	1961	1962	1963	1964	1965		
Gross national product	+ 2.7	+ 7.6	+ 4.6	+ 6.6	+ 5.2	+ 5.9	+ 3.4	142	—
Industrial production	+ 2.8	+ 7.7	+ 5.5	+ 6.2	+ 6.4	+ 7.4	+ 3.0	146	—
Total imports	- 1.7	+16.3	+ 7.2	+ 8.6	+12.2	+12.4	+ 3.6	174	14.2
Private consumers' expendi- ture	+ 1.9	+ 5.5	+ 5.9	+ 6.9	+ 6.8	+ 4.7	+ 3.2	141	63.8
Public current expenditure on goods and services	+ 6.6	+ 2.7	+ 3.4	+ 4.3	+ 1.2	+ 4.8	+ 2.3	128	13.3
Gross fixed asset formation	+ 2.3	+ 6.8	+10.5	+ 7.8	+ 7.5	+10.0	+ 7.1	165	21.7
Total exports	+11.9	+17.3	+ 5.4	+ 3.1	+ 8.2	+ 7.7	+10.9	184	15.2
Gross national product per capita	+ 1.7	+ 6.5	+ 3.5	+ 4.7	+ 3.3	+ 4.7	+ 2.3	130	—
Gross national product per person gainfully employed	+ 3.4	+ 7.6	+ 4.5	+ 6.4	+ 3.9	+ 4.7	+ 3.4	139	—

TABLE 3: Foreign trade (at current prices)

	% change on preceding year							Indices 1958 = 100	Million u.a.	% of the total
	1959	1960	1961	1962	1963	1964	1965	1965	1965	1965
Visible exports										
Total	+ 9.4	+22.5	+ 5.2	+ 2.0	+ 9.8	+11.3	+11.8	196	10 050	100
Intra-EEC	+33.7	+33.9	+18.8	+11.9	+14.2	+12.8	+18.0	362	4 116	41.0
To non-EEC countries	+ 2.4	+18.2	- 0.5	- 3.0	+ 7.2	+10.3	+ 7.8	149	5 934	59.0
Exports of food, beverages and tobacco										
Total	- 0.3	+36.2	+17.4	- 2.9	+22.0	+14.4	+11.5	241	1 601	15.9
Intra-EEC	+47.2	+54.6	+26.2	+ 1.4	+34.5	+16.6	+26.5	577	704	7.0
To non-EEC countries	-11.0	+29.3	+13.6	- 5.1	+15.4	+13.0	+ 2.0	165	897	8.9
Exports of raw materials and manufactures										
Total	+11.0	+20.2	+ 3.3	+ 3.0	+ 7.8	+10.7	+11.8	190	8 449	84.1
Intra-EEC	+32.6	+31.1	+17.5	+13.9	+10.9	+12.1	+16.4	336	3 411	34.0
To non-EEC countries	+ 4.8	+16.2	- 2.7	- 2.6	+ 6.0	+ 9.8	+ 9.0	146	5 038	50.1
Visible imports										
Total	- 9.2	+23.3	+ 6.3	+12.8	+15.9	+15.4	+ 2.7	184	10 338	100
Intra-EEC	+10.8	+36.3	+13.6	+20.0	+24.3	+20.3	+ 6.7	327	4 015	38.8
From non-EEC countries	-15.1	+19.0	+ 3.3	+ 9.2	+12.3	+12.4	+ 0.3	144	6 323	61.2
Imports of food, beverages and tobacco										
Total	-15.9	+ 6.2	- 2.3	+19.8	+ 5.1	+14.9	- 0.6	126	1 772	17.1
Intra-EEC	+54.3	+16.7	-12.3	+37.6	+37.4	+26.2	+ 8.9	410	378	3.6
From non-EEC countries	-20.8	+ 4.7	- 0.8	+17.4	0	+12.5	- 2.8	106	1 394	13.5
Imports of raw materials and manufactures										
Total	- 7.1	+28.7	+ 8.5	+10.9	+18.8	+15.5	+ 3.4	204	8 566	82.9
Intra-EEC	+ 7.5	+37.9	+16.3	+18.7	+22.7	+19.8	+ 6.5	321	3 638	35.2
From non-EEC countries	-12.5	+24.5	+ 4.5	+ 6.6	+16.3	+12.6	+ 1.2	161	4 928	47.7

TABLE 4: Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1958 = 100)	1964	143	146	145	150	149	149	129	84	139	146	151	148
	1965	141	145	145	148	148	151	129	91	142	153	156	160
	1966	150	156	157	158	158	161	142	95	153			
Building : number of permits issued ('000)	1964	39.8	39.3	43.1	47.6	41.5	47.6	51.0	33.3	44.2	67.9	47.3	72.5
	1965	38.8	44.7	45.9	43.8	44.6	50.5	41.8	44.4	49.6	53.2	57.6	83.0
	1966	41.3	36.3	42.1	48.0	36.6	49.4	44.2	40.5				
Private consumers' expenditure : turnover of department stores (1958 = 100)	1964	189	178	197	199	209	203	206	183	225	249	218	330
	1965	211	181	204	228	219	223	232	199	258	244	286	352
	1966	216	193										
Total visible imports (million u.a.)	1964	861	846	883	980	841	896	814	630	783	840	827	917
	1965	816	799	934	900	872	866	827	679	813	890	926	1 021
	1966	897	935	1 098	994	1 002	1 063	929	780	995	1 031	1 059	
Total visible exports (million u.a.)	1964	731	751	768	771	705	797	754	554	697	834	806	823
	1965	688	782	896	839	853	823	857	671	826	916	896	1 006
	1966	774	874	1 023	947	916	960	952	729	849	950	924	
Balance of trade (million u.a.)	1964	- 130	- 95	- 115	- 159	- 136	- 99	- 60	- 76	- 86	- 6	- 21	- 94
	1965	- 123	- 17	- 38	- 61	- 19	- 43	+ 30	- 8	+ 13	+ 26	- 30	- 15
	1966	- 123	- 61	- 75	- 47	- 86	- 103	+ 23	- 51	- 146	- 81	- 135	
Official gold and foreign exchange reserves (gross, million u.a.)	1964	4 481	4 494	4 477	4 533	4 630	4 737	4 813	4 827	4 863	4 902	4 999	5 105
	1965	5 172	5 254	5 316	5 367	5 341	5 350	5 336	5 346	5 381	5 381	5 449	5 459
	1966	5 468	5 503	5 571	5 649	5 724	5 821	5 967	5 963	5 893	5 856	5 793	
Money supply (FF '000 million)	1964	147.7	146.6	143.6	148.6	149.0	152.1	156.3	154.3	155.2	155.3	154.5	162.0
	1965	159.3	157.9	159.9	161.9	162.6	166.1	170.1	169.2	170.2	171.6	169.9	177.2
	1966	174.5	173.5	175.6	177.3	177.7	182.1	186.4	184.0	185.3			

France

NOTES

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

Table 1

- Total population at mid-year.
- Working population in employment at mid-year.
- Breakdown of gross domestic product for 1962 at factor cost.
- GNP at market prices.

Table 2

- GNP at market prices. Source: Rapport sur les comptes de la Nation, ministère de l'économie et des finances, Paris.
- Industrial production : value added by industry.
- Total exports and imports : goods, services and factor income.
- The figures for GNP per head and per person in employment from 1958 to 1964 are Commission estimates based on the component series.

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 and manufactures (groups 2-9 CST).

Table 4

- Industrial production, excluding construction, food, beverages and tobacco.
- Construction. Building permits granted for housing. Source : Bulletin statistique du ministère de la construction.
- Private consumption. Index of value of total turnover of department stores and "single-price" stores.
- Exports fob, imports cif. Conversion at official exchange rates.
- 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 end of month.
- Money supply. Source : Conseil national du Crédit. Fiduciary circulation (total of coins and notes in circulation, excluding coins and notes held by the Banque de France) plus sight deposits (deposits made with the Banque de France by private persons or enterprises, deposits with Post Office savings accounts or with Treasury agencies, plus the sight deposits relating to the activities pursued within France by the banks : registered banks, banques populaires, caisses de crédit agricole and the Banque française du commerce extérieur, no matter whether these deposits are shown in French francs or some other currency or whether they belong to residents or non-residents). End-of-month figures.

C. Italy

In 1966 the upward trend of business activity was even more distinct than in 1965, chiefly as a result of faster growth in private consumers' expenditure, but also owing to a gradual recovery in building and construction. The expansion, which was common to all the main sectors of the economy, and to which both foreign and domestic demand contributed, was accompanied by a further considerable improvement in productivity and an approximate stabilization of prices. Although the balance of payments deteriorated in the course of the year, it again closed with a large surplus.

In 1967 the expansion is likely to be maintained and consolidated, but it is not impossible that the upward pressure on prices may gradually gain in strength. At the same time, the growth of activity can be expected to benefit the trend of employment more than hitherto. The current balance of payments is likely to deteriorate further, and more appreciably than in 1966, but will still show a surplus.

In view of these prospects it seems that short-term economic policy, which in 1966 was still decidedly expansionary, should in the course of 1967 veer back more in the direction of caution as the cyclical forces in the economy gather momentum. Only in this way will it be possible to ensure an expansion of the economy which is balanced, rapid and lasting.

1. Balance-sheet for 1966

In 1966 there was a distinct upward trend in economic activity, which by about the spring had reached all the main sectors and to which both foreign and domestic demand contributed.

Exports of goods and services continued to be the most dynamic element of overall demand, although from mid-1966 they seemed to show a fairly distinct loss of momentum and, as expected, their yearly growth rate was not so marked as from 1964 to 1965.

Visible exports expanded rapidly. Though in some countries which are important customers for Italian products the economic situation slackened, this has so far been offset more or less clearly by a further improvement in Italy's competitive position on the international market. The value of visible exports, as defined for the foreign trade statistics, may have risen from 1965 to 1966 by just under 13 %; in terms of volume the increase was about one percentage point higher, as average export values declined further.

Analysis by type of goods shows that exports of capital goods and textiles expanded fastest, while the area analysis shows that exports to the other Community countries advanced more rapidly than to other areas.

Exports of services also continued to grow very vigorously. In particular, receipts from tourism showed a lively growth and income from capital abroad increased appreciably.

Total exports of goods and services, as defined for the national accounts, seem to have risen about 13 % in value and 12.5 % by volume, against 20.1 % and 19.9 % in 1965.

Domestic demand expanded considerably, which it had not done in 1965. Gross fixed asset formation, which had long been in the doldrums, showed on the whole a tendency to rise; after several years of decline, investment in building began to recover somewhat in the first half of 1966, the tide having probably been turned by investment in housing, which accounts for over half of all investment in building and construction. Relatively early in the year industrial building and public works (including some works of public utility commissioned by state-controlled enterprises) had shown signs of picking up. On account, however, of the low level of business activity towards the end of 1965, total building investment in 1966 was probably at best slightly higher than in 1965. Investment in plant and in machinery, on the other hand, which had begun to expand again as early as mid-1965, was probably well above the 1965 level, despite the fact that, during the first half of the year in particular, it was hampered by the losses of production caused by strikes.

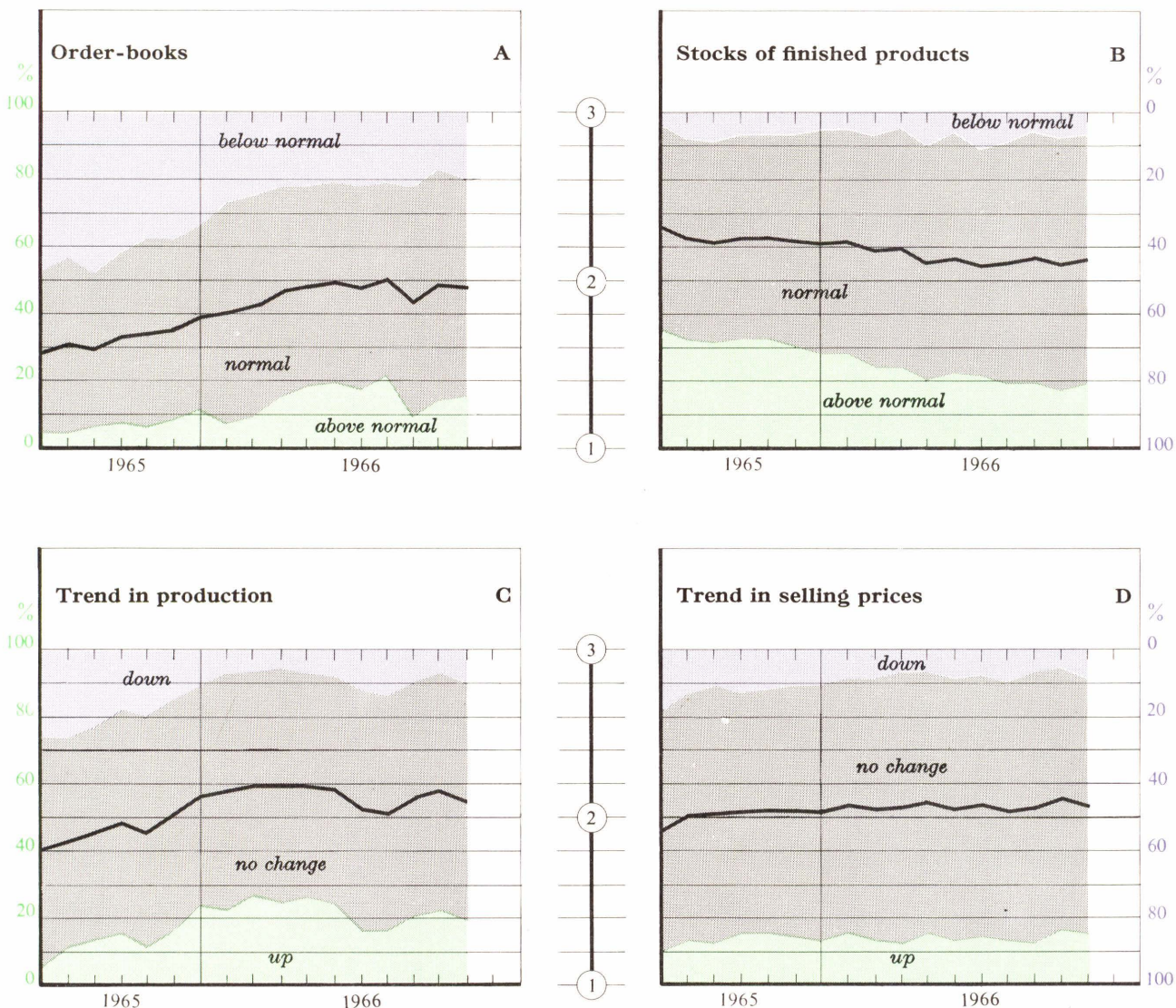
At present the total increase in gross fixed asset formation for 1966 is estimated at 4.5 % in value and 3.5 % by volume, compared with a fall of 6.8 % and 8.2 % for 1965.

Although investment in stocks was affected by the catastrophic weather in northern and central Italy in November to an extent which is still difficult to assess, it may well have expanded appreciably from 1965 to 1966. To judge by as yet incomplete indicators, this expansion was due almost exclusively to a faster build-up of stocks of raw materials and semi-finished products, itself connected with the rapid increase in industrial production.

Total consumer expenditure probably grew even faster than investment expenditure, at any rate in year-to-year terms, and probably also between the beginning of the year and the end. The same cannot perhaps be said of public current expenditure on goods and services, which rose somewhat more slowly than from 1964 to 1965; nevertheless it too has expanded fast, perhaps by a good 11 % in value and by 5 % by volume, against 11.6 % and 3.7 % from 1964 to 1965.

Private consumers' expenditure may well have expanded faster than before. The trend of production and net imports of industrial consumer goods in the first eight months of the year suggests, at any rate, a very lively increase in domestic demand for these goods. For 1966 as a whole it is estimated that the growth of private consumers' expenditure will be 8 % in value and 5.5 % by volume, against 6 % and 2.1 % for 1965.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

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

Expenditure on the more expensive types of consumer goods may well have grown particularly fast. The number, for example, of new passenger and estate cars registered from January to November 1966 was no less than 13 % higher than a year earlier.

This expansion of private consumers' expenditure is chiefly due to a fast growth of income, but also presumably to some reduction in saving, which was particularly high in 1965. Incomes other than wages and salaries, in particular incomes of enterprises and transfer incomes, seem to have expanded particularly fast; it is evident that the total wages bill also grew again at a considerable pace, probably a good 7 %. Agreed minimum hourly wages, it is true, increased only a little, mainly because the conclusion of new wage agreements in important branches of the economy were greatly delayed and the cost-of-living allowances given on the basis of the sliding wage scale went up at a relatively slow pace. Average actual hourly wages, however, certainly grew more quickly again, one reason being the movement of manpower from sectors of the economy with lower wages to others with relatively high pay. The total number of hours worked also showed a distinct rise, though in the year-to-year comparison this is exclusively because of an increase in per capita working time. Disposable incomes, moreover, doubtless expanded faster than gross incomes, since direct taxes rose at a relatively slow pace from 1965 to 1966 as an after-effect of the economic downswing in 1964.

On the domestic supply side, agriculture's contribution to real gross domestic product rose only 1.5 %, after a rise of 3.5 % in 1965. Though the fruit and vegetable crops were considerably better than a year earlier, the wheat harvest was below the 1965 level. In general the impact on agriculture of the disastrous weather was more serious than in other sectors.

In the course of the year the high pace at which industrial production was growing accelerated still further, and output for the year was higher than in 1965, despite a massive increase in the losses caused by strikes. As defined for the ISTAT index of industrial production, it may have risen by nearly 12 %, compared with an increase of 4 % in 1965. All the main branches of industry contributed to this growth, in particular textiles, chemicals and mineral oil refining. It should be noted that cement production has been moving upwards again since the fourth quarter of 1965.

After a two-year decline, building and construction (value added at constant prices) picked up again somewhat in the spring : however, on account of the low level reached at the end of 1965, the totals for the two years are likely to be much the same.

Real value added in the services sector may have been about 4 % higher than in 1965.

The above assumptions imply that the rise in real gross national product from 1965 to 1966 should be about 5.5 % (1964 to 1965, 3.4 %).

The trend of the number of persons employed continued to lag far behind the growth of production. Apparently further very considerable increases in productivity

were achieved through organizational measures within firms. Changes in the pattern of employment also helped to increase productivity. Finally, as already pointed out, the average per capita working time of wage earners and salaried workers grew quite distinctly. According to ISTAT the number of workers on short time in 1966 showed a fall of over 44 % by comparison with the previous year. In these circumstances the number of wage earners and salaried workers increased only slowly in 1966. The average level for the year has been about 1 % below that for 1965, when it had been some 2.6 % lower than in 1964.

Although the number of unemployed went down in the course of 1966, the decrease was very slight. According to ISTAT sample surveys the average number of unemployed in 1966 was no less than 770 000 (i.e. nearly 4 % of the working population), which was still 6.8 above the 1965 level.

Imports of goods and services expanded very vigorously. The seasonally adjusted figures for visible imports rose rapidly, but not, at least until the beginning of the autumn, as fast as in the first half of 1965. As defined for customs statistics they may have grown from 1965 to 1966 by no less than 15-16 % in volume and some 17 % in value (1964 to 1965: 1.6 % and 1.7 %). The most lively advance was made by imports of textiles, iron and steel, precision instruments and chemicals. In the breakdown by country of origin the increase in visible imports from the other Community countries was particularly marked.

Imports of services may have expanded at more or less the same pace as visible imports. In all, imports of goods and services (as defined for the national accounts, including factor income from abroad) must therefore have increased by 15 % by volume and by 17 % in value, as against a bare 1 % and 2.1 % from 1964 to 1965.

The price trend was decidedly calm. The implicit price deflator of the real gross national product is estimated to have risen by 2.5 % from 1965 to 1966, and therefore distinctly more slowly than in the years from 1961 to 1965. Numerous factors had a damping influence on prices, in particular the high elasticity of industrial output, the extraordinarily good crops of some products which serve consumption directly and, last but not least, the fact that unit production costs showed a relatively modest rise. On the one hand fixed costs, which were kept down by the internal organizational measures referred to above, were spread over a volume of production that was growing considerably. On the other hand the labour market situation did not cause wages to rise much, at least in industry, while the increase in productivity was considerable.

Wholesale prices moved very little. Consumer prices, too, showed no more than a relatively slow increase, especially food prices. Those of other goods and services, however, continued to rise quite distinctly, although less so than in the previous two years. The average wholesale price index for the first ten months of the year was 1.8 % above the 1965 level but in October showed no increase over October 1965 level; the corresponding figures for the consumer price index were 2.4 % and 1.8 %. For the first time in five years the cost-of-living bonuses, which are given on the basis of the sliding wage

scale and are linked with the changes in the cost of living in the preceding three months did not go up on 1 November.

The developments in foreign trade outlined above led to a distinct increase in the trade deficit from Lit. 99 000 million in 1965 to probably over Lit. 300 000 million in 1966 (customs statistics). Since at the same time unrequited transfers may have diminished somewhat, the 1966 surplus on current account was probably smaller than in 1965, when it was Lit. 1 428 000 million, although net receipts from services again grew appreciably.

Capital movements on the other hand can be expected to show a heavy deficit—the change from 1965 being due primarily to the fairly wide difference between interest rates in Italy and abroad. Foreign exchange statistics for the first ten months of the year showed a deficit of Lit. 327 000 million, against Lit. 6 000 million in the same period of 1965. The surplus on the overall balance of payments will therefore be far smaller in 1966 than in the previous year, when it was Lit. 996 000 million. As exports of money by the commercial banks continued, though at a slower pace, the increase in net official

Demand for and supply of goods and services

	1964 ⁽²⁾	1965 ⁽²⁾		1966 ⁽³⁾		1967 ⁽⁴⁾
	At current prices (in Lit. '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports ⁽¹⁾	5 486	+ 19.9	+ 20.1	+ 12.5	+ 13.5	+ 9
Gross fixed asset formation	7 202	— 8.2	— 6.8	+ 3.5	+ 4.5	+ 8
Public current expenditure on goods and services	4 659	+ 3.7	+ 11.6	+ 5	+ 11.5	+ 3
Private consumers' expenditure	20 841	+ 2.1	+ 6.0	+ 5.5	+ 8	+ 6.5
Gross national product	33 112	+ 3.4	+ 7.1	+ 5.5	+ 8	+ 6
Imports ⁽¹⁾	5 293	+ 0.9	+ 2.1	+ 15	+ 17	+ 14

⁽¹⁾ Goods, services and factor income.

⁽²⁾ ISTAT : I Conti Nazionali dell'Italia — Nuova Serie — Anni 1951-1965.

⁽³⁾ Commission estimates.

⁽⁴⁾ Commission forecasts.

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.

gold and foreign currency reserves was probably again much smaller than the surplus on the balance of payments; in the first nine months of the year it amounted to Lit. 120 000 million. Net reserves fell again in October, as they had already done in September (level at end of October 1966 : Lit. 2 920 million).

The domestic liquidity of the banking system again benefited greatly from developments in the balance of payments. Treasury transactions worked in the same direction, at least in the first nine months of 1966, despite a sharply growing supply of funds from the issue of long-term government securities, but their impact on liquidity was considerably weaker. As however bank advances expanded noticeably faster—in the first nine months total outstanding advances were 10.5 % larger than a year before—and as the banks continued to build up their security portfolios considerably, there was, despite a further rise in the calls they made on the central bank, a tendency for liquidity to decrease during the first three quarters of 1966. Bank liquidity continued nevertheless to be high.

The securities market was, apart from shares, decidedly active and the proportion of private buyers in relation to total demand increased distinctly. According to preliminary estimates by the Banca d'Italia, the value of net issues of fixed-interest securities was Lit. 3 000 000 million or some 50 % higher than in 1965; of this amount over half, or Lit. 1 770 000 million, consisted of securities issued directly or indirectly by the Treasury (Lit. 1 100 000 million more than in 1965). An issue of long-term Treasury bills in autumn, which at Lit. 680 000 million (gross) was the largest in Italy to date, was soon fully subscribed by the public and the banks; of this issue, however, only Lit. 380 000 million represented additional demand for capital. The net yield on bonds, which declined from mid-1964 on, has been rising slightly since spring 1966, but even this was due, towards the end of the year, partly to support operations by the Banca d'Italia. Share prices tended to harden quite a little after the rise at the turn of the year 1965/1966.

2. Outlook for 1967

In 1967 there will probably be rapid economic growth, which will be on a broad front and in the early stages is likely to be still fairly balanced. Quantitative forecasts of its extent are particularly uncertain, because the effects of the disaster already referred to cannot yet be assessed accurately. It is already possible to say, however, that economically supply and demand will both tend to rise as a result of the catastrophe which has proved so tragic in human terms. These additional impulses, which derive only from the need for renewal of investments and for other forms of replacement demand, are of course essentially different in character from those due to normal cyclical factors, because they increase wealth little if at all.

Demand from abroad may well continue to increase vigorously, though probably the pace of increase will once again be less rapid, for the expected faster growth of domestic demand may lead to some slackening of the export efforts made by businessmen and limit at least the growth rate of production intended for export. Furthermore the weakening

of business activity in some countries which are important customers for Italian products may gradually come to act as a brake on the expansion of exports. On the other hand Italy's strong competitive position suggests that the growth of its imports will continue to be rapid; they should also benefit from the pending improvement in export credit conditions and the quite successful efforts to intensify trade with the Eastern bloc countries. If it is assumed that the rapid increase in exports of services will also continue, the growth of goods and services for 1967 will probably be 10 % in value and 9 % by volume.

The expansion of domestic demand will probably accelerate both in the course of 1967 and in comparison with 1966.

This applies to gross fixed asset formation, both investment in plant and machinery and, even more, investment in building and construction, the recovery of which is expected to gain momentum in 1967. The measures taken at the end of 1965 to promote residential building should be having their full effect, especially as rents will be gradually decontrolled probably from July 1967 on. There are at the same time various indications that there will be a decided expansion of public works; because of the recent disaster there are considerable additional requirements to be met in this sector. Lastly, it appears that investment in industrial building can be expected to rise appreciably; the number of building permits issued, at any rate, has been growing for some time.

For a number of reasons, the outlook for investment in plant and machinery also appears to be quite expansionary. The margins of unused productive capacity, the existence of which has for some time doubtless curbed the propensity to invest, have probably shrunk, as for several years past the expansion of production has been accompanied by an absolute decline in investment. This assumption is supported by the results of the EEC business survey. In addition there will probably be greater efforts to invest in rationalization, since the facilities for rationalizing organization have been used very intensively in the last few years and are sure to be more or less exhausted for the present. Further, the profitability of enterprises has increased appreciably in the last two years and prospects for profits continue to be favourable despite a return to considerably heavier fiscal and "para-fiscal" burdens in connection with the flood damage (probable ending of the arrangement by which certain social charges were covered from the national budget, increase in direct taxation). For the present, at least, ample funds are still available to borrowers. Last but not least, there is an unmistakable psychological improvement in the climate of the business sector, due no doubt to the favourable attitude of the authorities towards investment. In recent years the Government has taken numerous credit and tax measures to encourage industrial investment and high priority is again given to the same objective in the "Report on forecasts and programming for 1967", which was submitted by the Government in September.

Total fixed asset formation may rise from 1966 to 1967 by 10 % in value and by 8 % by volume. A further vigorous increase in stock building is to be expected.

Consumer expenditure will probably grow fast both on a year-to-year comparison and during the course of the year. The growth rate of public current expenditure on goods and services will again be very considerable. Nevertheless it might be smaller than from 1965 to 1966; at any rate both the draft budget and the report already referred to point to the attempts being made to moderate the rapid growth of public current expenditure. But how far this objective can be achieved is uncertain because of the recent tragic events.

The expansion of private consumers' expenditure, on the other hand, is expected to accelerate. There are a number of pointers to a further and faster increase in direct taxation and—despite the measures being taken to assist those who have suffered from the flooding—possibly a somewhat more modest growth of transfer income than in 1966. These damping factors, however, may be outweighed by the expected acceleration in the growth of the total wages bill: the trend of employment will probably be more lively than in 1966, particularly because of the recovery of investment in building, and the pace at which wages are rising can also be expected to pick up again. In some important industries, such as foodstuffs and textiles industry, the conclusion of new wage agreements is imminent and in others, particularly the metal products industry and chemicals, new agreements have recently been concluded.

In these circumstances private consumers' expenditure in 1967 may be at least 9 % in value and by over 6 % by volume higher than in 1966.

This outlook for demand suggests that a very lively expansion of production is to be expected, especially in industry, where output will probably rise by 12 %. The growth rate for building and construction is particularly difficult to estimate, but it could be a good 6 %. Production in the services sector will probably rise at about the same pace as from 1965 to 1966, i.e. by some 4 %. If a more or less normal growth of agricultural production is assumed, the total real gross national product should expand by some 6 %.

The number of persons unemployed will probably diminish more rapidly in the course of 1967 and show a distinct fall even on a year-to-year comparison.

The expansion of imports of goods and services may accelerate in 1967 and on a year-to-year comparison it is expected that there will be a 14 % increase by volume and 16 % in value.

Prices may in the aggregate be only moderately higher than in 1966, but it is quite possible that their upward trend may accelerate somewhat in the course of the year. Pointers suggesting more lively developments in prices are: the expected faster growth of building demand, the weakness of which has doubtless had a damping effect on prices in recent years; the probability that fruit and vegetable crops will be less abundant than in 1966, coupled perhaps with certain production losses due to the floods; a probably firmer rise in unit wage costs; the raising of some direct and indirect taxes (on petrol, non-alcoholic drinks and domestic electric current) and the probable retransfer to enter-

prises of the social charges which had been covered by the State; and lastly, though the effect will be more limited, the gradual removal of rent control expected to begin on 1 July.

Forecasts of the trend of exports and imports imply a distinct deterioration in the trade balance in the course of 1967, but for the year as a whole a considerable surplus on current account can still be expected.

In such a situation those responsible for short-term economic policy should abstain from additional measures likely to inflate the internal demand in money terms, as only thus can the tendency for prices to stabilize be maintained and a durable expansion of the economy assured. In order to keep the danger of renewed overheating to a minimum, short-term economic policy should be made slightly more restrictive as the spontaneous expansionary forces of the economy gain in strength. The propensity of firms to undertake rapidly productive investment, which has picked up only very hesitatingly, must at the same time be given steady support. The very fast growth of consumer expenditure, on the other hand, must be gradually, but distinctly, slowed down.

For budget policy this means in the main that, while government expenditure affecting investment, which in 1966 may have even declined, should be stepped up considerably, current expenditure, which in the last few years has been growing rapidly, should be limited as strictly as the circumstances arising from the natural disaster allows. The total net stimulation provided by the budgets must gradually be reduced.

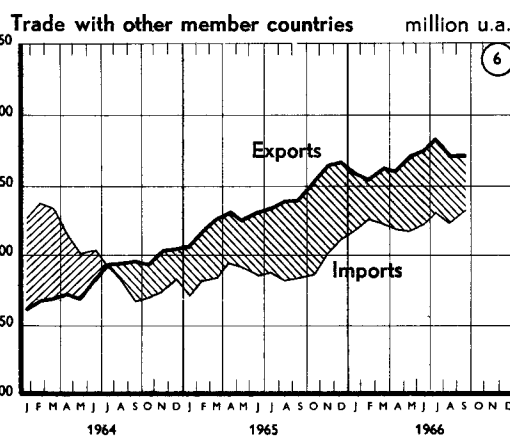
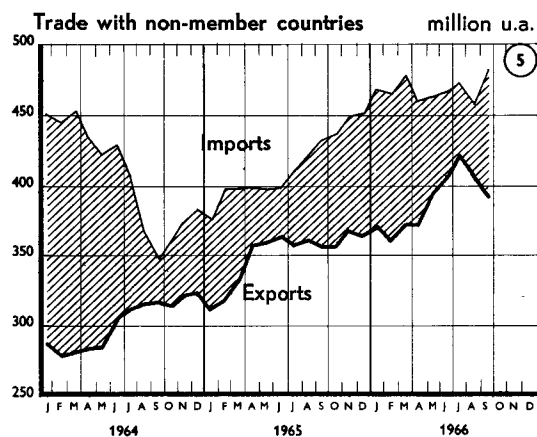
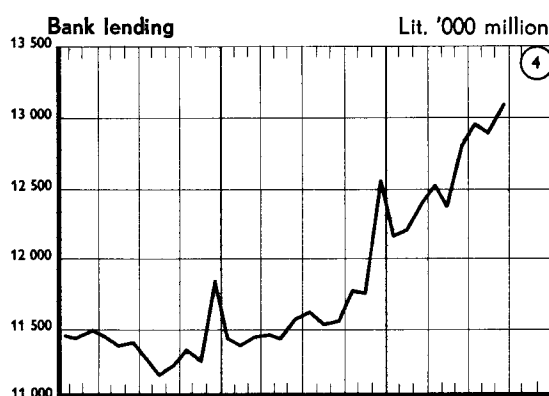
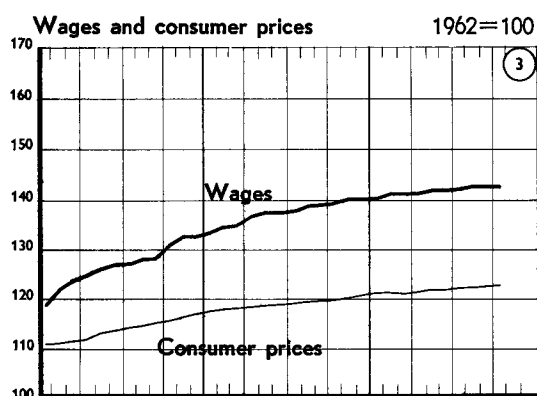
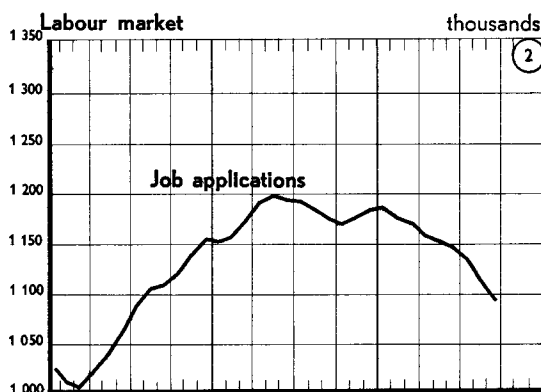
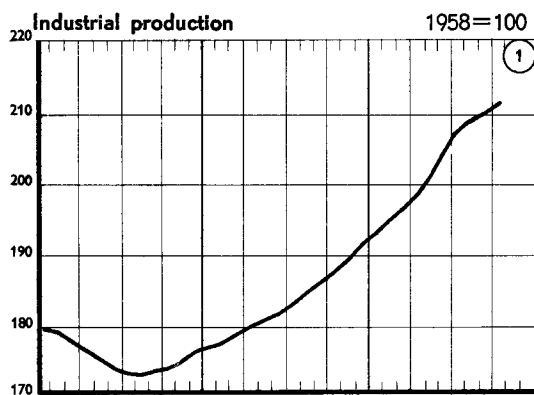
In this way the chances will improve of an appreciable revival in saving by the public authorities which in recent years has been shrinking extremely fast, and of limiting the calls the public authorities have to make on the resources of the capital market. These resources may well grow as public deficits gradually cease to be covered by borrowing on the short-term market—a change that is definitely to be recommended in view of the improvement in business activity. This would also reduce the danger that the cumulative effect of the public sector's financial deficit and of the rapidly expanding demand for external funds, which industry is likely to make in the not distant future, might overload the market and produce a bottle-neck that would hamper investment, or that credit might be expanded too fast and inflationary pressures could develop.

These considerations also make it clear how urgent is the need for rapid measures to stimulate saving and the capital market.

Credit policy should continue to be flexibly applied, at any rate for the time being, but the risk that the available supplies of liquidity and credit might build up too far must be constantly borne in mind. It is, moreover, quite clear that the more closely budget policy corresponded to the requirements of the economic situation the longer could credit policy remain flexible.

Lastly, if prices show signs of rising, the authorities should make judicious use of the possibility provided under the Treaty of Rome of reducing customs duties ahead of schedule in order to increase supplies more quickly. At any rate, the foreseeable trend of the balance of payments and the very high level of official gold and foreign currency reserves do not stand in the way of such a policy.

ECONOMIC INDICATORS



NOTES:

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

Graph 1. Trend curve; estimation established on the basis of indices adjusted by the SOEC for seasonal and fortuitous variations (excluding construction, food, beverages and tobacco).

Graph 2. Number of registered unemployed, in thousands. Series seasonally adjusted. Moving average of 3 months.

Graph 3. Source: ISTAT. Agreed minimum wages in industry.

Graph 4. Short-term loans. Source: Banca d'Italia.

Graphs 5 and 6. Series adjusted for seasonal and accidental variations (moving averages of 3 months). Exports fob, imports cif. Conversion at official exchange rates.

Italy

TABLE 1: Basic data (1965)

Total area ('000 sq. km.)	301.2
Total population ('000)	51 380
Density of population per sq. km.	171
Working population ('000)	19 199
Working population, breakdown by main sector (%)	
— Agriculture	25.8
— Industry	40.2
of which : Construction	10.1
— Services	33.9
Percentage share of gross domestic product	
— Agriculture	13.4
of which: Construction	39.5
— Industry	8.2
— Services	47.1
Gross product per capita (Lit.)	688 000

TABLE 2: Development of basic economic data

	% change by volume on preceding year							Volume indices (1958 = 100)	Contri- bution (in %) to GNP
	1959	1960	1961	1962	1963	1964	1965		
Gross national product	6.8	6.3	8.2	6.3	5.8	3.0	3.9	148.1	—
Industrial production	9.7	11.1	9.3	8.8	7.9	2.0	3.8	165.7	—
Total imports	12.0	37.8	14.8	16.4	22.6	- 5.4	0.6	240.7	15
Private consumers' expendi- ture	4.6	6.2	7.3	6.7	10.0	2.0	1.9	145.5	62
Public current expenditure on goods and services	4.4	4.0	4.8	5.4	5.1	4.1	3.7	136.0	15
Gross fixed asset formation	9.1	13.4	11.8	10.0	9.2	- 7.3	- 8.0	141.9	19
Total exports	19.8	18.2	16.5	12.2	7.0	12.0	20.1	266.5	18
Gross national product per capita	6.1	5.7	7.7	5.6	5.0	2.1	3.0	140.8	—
Gross national product per person gainfully employed	6.1	6.5	8.0	7.5	7.6	3.3	6.0	152.2	—

TABLE 3: Foreign trade (at current prices)

	% change on preceding year							Indices (1958 = 100)	Million u.a.	% of the total
	1959	1960	1961	1962	1963	1964	1965	1965	1965	1965
Visible exports										
Total	14.1	26.1	14.7	11.4	8.2	18.0	20.2	282.3	7 159.5	100
Intra-EEC	30.7	36.0	21.8	23.7	10.3	26.4	27.2	475.5	2 833.3	40.3
To non-EEC countries	8.9	22.3	11.8	5.8	7.0	13.4	15.9	221.6	4 276.2	59.7
Exports of food, beverages and tobacco										
Total	4.4	5.6	10.6	14.5	- 3.4	2.4	20.4	166.3	848.7	11.9
Intra-EEC	18.1	12.5	14.7	23.4	- 8.7	8.8	31.2	245.4	465.0	6.5
To non-EEC countries	- 3.7	0.4	7.4	6.5	2.1	- 3.3	9.4	119.6	383.7	5.4
Exports of raw materials and manufactures										
Total	16.6	30.7	15.5	10.9	10.2	20.5	20.2	311.5	6 310.8	88.1
Intra-EEC	36.3	45.4	23.9	23.9	15.6	30.4	26.5	580.0	2 418.3	33.8
To non-EEC countries	11.5	26.0	13.7	4.5	7.7	15.5	16.6	241.9	3 892.5	54.3
Visible imports										
Total	6.2	41.0	10.6	15.9	24.5	- 4.1	1.7	233.1	7 350.9	100
Intra-EEC	31.5	45.7	17.2	22.9	31.1	- 4.5	- 3.0	335.7	2 294.7	31.2
From non-EEC countries	- 0.8	38.4	8.1	13.0	21.5	- 3.9	3.9	204.6	5 056.2	68.8
Imports of food, beverages and tobacco										
Total	2.0	33.5	5.3	7.3	57.5	2.4	18.8	294.8	1 610.5	21.9
Intra-EEC	15.3	42.6	- 1.3	10.0	73.1	15.7	20.6	431.2	335.5	4.6
From non-EEC countries	- 0.2	31.8	6.6	6.8	54.4	- 0.6	18.4	272.2	1 275.0	17.3
Imports of raw materials and manufactures										
Total	7.1	42.4	11.6	17.5	19.2	- 5.5	- 2.3	220.1	5 740.4	78.1
Intra-EEC	33.6	46.0	19.2	24.1	27.8	- 6.6	- 6.1	323.4	1 959.2	26.7
From non-EEC countries	- 0.9	41.0	8.4	14.4	14.8	- 4.8	- 0.2	188.9	3 781.2	51.4

TABLE 4: Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1958 = 100)	1964	177.9	171.7	178.2	178.4	169.5	167.7	179.8	128.6	175.8	181.5	173.8	171.9
	1965	167.6	166.9	182.3	178.9	182.0	175.8	192.1	140.4	188.5	191.1	189.7	190.7
	1966	186.4	182.7	205.4	194.0	208.8	195.3	206.9	166.9	212.3			
Building: domestic turnover of building materials (1958 = 100)	1964	178.5	169.8	188.3	183.6	195.3	195.3	193.3	181.7	197.6	182.9	156.4	169.2
	1965	160.8	136.8	173.8	160.8	166.7	196.3	192.8	183.4	184.7	185.6	185.5	180.2
	1966	142.7	129.3	177.6	183.1	195.1	188.6	201.8	202.8	172.1	203.8		
Private consumers' expenditure: turnover of department stores (1958 = 100)	1964	254	210	255	246	277	300	280	232	290	355	289	513
	1965	270	215	249	303	234	318	296	241	330	354	319	542
	1966	313	231	275	313	319	338	306	(274)				
Total visible imports (million u.a.)	1964	722.2	721.4	609.9	639.1	602.0	649.0	539.1	471.0	545.7	592.0	509.6	595.8
	1965	550.3	619.5	556.0	580.7	570.9	592.8	609.7	609.1	632.1	644.0	676.8	666.0
	1966	721.7	691.2	679.2	655.9	685.1	721.6	690.9	638.6	839.3			
Total visible exports (million u.a.)	1964	475.7	452.0	414.8	505.1	444.2	532.1	546.6	454.9	538.4	538.8	500.5	532.8
	1965	514.1	562.1	583.0	618.6	546.8	657.5	587.7	578.5	624.4	601.6	643.7	609.0
	1966	623.1	600.2	671.6	629.1	702.2	739.7	683.9	620.9	693.2			
Balance of trade (million u.a.)	1964	-296.0	-243.7	-213.3	-156.8	-171.0	-126.1	+ 27.0	- 0.3	- 8.5	- 20.5	- 5.1	- 50.9
	1965	- 84.9	- 32.0	+ 13.1	- 6.5	- 43.8	+ 37.5	- 2.1	- 9.3	- 1.1	- 3.2	- 28.4	- 25.0
	1966	-144.3	- 64.2	- 14.9	- 55.8	+ 4.8	- 8.2	+ 16.3	+ 34.6	+135.7			
Official gold and foreign exchange reserves (net, million u.a.)	1964	3 154.1	2 958.7	2 748.3	2 723.9	2 761.2	2 826.2	2 898.2	3 071.0	3 257.1	3 432.1	3 615.2	3 756.3
	1965	3 797.8	3 873.9	3 755.8	3 811.5	3 895.5	4 032.3	4 250.4	4 390.7	4 323.0	4 270.2	4 303.4	4 566.2
	1966	4 425.9	4 386.4	4 337.6	4 404.2	4 433.8	4 537.3	4 772.8	4 995.8	4 758.2			
Money supply (Lit. '000 million)	1964	11 053	10 961	11 096	10 953	11 118	11 264	11 308	11 239	11 379	11 434	11 702	12 465
	1965	11 984	11 861	12 077	12 225	12 522	12 687	12 885	12 808	13 108	13 227	13 420	14 495
	1966	14 029	13 933	14 046	14 118	14 321	14 598	14 850	14 744				

() Provisional figures.

Italy

NOTES

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

Table 1

- Present-in-area population (resident population less persons temporarily abroad). Average for year. Source : Istituto Centrale di Statistica.
- Working population in employment. Average for year. Source : Istituto Centrale di Statistica, "Rilevazione nazionale delle forze di lavoro—20 ottobre 1965".
- Breakdown of gross domestic product by factor cost.
- GNP at market prices.

Table 2

- GNP at market prices.
- Industrial production : value added by industry at factor cost.
- Total exports and imports : goods, services and factor income.
- GNP per person in employment for 1959. Commission estimate.

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 and manufactures (groups 2-9 CST).

Table 4

- Industrial production. Source : Istituto Centrale di Statistica.
- Building. Internal trade in building materials, calculated from turnover taxes. Source : Istituto per lo Studio della Congiuntura.
- Private consumption. Retail sales of department stores, based on the turnover of 5 department stores and 2 "single-price" stores. Not very typical of the trend in private consumption as a whole.
- Exports fob, imports cif. Conversion at official exchange rates.
- Official gold and foreign exchange reserves. Source : Ufficio Italiano dei Cambi.
- Money supply. Notes and coin circulation, excluding cash holdings of the Treasury. Sight deposits of non-banks with registered credit institutions; bank drafts in circulation (whether *vaglia* or *assegna*) issued by the Central Bank and of other banks and credit institutions.

D. The Netherlands

A certain slackening in the rate of expansion of overall demand in the second half of 1966 may mean that economic growth in the full year 1966 will be somewhat less than in 1965.

The growth of exports slowed down, but more important were the difficulties over financing, as these had an increasingly restrictive effect on overall investment expenditure—which nevertheless was well above the total for 1965. These difficulties were in turn due mainly to the unfavourable trend of public saving and of possible savings by enterprises, and also to the effect on internal liquidity produced by the deterioration in the balance of payments and the restrictive credit policy. On the other hand, the vigorous expansion of current expenditure on goods and services continued at a rate only slightly slower than before.

Although the labour market began to show signs of easing, the basic trend of costs and prices was again sharply upwards. To this were added “autonomous” factors pushing prices upwards particularly higher indirect taxation. For the full year, the increase in consumer prices will have been much more vigorous than in 1965. Furthermore, the deficit on current account for 1966 will be the highest recorded in the Netherlands since 1950.

The tendency for excess demand to diminish that was apparent towards the end of 1966 should continue during 1967. The growth of expenditure on fixed investment is likely to weaken very distinctly, and the volume of this investment could even show an actual decline. Since the pull exerted by demand from abroad will not be appreciably stronger, this can be expected to inhibit the growth rate of private consumption also; what happens here, however, will depend largely on the decisions taken with regard to wages policy.

In spite of the further easing of the labour market forecast for 1967, the after-effects of earlier increases in unit costs and the effect of their continued if slightly weaker rise will prevent the re-establishment of domestic equilibrium. The current payment account may indeed recover, but hardly to the extent necessary.

It now seems to be recognized that it is not possible to continue a fiscal policy which has not only had an inflationary impact but has at the same time impaired the conditions for balanced economic growth. The time would seem to be ripe for a fiscal policy which increases public saving at the expense of public and private consumption and promotes economic growth by bringing back better conditions for the financing of investment.

1. Balance-sheet for 1966

The economy in 1966 was characterized on the one hand by a high growth rate for the full year, due to rapid expansion in the first six months, and on the other by a tendency for business activity to slow down in the course of the year.

The rate at which exports of goods and services were expanding had shown a slight tendency to slacken in 1965, and in 1966 this tendency became more distinct. Customs statistics show that visible exports will have increased by some 6.5 % (in value) and 6 % (by volume), against 10 % and 9 % in 1965. In the third quarter, the year-to-year rate of increase in value was of the same order as the average for the year.

The fairly quiet trend of exports during 1965 undoubtedly contributed to the lower rate of annual growth in 1966. While agricultural exports were hindered by special factors in the early months of the year (especially the outbreak of foot-and-mouth disease), the slackening was in part attributable to economic conditions also, inasmuch as the expansion of demand from countries that are important customers of the Netherlands weakened during the second half of the year; despite certain price concessions, Dutch exporters were not able fully to counteract the effects of this development.

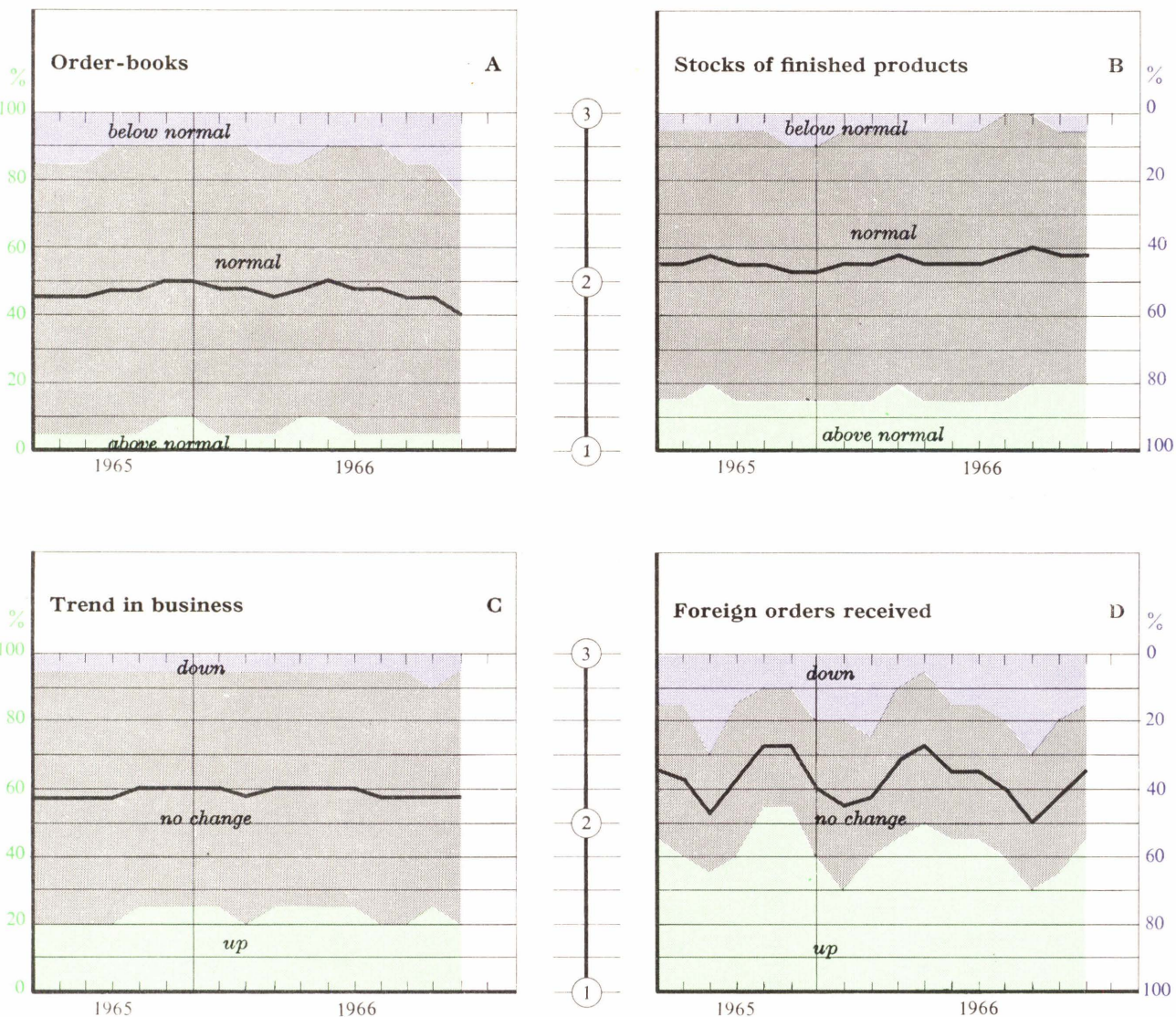
In spite of the sharp decline in the growth of sales to the Federal Republic of Germany and Italy attributable among other things to a fall in exports of transport equipment, Dutch exports to the Community expanded, in contrast with 1965, more rapidly than exports to non-member countries, which from the early months of 1966 onward were affected by a distinct decline in exports to the United Kingdom.

The increase in overall returns from services and factor income was also lower than in 1965, owing mainly to a marked contraction in the growth of receipts from tourism. All in all exports of goods and services, as defined for the national accounts, should have increased by 6 % in value (5.5 % by volume) in 1966, as compared with 10.6 % (+ 9.1 %) in 1965.

In contrast with demand from abroad domestic demand showed a slight upward trend in 1966 as a result of increased investment activity. This is however true only of the year-to-year comparison, as the seasonally adjusted figures showed a distinct slackening in the expansion of investment during the second half of the year.

The very strong impetus given to the economy by gross fixed asset formation reflects in the main an increase over the 1965 growth in investment expenditure by enterprises. Investment by public enterprises, particularly in the extension of plant for natural gas extraction and in the purchase of aircraft, contributed to this increase. Investment by the private sector in plant and machinery and in construction also increased at a higher rate than in 1965. Determining factors here were the introduction early in 1965 of a more expansionary policy for the grant of building permits to industry, and the fact that profits proved to be slightly more favourable than anticipated. As the year wore on, however, the effect of increased labour costs on profit margins became more and more

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION

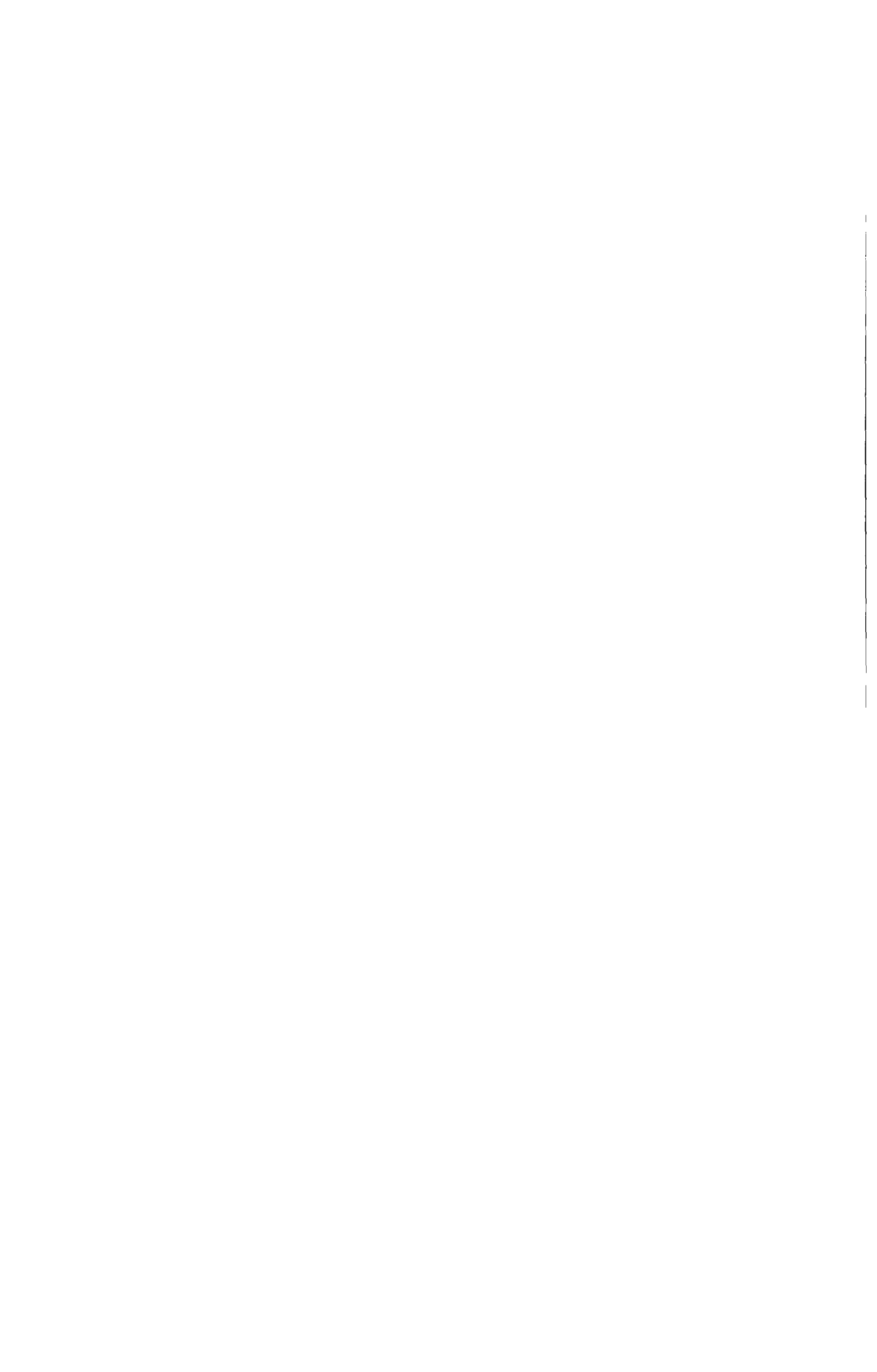


Source : Business survey of the Centraal Bureau voor de Statistiek.

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

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

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



apparent, and this, put a brake on investment by small and medium-sized enterprises in particular. This tendency for expansion to slow down was reinforced by the shortage and high cost of borrowing money for financing purposes. Despite this change in business trends in the autumn months, stockbuilding by enterprises in 1966 may have risen by not less than 13.5 % in value (9 % by volume), compared with an increase of 6.9 % (3.8 %) in 1965.

Expenditure by the public authorities on gross fixed asset formation is likely to show a further distinct increase on 1965 (about 9 % in value, against 8.3 % in the previous year). Nevertheless, there was in this sector a fairly distinct decline in growth in the second half of 1966 following the introduction of restrictive measures in May and the financial difficulties experienced by the local authorities in particular.

As against this, expenditure on housing slackened somewhat in 1966. Here too the shortage of funds for financing, both in the subsidized and in the privately financed sectors, was in part responsible, but the persistent rise in prices also played a large part. The total of about 120 000 completions in 1966 exceeds the 1965 total by only about 5 000. It should be noted, however, that the average size of dwelling (in cubic metres) is likely to have increased quite considerably in 1966. Once again prices showed a lively upward trend.

For the full year 1966, gross fixed asset formation may have increased by about 12.5 % in value and 7.5 % by volume, compared with 9.4 % and 5.1 % in 1965.

Stockbuilding also showed an appreciable increase on 1965. The ratio between the increase in stocks and gross national product, which stood at 1 % in 1965, may have exceeded 2 % in 1966. This acceleration is attributable in the main to the stockpiling of raw materials and semi-manufacturers which began as early as the middle of 1965. It gradually began to slacken again only from the spring of 1966 onwards while stocks of finished industrial goods may have shown a slight upward trend during the year.

Despite the measures introduced in May, which affected in particular expenditure on the defence forces and the recruitment of staff in the public sector, the increase in public current expenditure on goods and services seems to have been as rapid in 1965.

Private consumers' expenditure on the other hand may have expanded a little more slowly. The growth rate for the full year may have been in the region of 10 %, compared with 11.9 % in 1965; in terms of volume there was, because of the accelerated upward movement of prices (6.2 % as against 3.8 %) a very distinct weakening in the pace of growth—almost 4 % in 1966, against 7.8 % in 1965.

The reduced rate of expansion in expenditure over the year was largely caused by the hesitant growth in sales of consumer durables following abnormally high sales towards the end of 1965 in anticipation of increased taxes on consumption. A further contributory factor however was the fact that the growth of the disposable incomes of households was slightly less brisk, while the savings ratio actually tended if anything to decline.

There was little reduction in the rate at which the total wages bill expanded; the slight slackening of tempo in relation to 1965 was caused mainly by a levelling off in the rate at which the total number in paid employment was rising, and this in turn was largely due to a decline in the numbers employed in industry. Per capita wage increases may have exceeded 10.5 %, despite the 7 % limit on increases in agreed wage rates imposed by the authorities in May; this can hardly be regarded as a significant reduction on the 11 % recorded in 1965. The expansion of the other sources of revenue of households (income from self-employment and property, and transfer incomes) was somewhat slower. Furthermore, the effects of direct taxation may have been more pronounced than in 1965.

The increase in the labour force, the tendency for real demand to slacken that made itself felt during the year and appreciably greater advances in productivity led to an easing of the pressures on the labour market. The seasonally adjusted number of unfilled vacancies had fallen back to 92 000 by the end of November (against 130 000 in November 1965), while the number of unemployed rose to 60 000 (compared with 37 000 a year ago). The seasonally adjusted unemployment rate (percentage of unemployed in the total labour force) was 1.3 % at the end of November. Geographically and occupationally there were differences in the extent to which the pressures eased, and the change was more marked in the case of male than female labour. Towards the end of the year, the supply of and demand for labour in the building industry were virtually in balance.

As a result of the trend in overall demand outlined above and of the increased production capacity created by last year's boom in investment, the degree of utilization of production capacity fell gradually during 1966. In industry this led to a certain reduction in the growth rate of the adjusted figures during the second half of the year. Nevertheless, a further increase of at least 6 % in industrial production (value added) can be expected in 1966 (7 % in 1965). The CBS index of production per working day shows that the growth rate for the third quarter was 7 % higher than in the corresponding period last year.

In spite of slightly higher output in the building and construction and in agriculture, the growth rate of the gross national product in 1966 will be lower than in 1965, principally because the value added in the services sector expanded less than in 1965. The real gross national product is likely to have increased by more than 4.5 %, against 5.4 % in 1965. This would be slightly lower than the growth rate forecast in the last Quarterly Survey.

Despite the fact that there was increased elasticity of domestic supply, imports of goods and services rose more rapidly than in 1965. Customs returns show that visible imports for the first ten months of 1966 were 8.5 % higher by volume (10.2 % in value) than in the corresponding months of the previous year. Stockpiling of raw materials contributed to this development, at least over part of the year, but the trend in purchases of other goods, especially consumer goods, was a very dynamic factor; imports from other Community countries expanded steadily, while imports from non-member countries tended to contract from the beginning of the year, with the result that for the full year the former rose more markedly than the latter.

A more lively increase in expenditure on business and holiday travel abroad meant that imports of services increased rapidly in 1966. Finally, if the sharp rise in transfers of factor income is taken into account, the growth rate for imports of goods and services combined (as defined in the national accounts) can be estimated at 8 % in volume and 9 % in value. The corresponding growth rates for 1965 were 7.4 % and 7.7 %.

Price levels increased more vigorously in 1966 than in 1965. This was only in part due to the special factors which affected the price of agricultural produce and the higher indirect taxation which came into effect at the beginning of the year; a more considerable part seems to have been played by the sharper impact of the rise in production costs, which in turn was due to too sharp an increase of demand in money terms. Wholesale prices for manufactured goods increased by 4.5 % between December 1965 and September 1966 following an increase of 1.3 % a year earlier. In January to September 1966 average wholesale prices were 5.6 % higher than in the same period last year. The corresponding increase in the cost of living was 6.2 % (5 % in 1965). However, under the influence of seasonal reductions in the prices of certain foods and a tightening of the official policy of direct price controls this index, which had risen very rapidly until the month of April, tended to fall slightly at times later in the year. For the third quarter the rate of increase was none the less still 4.9 % higher than a year before. The items most affected by the more rapid increase in prices during 1966 were certain services (rents, transport and entertainment) and food, textiles and tobacco.

As a result of the slackening of the growth rate for volume of exports and an accelerated rate of expansion of volume of imports, but also because of a deterioration in the terms of trade, the external balance suffered to the extent of some 1 % of the gross national product. Although the current balance of payments (on a transactions basis) was in virtual balance in 1965, there may well be a deficit of some Fl. 800 million in 1966, exceeding the record deficit of 1964, the year of the "wage explosion". Furthermore the considerable surplus on capital transactions in 1965 has been reduced owing to an increase in official exports of capital.

All in all there was again a sharp drop in net gold and foreign exchange reserves. They fell by Fl. 613 million between the end of December 1965 and the end of September 1966 (a reduction of Fl. 465 million was recorded in the corresponding period a year earlier). The reserves of the Central Bank fell by Fl. 24 million and the net foreign exchange holdings of the commercial banks were reduced by Fl. 589 million. At the end of September short-term foreign indebtedness of the commercial banks could be described as heavy, whereas at the end of 1965 their net credit balance had stood at Fl. 120 million.

The expansion of internal liquidity slackened slightly until at any rate the summer months of 1966. The effects of the deterioration in the current account and capital account situation were primarily responsible, although transactions by the public sector, particularly the short-term borrowing practised by the local authorities, continued to have a strong expansionary effect. Transactions by industry, where demand for liquidity rose appreciably in response to expanding production and rising costs and prices, had a similar if less marked effect.

The demand for funds from the banking system was particularly brisk in the first four months of 1966; the expansion of short-term credit over this period was considerably in excess of the limits fixed. As the year wore on the expansion of this form of credit moderated, but the growth of medium-term credit may have continued into the autumn months at least. As a result, pressure on bank liquidity was considerably higher in 1966, as is evident from the fall in the net foreign exchange holdings of the commercial banks, their increased calls on the Central Bank and the higher interest rates on the money market.

Demand for and supply of goods and services

	1964 ⁽¹⁾	1965 ⁽¹⁾		1966 ⁽²⁾		1967 ⁽³⁾
	At current prices (in Fl. '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports ⁽⁴⁾	30.28	+ 9.1	+ 10.6	+ 5.5	+ 6	+ 6.5
Gross fixed asset formation	15.38	+ 5.1	+ 9.4	+ 7.5	+ 12.5	- 0.5
Public current expenditure on goods and services	9.78	+ 0.9	+ 11.2	+ 2.5	+ 11.5	+ 2.5
Private consumers' expenditure	35.58	+ 7.8	+ 11.9	+ 4	+ 10	+ 3.5
Gross national product	61.83	+ 5.4	+ 11.0	+ 4.5	+ 10.5	+ 3
Imports ⁽⁴⁾	30.89	+ 7.4	+ 7.7	+ 8	+ 9	+ 3

⁽¹⁾ Statistical Office of the European Communities, National Accounts 1955-1965.

⁽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.

In 1966, official issues on the stock market increased, while issues by the private sector (apart from those initiated abroad) tended to remain static. The private sector may, however, have increased its demand for capital outside the stock exchange. Be that as it may, the tendency for long-term interest rates to increase continued into the spring, when they levelled off or even fell back slightly.

2. Outlook for 1967

There may be a fairly pronounced decline in economic growth in 1967 due in particular to a perceptible slackening of investment activity.

Exports—in terms of volume at least—can be expected to expand somewhat more rapidly than in 1966, when incidentally the pace was the lowest for any year since 1962. Dutch exporters seem prepared to accept certain price-cuts to maintain their position on foreign markets, and it may be that special factors (deliveries of natural gas and agricultural produce) will prove more favourable than in 1966. Finally, intra-Community customs duties will be further reduced in mid-1967. However, some unfavourable influences must also be expected. The overall business prospects in a number of countries that purchase large quantities from the Community are distinctly less promising than they were a year ago. There is furthermore a danger that labour costs per unit of production will once again rise more vigorously in the Netherlands than in its competitor countries as a whole. In the circumstances, the increased flexibility of exports caused by the fall-off in the expansion of domestic demand will certainly not be entirely reflected in increased exports.

Provided invisible exports and factor income advance further, total exports as defined for the national accounts could increase by 6.5 % both in value and volume.

Domestic demand will expand less than in 1966, owing principally to a marked decline in the rate at which investment expenditure is increasing. The adjusted figures for gross fixed asset formation are unlikely, in terms of volume at least, to maintain the record level attained probably somewhere in the third quarter of 1966. This will undoubtedly be the case in investment by enterprises, where the rapid increase noted till the autumn will presumably give way to a weaker trend. In view of the deterioration in the volume of funds available for investment, the reduced degree of utilization of production capacity and the uncertain short-term economic outlook, a reduction in investment activity is only to be expected, especially as the stimulating effects of increased capacity in the building industry and the consequent ease with which buildings permits for industrial construction can be obtained are gradually diminishing. Furthermore, it is probable that public enterprises will no longer be contributing to the growth of investment. For the full year 1967 it would appear that investment by enterprises will at best increase slightly in value; in volume a decrease of from 2 to 3 % may be expected.

Expenditure on housing should not show any very distinct increase, since the effect of the reduction in the number of starts caused by financing difficulties in 1966 will become apparent in 1967. In this sector, however, where the public authorities play a major role, and indeed in the whole sphere of public investment, decisions of major importance for 1967 have yet to be announced. In any case no increase is likely in the investment expenditure of the local authorities, principally because of the tightness of funds.

All in all there could be a slight expansion of expenditure on gross fixed asset formation in 1967; in terms of volume it is unlikely to reach the level of the previous year again.

Investment in stocks will probably increase much less rapidly than in 1966 because of the expected slowdown in economic expansion in the Netherlands and the probable price trends on world markets.

The difficulties encountered in drawing up the 1967 budget make any valid estimate of the development of public current expenditure on goods and services impossible; there could however be a certain fall-off in the rate of growth.

The same applies to transfer incomes of households. When this survey was being prepared, no general decisions had been taken concerning developments in wages and salaries, the most important source of income. Nevertheless in the light of the present tendency to moderation—due to the easier situation on the labour market, the general shortage of ready funds and the poor balance of payments position—there is some reason to believe that in many cases the rise in agreed wage rates will be relatively close to the forecast increase in the growth of productivity. Furthermore, allowance must be made for several existing factors which will tend to increase wages (increases granted in 1966, higher allowances to offset higher rents) and for existing medium-term wage agreements which not only link wage increases to the cost-of-living index but also provide for fairly high annual rates of increase. Finally, despite the tendency for the labour market situation to ease, wage drift will still occur. It can be estimated therefore that per capita wages and salaries will show a further increase of almost 8 % and that—in view of a further if relatively small increase in the numbers employed—the overall wages and salaries bill will increase by almost 9 %.

While the incomes of households derived from self-employment and property, on the other hand, are expected to expand relatively slowly, the reduction in direct taxation planned for mid-1967 will presumably have the effect of expanding total available income considerably.

All in all, then, a very provisional forecast can be made that—provided there is a small increase in—private consumers' expenditure will show a further vigorous increase of some 8.5 %. Since prices are expected to increase, this would mean an increase of slightly more than 3.5 % in real terms.

The tendency for the labour market situation to ease should continue in 1967, although the rate of increase in the labour force will decline further and the agreed working week in industry is to be shortened towards the middle of the year. It is probably, furthermore, that the net inward flow of migrants will give way to a net outflow. For the full year the rate of increase in the total number of hours worked (the average hours worked multiplied by the number in paid employment) is likely to slacken and the average unemployment rate for the year to reach a level that represents full employment rather than over-employment.

In view of the reduced rate of expansion forecast for overall demand in 1967, particularly with regard to investment, internal production is likely to expand less than in 1966. In the case of industrial production an increase of the order of 4.5 % is possible. Considering the slower growth rates forecast for the remaining sectors—with the exception of agriculture which should expand at the same rate as in 1966 if weather conditions are normal—the real gross national product can be expected to expand by some 3 % in 1967.

Following the more rapid growth recorded in 1966, imports of goods and services (as defined for the national accounts) can be expected to expand appreciably less fast in 1967; in volume their growth rate should amount to some 3 %. Among visible imports, the growth rate for purchases of raw materials and semi-manufactures in particular may contract appreciably, which would mean that imports from non-member countries would be harder hit than imports from other Community countries. It must, however, be expected that the loss of the competitive advantages which the Netherlands has had over several of its competitor countries in prices and costs will undoubtedly tend to keep the propensity to import at a high level in 1967.

The less brisk expansion of demand is unlikely to lead as yet to pronounced slackening in the upward movement of internal price levels. On the one hand, it would appear that cost inflation, as a result of the persistent of slightly weaker increase in wage costs, will continue for quite some time. Added to this are the after effects of earlier increases in costs. The upward movement will be considerable both in the prices for industrial goods—despite the moderating influence exerted by the trend of demand, the easing of world prices for certain raw materials and the pressure exerted by the government's direct price control policy—and even more in prices in the services sector. The rates charged by several public enterprises may well be increased from the beginning of the year, and rents also can be expected to be higher than in 1966. Furthermore, increases in indirect taxation which are, it seems, to be introduced in the middle of the year, will tend to make prices higher. Finally, if other "autonomous" factors which tend to cause prices to rise are taken into account, particularly agricultural prices, it is quite likely that consumer prices will increase by some 4.5 %.

The very distinct deterioration of the external balance in 1966 should, on the basis of these assumptions, be followed by a definite recovery in 1967. It is not however to be expected that the current account (including unrequited payments and remittances) will again show a satisfactory surplus.

Faced with the probability of an economic development which betrays at one and the same time inflationary or immediately post-inflationary symptoms and a tendency for business activity to slow down—in short, by a weakening of economic expansion in real terms—coupled with an insufficient improvement in the balance on current account, those responsible for economic policy have a very delicate task to perform. Their task will be complicated by the fact that the weakening is at present concentrated in the "wrong sector", affecting investment by enterprises rather than consumption; responsibility for this situation rests with the hitherto failure to deal with excess demand, with the effects of rising costs, the deterioration of the external balance, direct price control,

the consequent pressure on profit margins and, above all, with a "policy mix" in which a highly expansionary budget policy conflicted with a restrictive credit policy.

The boom in investment was undoubtedly too strong, although the statistics must be viewed with caution because the high rate of growth was due in part to large investments by enterprises in public ownership or in which the public authorities hold a share. On the other hand it would be undesirable for overall investment to decline in absolute terms, or for investment in the private sector to drop too sharply. The same applies to housing, although here the slowdown is tending to have less effect. Finally, any serious reduction in investment by the local authorities is to be avoided, despite the fact that for a time they had to be called upon to moderate their expansion.

There is no doubt that this overall trend in investment will exert an increasingly restrictive influence on the rate of expansion of wages and consumption, which is still far too high; on the other hand there is also a possibility that it might become a serious threat to real economic growth and full employment.

In the circumstances, a change in the ingredients of economic policy is to be recommended more urgently than ever before. The budget policy of the public administrations must be reformed in such a way that it ceases to exert an inflationary influence partly through financing their heavy deficits by short-term borrowing and partly by making excessive demands on the capital market which curb investment by other sectors. In other words, a strong recovery in public saving appears to be necessary, and this can only be achieved by a reduced rate of expansion in current expenditure and/or measures which will lead to a rapid increase in current revenue. If a budget policy on such lines were put into practice, the strictness of credit policy could and should doubtless be relaxed at an early date.

The authorities have announced, following the Government crisis, that they now intend to pursue a policy along these lines as has been recommended for some time. It is to be hoped that no time will be lost in implementing an economic policy which reflects both the need to stabilize price and unit costs and also the aim of economic expansion; otherwise it could indeed be too late, which would mean that equilibrium could no longer be restored without some measure of recession.

Though the draft budget for 1967 submitted by the previous Government will be adhered to in principle, it has at the time of writing this report been proposed to make the second cut in income tax on 1 July instead of 1 January, while the general 20 % increase in turnover tax which was to have come into effect on 1 January 1968 will now be brought forward to 1 July 1967. The dates for the implementation of these fiscal measures may however be changed in the light of the economic situation. For the rest, the other tax measures included in the draft budget are to be maintained—more rapid collection of tax on incomes over Fl. 15 000, higher excise duty on petrol and diesel oil, increased turnover tax on textiles and shoes, retention of the increase in corporation tax approved in 1966, continued suspension of relief afforded through depreciation allowances, etc.

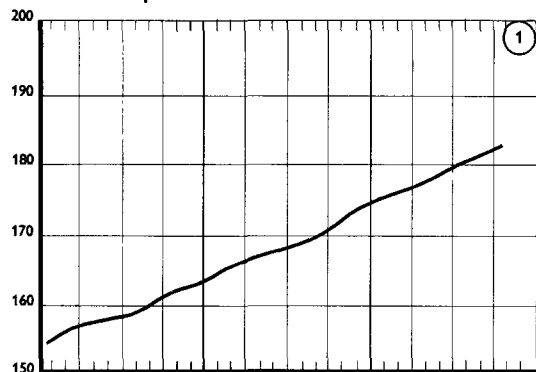
Although there is no way of knowing whether the expansion of Government expenditure on goods and services can be brought down to the figures shown in the draft budget—in accordance with the wish expressed by the authorities—introduction of the new tax measures should reduce the Government's budget deficit by some F. 500 million on the cash transactions. At the same time there is a proposal for funding part of the short-term debts of the local authorities.

The implementation of such a programme would undoubtedly have a stabilizing effect. Increased prices resulting from higher indirect taxes could certainly not be regarded as inflationary. Whether the pattern of these measures pays sufficient attention to the problem of growth is, however, open to question. It would be preferable to curb the expansion of current expenditure on consumption and transfers rather than burden enterprises with increased corporation tax and speedier tax collection. The day may not be far off when it would be advisable to restore certain depreciation allowances, though this should only be done to the extent that alternative resources have been made available through the application of other measures to reduce consumption.

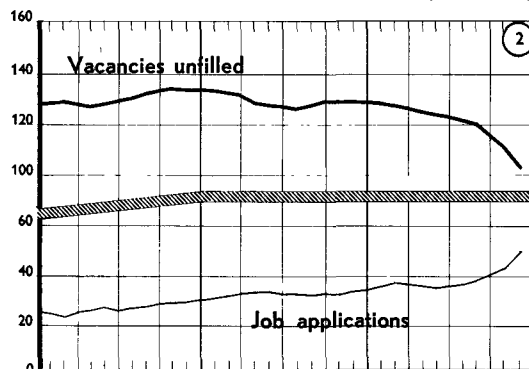
Finally, the authorities are endeavouring to persuade both sides of industry to show a moderation consonant with the requirements of economic policy. Such moderation would be welcome, especially as experience has shown that unless a special effort is made there can be a considerable time-lag between economic developments and the reaction of employers and employees to these developments. At the stage of the economic cycle on which the Netherlands economy is now entering, the upward pressure on prices would be prolonged and the danger of severe repercussions on employment enhanced.

ECONOMIC INDICATORS

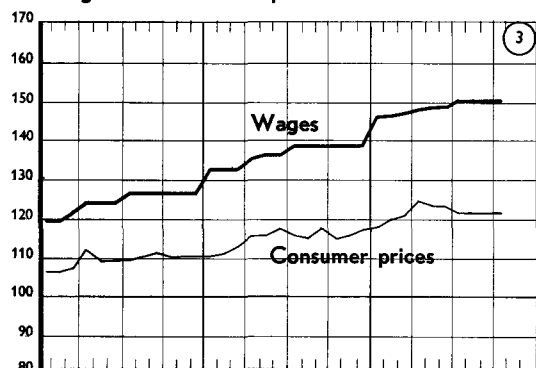
Industrial production 1958=100



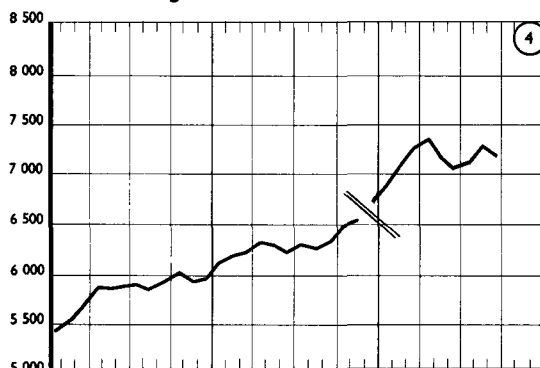
Labour market (thousands)



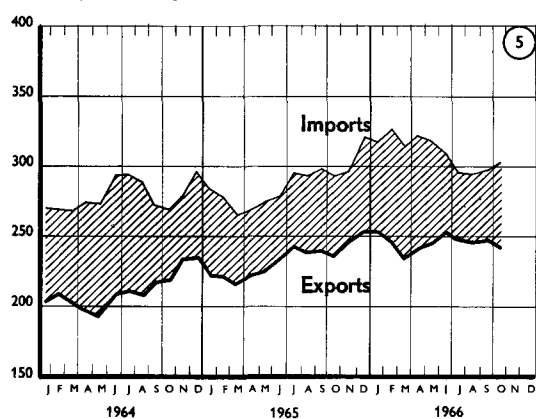
Wages and consumer prices 1962=100



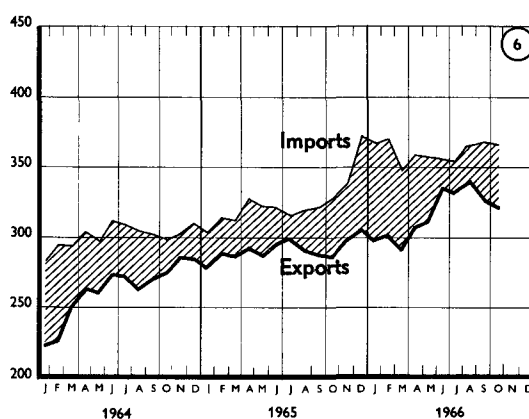
Bank lending Fl. million



Trade with non-member countries million u.a.



Trade with other member countries million u.a.



NOTES:

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

Graph 1. Trend curve; estimation established on the basis of indices adjusted by the SOEC for seasonal and fortuitous variations (excluding construction, food, beverages and tobacco).

Graph 2. Adjusted for seasonal variations. Three-months moving average.

Graph 3. Index of consumer prices — general index. Source: CBS. Wages — index of gross hourly earnings in industry (excluding mining, quarrying and construction). Index of negotiated wages.

Graph 4. Short-term bank advances. Revised series as from december 1965.

Graphs 5 and 6. Series adjusted for seasonal and accidental variations (moving averages of 3 months). Exports fob, imports cif. Conversion at official exchange rates. 1 unit of account = 0.888671 gm. of fine gold = US \$1 at the official rate of exchange.

Netherlands

TABLE 1: Basic data (1965)

Total area ('000 sq. km.)	33.5
Total population ('000)	12 292
Density of population per sq. km.	367
Working population in 1961 ('000)	4 289
Working population, breakdown by main sector in 1961 (%):	
— Agriculture	10
— Industry	42
of which : Construction	10
— Services	48
Percentage share of gross domestic product :	
— Agriculture	8.3
— Industry	41.2
of which: Construction	(7)
— Services	50.5
Gross product per capita (Fl.)	5 584

TABLE 2: Development of basic economic data

	% change by volume on preceding year							Volume indices (1958 = 100)	Contri- bution (in %) to GNP
	1959	1960	1961	1962	1963	1964	1965	1965	1965
Gross national product	+ 5.2	+ 8.9	+ 3.5	+ 3.8	+ 3.7	+ 8.8	+ 5.4	146	—
Industrial production	+ 9.0	+10.1	+ 4.2	+ 4.8	+ 5.4	+10.1	+ 5.3	160	—
Total imports	+13.8	+17.3	+ 5.8	+ 7.5	+ 9.5	+14.8	+ 7.4	205	48
Private consumers' expendi- ture	+ 4.6	+ 6.4	+ 5.8	+ 6.5	+ 7.7	+ 6.1	+ 7.8	154	58
Public current expenditure on goods and services	- 1.2	+ 6.6	+ 4.4	+ 5.1	+ 7.8	+ 2.8	+ 0.9	129	16
Gross fixed asset formation	+12.0	+11.6	+ 6.7	+ 4.4	+ 2.1	+16.9	+ 5.1	175	24
Total exports	+11.5	+13.3	+ 3.0	+ 6.2	+ 6.2	+11.8	+ 9.1	179	49
Gross national product per capita	+ 3.7	+ 7.6	+ 2.2	+ 2.4	+ 2.2	+ 7.3	+ 3.9	133	—
Gross national product per person gainfully employed	+ 4	+ 7	+ 2	(+ 2.5)	(+ 2)	(+ 7)	(+ 4)	(134)	—

() Provisional figures.

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year							Indices 1958 = 100	Million u.a.	% of the total
	1959	1960	1961	1962	1963	1964	1965			
Visible exports										
Total	+12.1	+11.7	+ 6.9	+ 6.5	+ 8.2	+17.0	+10.1	199	6 396	100
Intra-EEC	+19.4	+15.3	+10.9	+10.0	+17.3	+22.1	+10.2	267	3 564	55.7
To non-EEC countries	+ 6.9	+ 8.4	+ 3.6	+ 3.2	- 0.6	+11.2	+10.0	151	2 832	44.3
Exports of food, beverages and tobacco										
Total	+14.4	+ 5.3	+ 0.8	+ 6.9	+ 9.3	+ 9.5	+13.0	176	1 568	24.5
Intra-EEC	+28.9	+ 6.1	+ 3.1	+10.0	+12.1	+12.8	+19.7	231	972	15.2
To non-EEC countries	+ 3.4	+ 4.4	- 1.8	+ 3.3	+ 5.3	+ 5.1	+ 3.6	126	596	9.3
Exports of raw materials and manufactures										
Total	+11.2	+14.2	+ 9.2	+ 6.3	+ 7.9	+19.6	+ 9.2	208	4 328	75.5
Intra-EEC	+16.1	+20.7	+14.3	+10.0	+19.4	+25.6	+ 7.1	283	2 592	40.5
To non-EEC countries	+ 8.1	+ 9.6	+ 5.2	+ 3.2	- 2.4	+13.1	+11.9	159	2 236	35.0
Visible imports										
Total	+ 8.7	+15.0	+12.8	+ 4.6	+11.6	+18.2	+ 5.9	206	7 471	100
Intra-EEC	+15.3	+18.6	+21.1	+ 6.7	+14.9	+19.0	+ 8.7	263	3 987	53.4
From non-EEC countries	+ 3.9	+12.2	+ 5.8	+ 2.5	+ 8.3	+17.4	+ 2.9	165	3 484	46.6
Imports of food, beverages and tobacco										
Total	+ 9.4	+ 3.4	+ 5.9	+ 6.3	+15.5	+16.2	+ 3.5	177	988	13.2
Intra-EEC	+ 9.5	+16.4	+41.5	- 7.0	+11.8	+22.0	+13.1	282	225	3.0
From non-EEC countries	+ 9.3	+ 1.2	- 1.0	+10.0	+16.3	+14.9	- 1.2	159	763	10.2
Imports of raw materials and manufactures										
Total	+ 8.5	+17.2	+14.0	+ 4.3	+11.0	+18.6	+ 6.3	211	6 483	86.8
Intra-EEC	+15.6	+13.3	+20.0	+ 7.6	+15.0	+19.0	+ 7.8	262	3 762	50.4
From non-EEC countries	+ 2.3	+15.6	+ 7.7	+ 0.7	+ 6.1	+18.0	+ 4.2	167	2 721	36.4

TABLE 4 : Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1958 = 100)	1964	146	151	154	154	158	153	138	141	154	167	168	164
	1965	157	159	159	163	166	164	145	147	165	177	179	174
	1966	165	168	174	178	176	176	151	163	176	187		
Investment (Fl. million)	1964			3 333			4 030			3 913			4 100
	1965			3 744			4 233			4 224			4 581
	1966			4 100			4 916			4 913			
Building (Fl. million)	1964			1 362			1 632			1 783			1 613
	1965			1 545			1 814			1 993			1 854
	1966			1 537			2 079			2 249			
Private consumers' expenditure (1958 = 100)	1964	157	146	159	158	173	162	183	163	168	184	174	195
	1965	175	153	175	186	189	182	207	176	187	199	201	232
	1966	192	169	194	209	206	204	221	197	203	211		
Total visible imports (million u.a.)	1964	589	569	549	640	562	623	636	499	559	628	567	630
	1965	554	564	630	614	577	617	665	587	620	676	625	793
	1966	625	626	759	701	630	634	652	620	696	670	669	
Total visible exports (million u.a.)	1964	452	446	440	479	455	491	484	405	561	552	505	538
	1965	477	439	532	506	501	554	543	438	596	594	557	611
	1966	500	470	572	570	544	612	549	498	632	598	616	
Balance of trade (million u.a.)	1964	- 137	- 123	- 109	- 161	- 107	- 137	- 152	- 94	+ 2	- 76	- 62	- 92
	1965	- 77	- 75	- 99	- 108	- 76	- 63	- 121	- 98	- 24	- 82	- 68	- 132
	1966	- 125	- 156	- 188	- 131	- 86	- 71	- 103	- 122	- 64	- 72	- 53	
Official gold and foreign exchange reserves (million u.a.)	1964	1 860	1 841	1 333	1 802	1 817	1 786	1 869	1 879	1 960	1 965	2 069	2 084
	1965	2 075	2 094	2 069	2 033	2 036	2 010	2 042	2 053	2 065	2 088	2 120	2 058
	1966	1 970	1 972	1 997	1 943	1 953	1 918	2 012	2 010	1 996	(1 999)	(2 062)	
Money supply (Fl. '000 million)	1964	14.31	14.31	14.29	14.51	14.99	15.08	15.10	15.10	15.13	15.01	15.27	15.45
	1965	15.53	15.56	16.67	16.05	16.62	16.81	17.01	17.04	16.89	16.89	16.97	17.15
	1966	17.09	17.07	17.04	17.50	18.10	18.58	18.43	18.04	17.98	17.77		

Netherlands

NOTES

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

Table 1

- Total population at mid-year.
- Working population in employment, average for year.
- Breakdown of GNP by factor cost.
- GNP at market prices.

Table 2

- GNP at market prices.
- Industrial production : value added by industry.
- Total exports and imports : goods, services and factor income.
- Industrial production as % of GNP in 1961.

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 and manufactures (groups 2-9 CST).

Table 4

- Industrial production. Source : Centraal Bureau voor de Statistiek (CBS). General index, adjusted for number of working days.
- Investment. Source : CBS. Gross fixed investment. Total in value, quarterly figures.
- Construction. Source : CBS. Building production. Total in value, quarterly figures.
- Private consumption. Source : CBS. Index of value of private consumption.
- Exports fob, imports cif. Conversion at official exchange rates.
- Official gold and foreign exchange reserves. Gross reserves of gold and convertible currency held by the official monetary institutions.
- Money supply. Notes and coin circulation, excluding cash holdings of monetary institutions. Sight deposits with credit institutions.

E. B.L.E.U.

Belgium

Economic growth continued in 1966, but the advance over the previous year was somewhat slower than it had been in 1965.

The slowdown was primarily due to the reduced pace at which exports expanded. Domestic demand, on the other hand, grew faster than from 1964 to 1965; this was largely attributable to a more rapid rise in the investment outlays for enterprises—mainly, it should be noted, of those enterprises owned by foreigners. The growth of private consumers' expenditure lost some of its momentum.

Although there was some further tendency for pressures on the labour market to ease, no real progress towards stability of prices and wage costs per unit of output was registered in 1966. The year-to-year increase in prices was even somewhat greater than from 1964 to 1965. In addition, there was a distinct deterioration of the current account in the balance of payments.

The trend of overall demand expected for 1967 means that real gross national product may quite possibly register the same rise as in 1966. The expansion of exports for the full year may be much the same as in 1966. While fairly vigorous stimuli may still come from gross fixed asset formation as well. The expansion of private consumers' expenditure is likely to continue losing something of its momentum, but the rate at which prices are increasing may also slacken slightly, so that the rise in the volume of consumption may be about the same as from 1965 to 1966.

As the outlook for prices and the current payments situation are still far from satisfactory, it would seem that those responsible for budget policy and credit policy will once again have to act with caution—at any rate there must be no policy of more general expansion. A reasonable amount of encouragement can none the less be given to investment, provided public and private saving is stepped up sufficiently.

1. Balance-sheet for 1966

The expansion of demand from abroad slackened considerably in 1966, so that for the full year the growth rate of exports was the lowest recorded for some years past. In part this was certainly due to the pattern of exports, particularly in view of the current situation on the world markets for iron and steel products. Moreover, the easing of the boom conditions in important neighbouring countries resulted in a decline in goods re-exported after processing, though the available statistics have overstated the decline. It

is also quite possible that the slower rate of growth reflects a weakening of Belgium's competitive position under the impact of more difficult conditions of competition.

Exports of goods to member countries showed a quite appreciable tendency to weaken, mainly owing to a decrease in exports to Germany, which was particularly pronounced in the second half of the year. Exports to non-member countries, on the other hand, again showed a slight increase, due especially to the vigour with which sales to the United States were rising. The foreign trade statistics show that visible exports in the third quarter were 4 % higher in value than a year earlier. As defined for the national accounts, they probably went up by 7.5 % in value and 7.0 % by volume for the full year of 1966, compared with an increase of 9.2 % and 8.4 % in 1965.

As exports of services continued to expand briskly the increase in total exports of goods and services for the year can be estimated at 8 % in terms of value and 7 % in terms of volume.

Unlike exports, domestic demand grew faster than between 1964 and 1965. Expansion is likely to have reached 9 % in terms of value.

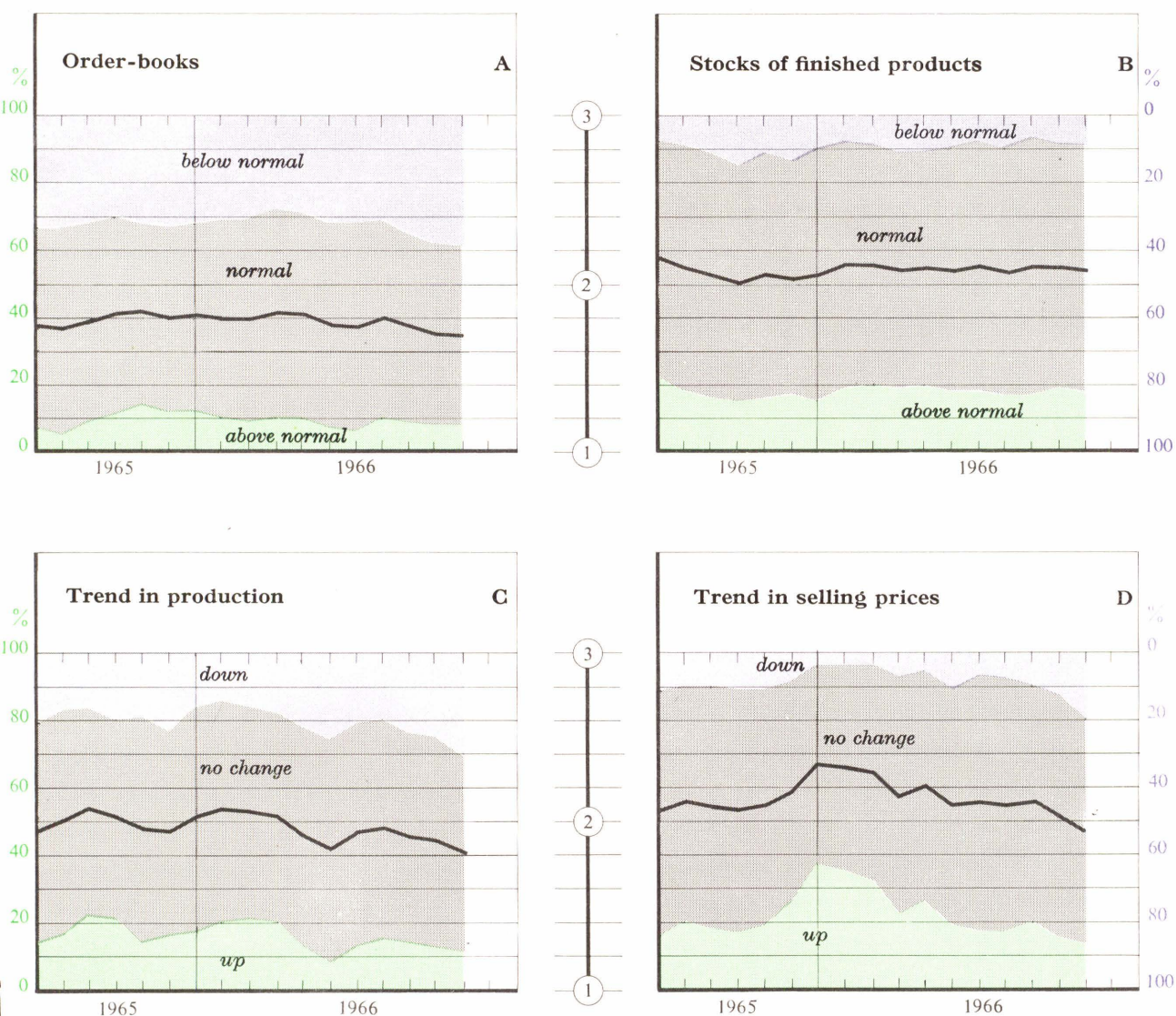
As for gross fixed asset formation, it must be pointed out that the increase from 1965 to 1966, at present estimated at 7.5 % (value) and 4 % (volume), has proved to be somewhat greater than originally predicted. This is almost exclusively due to a rather expansionary trend of investment by enterprises, which may have become even more pronounced in the second half of 1966. Investment by foreign enterprises, it is true, was the main factor contributing to this development, while investment in the more traditional sectors—apart from fuel and power—will scarcely have risen. As the year advanced neither the extent of utilization of production capacities nor profit margins developed in a way that could increase the propensity to invest of entrepreneurs. From 1965 to 1966 the overall increase in investment by enterprises will probably have reached 9.5 % in value and 6.0 % by volume.

Investment in housing, however, only rose slowly, at any rate when judged from the incomplete information available; while the number of building permits issued has been higher than in the previous year, the trend of actual expenditure in this sector of the building industry was affected during most of the year by a reduced number of starts registered in 1966.

Public expenditure on goods and services increased appreciably in spite of difficulties in obtaining finance and the consequent curtailment of both central government and local authority projects. The orders placed by central government authorities, especially those for road construction, continued to rise steadily as the year advanced.

Stockbuilding in industry has expanded faster than in 1965, despite the measures taken by the Bank of Belgium to limit the growth of the credits needed to finance these stocks. On the other hand, it is scarcely likely that there will have been any considerable rise in the volume of work in progress during the course of the year.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

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

The upward trend of total expenditure on consumption has fallen off, if only slightly. The expansion of public consumption seems however to have continued at an even faster pace than in 1965, mainly as a result of the system of sliding-wage scales and of the programme for raising public wages and salaries. In the aggregate, this form of expenditure was probably some 13 % higher than in 1965.

The growth of private consumers' expenditure, on the other hand, is likely to have slowed down a little in year-to-year terms; at the beginning of the year its rise had been affected by anticipatory purchases made as a result of the announcement in the fourth quarter of 1965 that there would be an increase in some indirect taxes. The incomes of households grew somewhat more slowly than in the previous year, largely because the rise in the wages bill for person in paid employment was some 9 % instead of the 10 % still recorded in 1965. The deceleration was particularly apparent in the second half of the year, when the effect of the sliding-wage scale was slighter. It seems too that the total number of hours worked ceased to rise in 1966. Transfer incomes, on the other hand, again went up appreciably, mainly owing to higher old-age pensions and family allowances. Moreover, the propensity to save of households appears to have risen somewhat in comparison with 1965. In the circumstances, the growth of private consumers' expenditure from 1965 to 1966 may be estimated at 7.5 % in value and 3.0 % by volume.

Owing to the slower expansion of overall demand, the growth of domestic supply gradually slackened as the year advanced.

The INS index of industrial production, adjusted for seasonal and fortuitous variations, even showed a decline for the third quarter compared with the first quarter of 1966; the unadjusted index was back to a mere 1.5 % above the figure reached a year earlier. For the full year the growth of industry's contribution to the national product may none the less be some 2 %, mainly thanks to higher production in the capital goods industry.

Building production was higher than in 1965, when it had fallen slightly below the level of the previous year. The growth of value added in agriculture can be estimated at some 2 %, but this did not make good the quite noticeable decline of a year earlier.

In the light of these developments in goods production, and assuming an increase of not less than 3.5 % in the value added by the services sector, the growth of real gross national product from 1965 to 1966 can be estimated at a good 3 %, or somewhat less than from 1964 to 1965 (3.3 %). As the rise in the overall price level has been somewhat more lively, the increase in terms of current prices may have been much the same as the 8 % registered in 1965.

The relatively slight growth of production coupled with faster advances in productivity led to a further easing of pressure on the labour market. This trend was strongly reinforced by the fact that the total number of hours worked fell in the sectors faced with structural difficulties. The unemployment rate, calculated on the basis of the civilian labour force and the number of applicants for jobs drawing unemployment benefit and

fully or partly capable of working, was 1.2 % at the end of October 1966, compared with 1 % at the end of October 1965. The average unemployment rate in 1966 was probably about 1.4 %.

Imports of goods and services expanded more slowly during the second half of the year, but their growth continued to be appreciably more vigorous than that of production; in view of the specially lively increase which lasted till the summer, their expansion for the full year may still in terms of volume have amounted to a good 9.5 %, compared with 7.8 % between 1964 and 1965.

Within this expansion, visible imports from other Community countries suffered from a slackening of temporary imports for processing traffic. Imports from non-member countries, on the other hand, continued to rise at a fairly rapid pace at any rate until autumn. Customs returns show that the value of goods imported in the third quarter was some 13.5 % higher than a year earlier. It may be assumed that for the full year 1966 visible imports, as defined for the national accounts, were 9.5 % (by volume) and 11.5 % (in value) higher than in 1965.

The continued lively upward movement of the general price level may have been due rather to the tendency for costs to rise than to the pressure of demand. Despite appreciable advances in productivity, wage costs per unit of output rose considerably further. In addition, the increase in prices paid for imports was distinctly greater than from 1964 to 1965, although world prices for raw materials developed more favourably as the year advanced.

The upward movement of wholesale prices for finished industrial products slackened somewhat in the course of the year, but the change was not reflected in retail prices. The retail price index continued to rise throughout the year, apart from a slight drop in July-August, due in part to seasonal variations and in part to the supply of some vegetable foodstuffs (particularly potatoes) being better than in 1965. The rate of rise seems however to have slackened after the summer, doubtless as a result of temporary measures taken to control the prices of goods and services. In October-November the index was 3.7 % higher than a year earlier. For the full year 1966, the upward movement of prices affecting private consumers' expenditure (as defined for the national accounts) is likely to have been almost 4.5 %, or about the same as in 1965.

As a result of the slower expansion of exports and the continued vigorous increase in imports, the trade balance showed a considerable deterioration. For the first nine months of 1966 it closed with a deficit of about Bfrs. 11 000 million (according to customs returns), in contrast to a surplus of slightly more than Bfrs. 2 000 million in the corresponding period of 1965.

The overall balance of payments for 1966 will probably close with a deficit (as against a surplus of Bfrs. 8 500 million in 1965). Not only is there a debit balance on current account (over Bfrs. 4 000 million for the first nine months of the year) due to the deterioration in the trade account and in certain items of the balance of services, but an

increase in the purchases of foreign securities by residents has led to a reduction in the surplus on private capital transactions, a surplus which has been mainly the result of direct investment by non-residents. In contrast to this, official capital transactions for the first nine months showed a smaller deficit than in the same period of 1965; net repayments of foreign debt were on a smaller scale. In the final quarter of the year there was even a slight surplus for some time, due to new short-term loans obtained by the Treasury abroad.

Demand for and supply of goods and services

	1964 ⁽¹⁾	1965 ⁽¹⁾		1966 ⁽²⁾		1967 ⁽³⁾
	At current prices (in Bfrs '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports ⁽⁴⁾	295.2	+ 8.5	+ 10.4	+ 7	+ 8	+ 7
Gross fixed asset formation	163.8	+ 1.4	+ 5.5	+ 4	+ 7.5	+ 5
Public current expenditure on goods services	98.1	+ 5.3	+ 9.6	+ 4	+ 13	+ 3
Private consumers' expenditure	507.1	+ 3.4	+ 8.1	+ 3	+ 7.5	+ 3
Gross national product	773.8	+ 3.3	+ 8.2	+ 3	+ 8	+ 3
Imports ⁽⁴⁾	295.0	+ 7.8	+ 7.9	+ 9.5	+ 11	+ 7.5

⁽¹⁾ Statistical Office of the European Communities, National Accounts 1955-1965.

⁽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.

In 1966, then, transactions with abroad exercised a restraining influence on the expansion of internal liquidity. This expansion has continued, largely as a result of transactions by the public authorities and of the increase in bank advances to trade and industry. Although the Treasury deficit for January-October was slightly less than in the corresponding period of 1965, there has been no appreciable reduction in the extent to which the total deficit on the various public budgets has been met by short-term borrowing. The increase in bank advances to business and private customers seems to have

slightly exceeded the limits fixed by the central bank in April, which incidentally were quite high; from the end of December 1965 to the end of September 1966 it amounted to almost Bfrs. 11 400 million, compared with Bfrs. 8 200 million in the corresponding period of the previous year.

The upward movement of interest rates continued both on the money market and on the capital market. This trend is only in part to be explained by the increase of interest rates abroad : the money market in particular suffered also from the deterioration in the balance of payments. But more important still, the demand for capital, both from the business sector and from the public authorities, rose faster than the supply of private savings.

2. Outlook for 1967

According to the present state of the forecasts, which are naturally still by no means firm, the growth of overall demand can be expected to continue in 1967 at much the same rate as in 1966.

Several factors indicate that exports of goods and services will expand at about the same pace as in 1966.

There is little likelihood of the upward movement of visible exports to other Community countries being more dynamic than in 1966, particularly as the expansion of demand for imports in the Netherlands will probably slacken and business activity in Germany is weakening; however, as the year advances Germany may once again provide somewhat more vigorous stimuli. Nor will there be any important change in the growth of exports to non-member countries. The development of sales to the United Kingdom will probably slow down, and though exports to the United States may continue their lively rise, this is unlikely to be as pronounced as from 1965 to 1966. On the other hand exports to the remaining non-member countries, and in particular to developing countries, may be expected to grow considerably.

It is, however, far from certain that the weakening in the expansion of demand from the main importing countries can be fully offset by an increase in Belgium's share of sales on export markets, despite the considerable production capacity available and the support measures that have been adopted to assist with the financing of exports. The benefit to be derived from these developments may be impaired by the trend of prices and costs, which has in the past few years been less favourable for Belgium than for its main competitors, and by changes in the pattern of world demand.

In view of this outlook for visible exports, and on the assumption that both earnings from services and factor income will rise rather more weakly than in 1966, it seems reasonable to forecast that in 1967 total exports of goods and services (as defined for the national accounts) will be 8 % in value and 7 % by volume higher than in 1966.

Domestic demand in money terms is likely to continue its vigorous expansion in 1967.

It can be expected that the rise in expenditure on gross fixed asset formation will be at least as appreciable as in 1966. Investment by enterprises should show a steady expansion, mainly as a consequence of the projects being executed by foreign enterprises. In this sector there might, however, be some slackening in the second half of the year, as large new projects were started on a more limited scale in 1966. Investment in the traditional sectors can be expected to increase only slightly, in view of the outlook for overall demand and of the recent and foreseeable trend of profit margins; any upward movement would be due in the main to measures of support taken by the public authorities.

As far as housing is concerned, the trend in the number of dwellings started during the past few months and the objectives of the policy pursued in the field of publicly assisted residential building suggest that in 1967 growth will be somewhat more vigorous than in 1966. Lastly, it would seem, particularly in the light of the forecasts submitted with the budget estimates, that public investment will show a further sharp expansion. However, these forecasts are based on the rather unsafe assumption of an improvement in the terms for obtaining finance—and this would have in large measure to be the result of increased saving by the public authorities themselves.

In the aggregate, then, gross fixed asset formation in 1967 may be about 8 % in value and 5 % by volume higher than in 1966.

Neither the probable trend of production nor the expected movements in world prices will exert any great influence on stockbuilding.

Several factors—including the Government's efforts to balance the ordinary budget—suggest a less brisk growth of public consumption in 1967. The expansion of public spending on goods and services may be slightly below that in 1966, in spite of the effects of the programme for raising wages and salaries and the increased number of persons employed in public service; at present this increase is estimated at some 10 %.

The increase in incomes of households will certainly be influenced by some slackening in the growth of the total wages bill. This assumption takes into account the slackening of the rise in agreed wage rates that should ensue from the tendency for the situation on the labour market to ease; at the same time it reflects the belief that the impact on wages of the sliding-scale system will ease somewhat, in consequence of a certain slackening in the upward trend of consumer prices. Be all that as it may, the rise in gross wages and salaries per person employed in 1967 is likely to be about 7.5 %.

The total number of hours worked will probably not go up notably, as the expansion of domestic production that has been forecast will be accounted for mainly by advances in productivity. Moreover, it would seem that, despite the social measures the Government plans to put through in 1967, there can be no question of transfer incomes rising

more rapidly in 1967 than in 1966. Finally, the incomes derived by individuals from property and self-employment may increase only slowly. Provided these assumptions prove to be correct and the savings ratio does not change appreciably, private consumers' expenditure in 1967 may be expected to expand by almost 7 %. As a result of a slight slackening in the upward movement of prices, the increase by volume will probably remain practically unchanged at some 3 %.

In view of the developments expected in overall demand, production should grow further; as in 1966, however, its growth may well be relatively moderate. Industrial production—value added at constant prices—will probably expand at about the same rate as in 1966 (some 2 %); here the new capacity coming into production, mainly in the iron and steel industry and in the motor industry, will provide an important element of support. The output of building and construction should rise faster than in 1966, mainly as a result of the more expansionary trend expected in the demand for public works and for housing. With output in the services sector likely to increase on more or less the same scale as in 1966, the real gross national product may go up by fully 3 %.

The reduction in the pace at which stocks of raw materials and semi-manufactures are being built up may slow down the expansion of imports, though it may not be very noticeable till the second half of the year, when purchases of plant and equipment will also start to slow down.

Imports of goods and services are at present expected to rise in 1967 by about 7.5 % (volume). Import prices may display a slight upward trend. On the whole, import values may rise somewhat less rapidly than in the preceding year, but the deficit on current account might none the less be as heavy as in 1966.

The prospects for domestic production suggest that there should be a further tendency for pressures on the labour market to ease. The growth of the national product forecast for 1967 may very possibly be accompanied by stagnation in employment. If in addition it is assumed that there will be no change in the agreed length of the working week, the unemployment rate can be expected to rise slightly to an annual average distinctly in excess of 1.5 %.

This is one of the reasons why a slight slackening in the upward movement of prices can be expected during 1967 and the total rise for the year should be slightly lower than in 1966. The increase in wage costs per unit of output may be somewhat less rapid, and there is at the moment no reason to expect for 1967 any special factors of the kind which led to a higher price level in 1966, such as the increase in indirect taxes or the particularly heavy rise that occurred in certain food prices. It must not however be forgotten that at the beginning of 1967 certain delayed price increases may be put through if the present sharper price control is relaxed and certain public service charges are raised. The forecast increase of 3.5 % in consumer prices is in any case still fairly high.

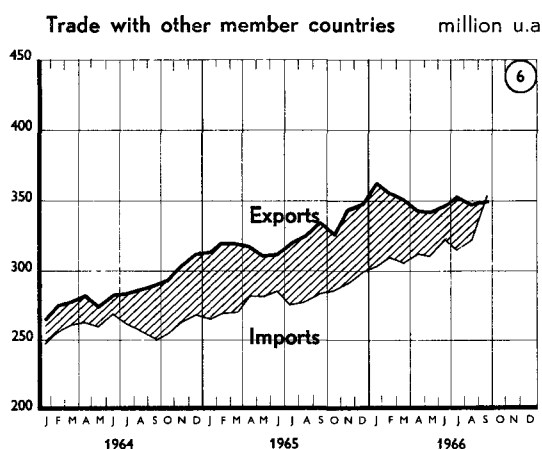
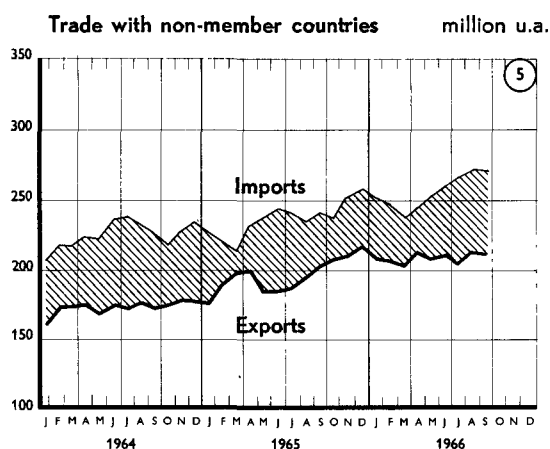
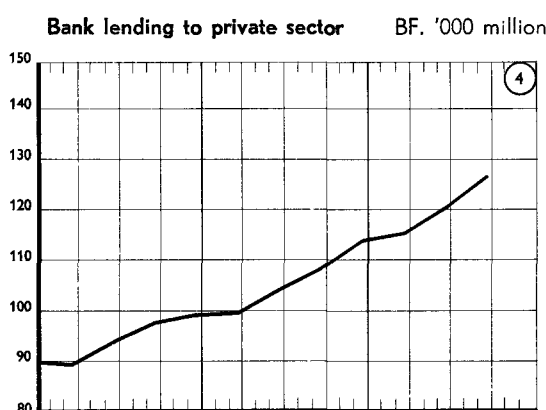
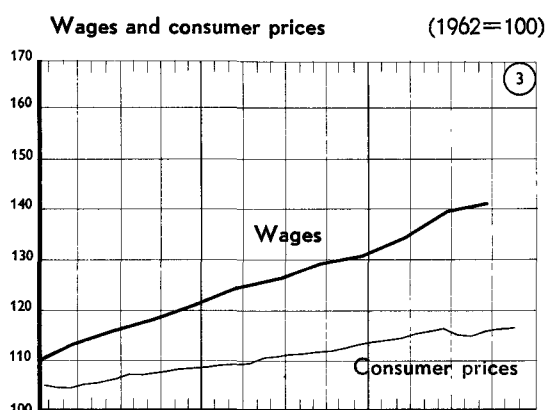
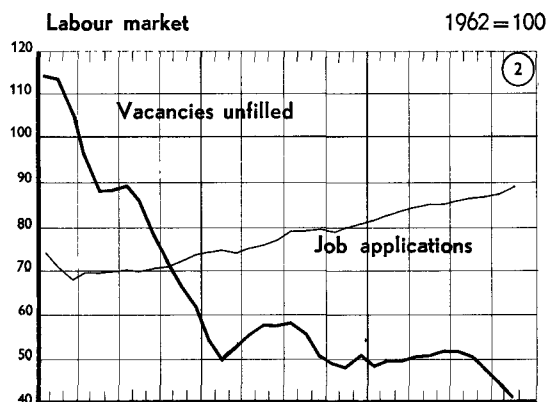
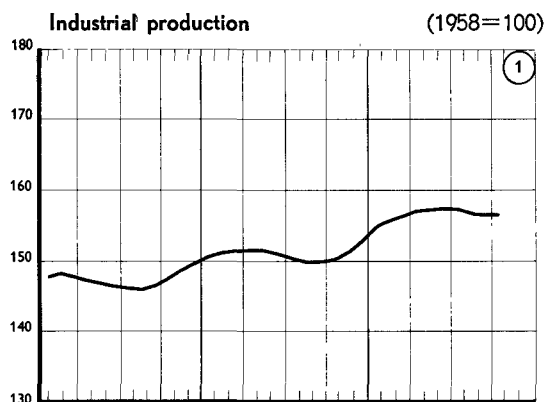
In these circumstances, and even though the prospects outlined above suggest that the expansion of overall demand in money terms will not gather momentum, it

would still be premature to return to a decidedly expansionary line of policy. It is still most important that more should be done to keep down prices and wage costs per unit of output. If the expansion in domestic demand in money terms were to accelerate again too early, the tendency for the situation on the labour market to improve and for costs and prices to ease could soon give way to fresh strains. Besides, the unsatisfactory state of the current balance of payments is an argument against an expansionary economic policy and very much in support of a careful control over the increase in domestic demand.

It must, however, be pointed out that budget policy in Belgium certainly does not go far enough in this direction. On the contrary, the misgivings expressed in the last Quarterly Survey concerning the trend of public revenue and expenditure seem to be even more justified in the light of recent changes in the outlook. It seems, for instance, increasingly probable that the rise in revenue has been overestimated and, more important, recent information suggest that the estimates of ordinary expenditure for 1967 will be exceeded as the year advances, mainly as a result of the insufficiency of the action taken to place the financial operation of certain semi-official institutions on a sound footing. This could appreciably impede the requisite expansion of public saving, and so either adversely affect both public investment and the promotion of investment by enterprises, or cause the Government to resort once more to short-term borrowing to cover its investment programme.

Every possible effort should, on the contrary, be made to contain the expansion of current expenditure and, thanks to the resultant improvement in the balance of the ordinary budgets of public administrations, to bring the deficits below the level of the previous year; this would reduce the upward pressures on prices, since short-term borrowing would be avoided, and would lead to an increase in public saving. It is evident that more funds from private saving would then be left for the financing of investment by private enterprises. It would at the same time obviate the possibility that, with price and cost increase persistently higher than is acceptable and a risk of sizeable deficits on the current payments account, credit policy would have to be so restrictive that it would considerably impede the expansion of fixed investment by industry.

ECONOMIC INDICATORS



NOTES:

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

Graph 1. Trend curve; estimation established on the basis of indices adjusted by the SOEC for seasonal and fortuitous variations (excluding construction, food, beverages and tobacco).

Graph 2. Completely unemployed persons, receiving unemployment benefit. Adjusted for seasonal variations. Three-months moving average.

Graph 3. General index of retail prices. Source: Ministère des Affaires Economiques. Agreed wages for operatives, all branches; source: Ministère du Travail et de l'Emploi.

Graph 4. Short-term loans made by monetary institutions.

Graphs 5 and 6. B.L.E.U., series adjusted for seasonal and accidental variations (moving averages of 3 months). Exports fob, imports cif. Conversion at official exchange rates. 1 unit of account = 0.888671 gm. of fine gold = US \$1 at the official rate of exchange.

Belgium

TABLE 1: Basic data (1965)

Total area ('000 sq. km.)	30.5
Total population ('000)	9 464
Density of population per sq. km.	310
Working population ('000)	3 765
Working population, breakdown by main sector (%)	
— Agriculture	5
— Industry	42
of which : Construction	8
— Services	53
Percentage share of gross domestic product :	
— Agriculture	6.2
— Industry	41.7
of which : Construction	6.9
— Services	52.1
Gross product per capita (Bfrs.)	88 400

TABLE 2: Development of basic economic data

	% change by volume on preceding year							Volume indices (1958 = 100)	Contri- bution (in %) to GNP
	1959	1960	1961	1962	1963	1964	1965		
Gross national product	+ 2.6	+ 5.6	+ 4.7	+ 5.5	+ 4.6	+ 6.6	+ 3.3	138	—
Industrial production	+ 4.2	+ 8.5	+ 4.7	+ 7.6	+ 4.9	+10.8	+ 2.3		
Total imports	+12.2	+12.4	+ 7.0	+ 6.8	+ 8.0	+11.1	+ 7.8	186	38.0
Private consumers' expenditure	+ 2.0	+ 6.0	+ 2.2	+ 4.8	+ 5.3	+ 3.9	+ 3.4	131	65.5
Public current expenditure on goods and services	+ 5.3	+ 5.4	+ 1.6	+ 9.1	+11.5	+ 4.2	+ 5.3	151	12.8
Gross fixed asset formation	+ 8.8	+12.6	+10.7	+ 5.8	- 1.0	+12.8	+ 1.4	162	20.7
Total exports	+ 7.2	+ 9.6	+ 8.3	+ 7.6	+ 7.3	+12.5	+ 8.5	179	38.9
Gross national product per capita	+ 2.1	+ 5.1	+ 4.2	+ 4.8	+ 3.8	+ 5.7	+ 2.3	132	—
Gross national product per person gainfully employed	+ 2.8	+ 5.7	+ 4.3	+ 4.2	+ 4.1	+ 5.7	+ 2.2	133	—

TABLE 3: Foreign trade (at current prices)

	% change on preceding year							Indices (1958 = 100)	Million u.a.	% of the total
	1959	1960	1961	1962	1963	1964	1965			
Visible exports										
Total	+ 7.9	+14.7	+ 3.9	+10.2	+11.9	+15.5	+14.2	209	6 382	100
Intra-EEC	+10.5	+25.2	+ 9.7	+17.7	+19.6	+19.0	+12.8	287	3 947	61.8
To non-EEC countries	+ 5.7	+ 5.3	- 1.7	+ 1.9	+ 1.6	+10.3	+16.5	145	2 435	38.2
Exports of food, beverages and tobacco										
Total	+ 0.5	+ 6.3	+15.6	+29.6	+29.6	+ 3.2	+31.5	281	430	6.7
Intra-EEC	+14.8	+11.8	+18.7	+31.2	+30.7	+ 5.2	+31.6	361	318	5.0
To non-EEC countries	-18.9	- 4.4	+ 8.7	+25.7	+26.8	- 2.1	+31.3	174	112	1.7
Exports of raw materials and manufactures										
Total	+ 8.4	+14.9	+ 3.4	+ 9.2	+10.9	+16.4	+13.1	205	5 952	93.3
Intra-EEC	+10.4	+26.1	+ 8.9	+16.7	+18.8	+20.1	+11.4	281	3 630	56.9
To non-EEC countries	+ 6.9	+ 5.6	- 2.0	+ 0.9	+ 0.7	+10.8	+15.8	144	2 322	36.4
Visible imports										
Total	+ 9.8	+15.0	+ 6.6	+ 8.0	+12.2	+15.9	+ 7.6	203	6 373	100
Intra-EEC	+10.9	+16.8	+12.7	+ 8.9	+15.5	+17.5	+10.1	238	3 473	54.5
From non-EEC countries	+ 8.8	+13.3	+ 1.0	+ 7.1	+ 8.8	+14.0	+ 4.8	173	2 900	45.5
Imports of food, beverages and tobacco										
Total	+ 6.6	+ 1.6	+ 0.1	+11.0	+ 9.0	+16.8	+15.2	176	826	13.0
Intra-EEC	+13.2	+ 4.2	+ 7.4	+ 3.2	+17.2	+16.3	+22.5	217	339	5.3
From non-EEC countries	+ 3.4	+ 0.1	- 4.0	+15.9	+ 4.3	+17.2	+10.6	156	487	7.7
Imports of raw materials and manufactures										
Total	+10.4	+17.1	+ 7.6	+ 7.6	+12.7	+15.7	+ 6.6	208	5 548	87.0
Intra-EEC	+10.6	+13.4	+13.3	+ 9.4	+15.4	+17.6	+ 8.9	240	3 134	49.2
From non-EEC countries	+10.2	+15.9	+ 1.9	+ 5.6	+ 9.6	+13.4	+ 3.7	177	2 414	37.8

TABLE 4: Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1958 = 100)	1964	141	138	144	151	137	149	127	136	151	161	148	150
	1965	141	140	156	151	145	149	124	140	156	160	150	159
	1966	145	145	160	152	146	158	118	147	162	156		
Investment (1961 = 100)	1964	112.4	127.4	134.7	145.7	148.0	145.6	121.1	128.3	141.9	137.7	152.9	145.5
	1965	116.7	121.4	135.9	156.6	155.0	159.7	113.2	144.6	146.7	152.1	139.6	154.9
	1966	106.7	141.0	154.7	155.1	165.9	170.0						
Building (1962 = 100)	1964	92.8	108.2	109.5	124.5	112.6	126.0	99.0	111.0	125.2	125.9	116.2	103.9
	1965	86.3	82.1	107.0	117.5	111.4	121.4	79.9	116.8	121.4	120.5	96.9	102.3
	1966	68.1	97.3	117.6	108.8	106.9	118.9	71.1	117.8	122.6	112.7		
Private consumers' expenditure (1961 = 100)	1964	117.0	116.4	118.7	122.2	124.4	124.6	125.7	123.7	121.9	124.1	125.5	128.1
	1965	126.1	126.4	131.2	134.5	137.0	135.3	134.9	133.0	133.0	135.8	136.8	141.8
	1966	135.2	136.0	138.9	145.3	141.7	145.1	143.6	141.2				
Total visible imports (million u.a.)	1964	492	475	481	515	479	513	486	419	480	512	491	536
	1965	455	477	547	552	514	518	505	454	553	554	570	609
	1966	500	547	607	555	583	607	520	593	601			
Total visible exports (million u.a.)	1964	451	449	468	490	426	484	453	377	477	520	491	502
	1965	482	519	571	507	484	551	513	432	586	546	575	617
	1966	503	523	629	562	537	621	514	475	606	575		
Balance of trade (million u.a.)	1964	- 41	- 26	- 13	- 23	- 53	- 28	- 33	- 42	- 3	- 8	- 0	- 34
	1965	+ 27	+ 43	+ 24	- 45	- 31	+ 34	+ 8	- 21	+ 33	- 8	+ 5	- 8
	1966	+ 4	- 19	+ 22	+ 6	- 47	+ 14	- 6	- 118	+ 5			
Official gold and foreign exchange reserves (million u.a.)	1964	1 796	1 794	1 795	1 789	1 812	1 788	1 796	1 816	1 834	1 870	1 954	1 992
	1965	2 000	2 006	2 002	2 026	2 010	2 000	2 010	2 028	2 018	2 010	2 010	1 996
	1966	1 968	1 946	1 956	1 954	1 950	1 950	1 964	1 956	1 926	(1 980)	(1 962)	
Money supply	1964	271.2	270.1	274.3	276.1	282.0	287.1	282.7	282.2	285.1	286.4	285.2	298.7
	1965	290.4	290.4	294.2	300.3	303.0	310.6	306.3	303.2	307.9	308.6	310.4	320.0
	1966	311.3	303.5	316.0	321.0	325.2	331.2	330.7	325.7	324.1	325.1		

() Provisional figures.

Belgium

NOTES

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

Table 1

- Total population at mid-year.
- Working population in employment, average for year.
- Breakdown of gross domestic product by factor cost.
- GNP at market prices.

Table 2

- GNP at market prices.
- Industrial production : value added by industry.
- Total exports and imports : goods, services and factor income.

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 and manufactures (groups 2-9 CST).

Table 4

- Industrial production. Source : Institut National de Statistique (INS). General index.
- Investment. Source : Département de l'économie appliquée de l'Université libre de Bruxelles (DULBEA). Current prices.
- Construction. Source : INS. Index based on number of man-hours worked.
- Private consumption. Source : DULBEA. Current prices.
- Exports fob, imports cif. Conversion at official exchange rates.
- Official gold and foreign exchange reserves. Gross reserves of gold and convertible currency of the official monetary institutions.
- Money supply. Notes and coin circulation, excluding cash holdings of the Treasury, the Central Bank and other banking institutions other than the Postal Cheque Office. Residents' sight deposits (up to one month) with banking institutions. Holdings of the special agencies of the Treasury and non-residents' holdings on postal cheque accounts.

Grand Duchy of Luxembourg

Since 1964 the economic situation in Luxembourg has been marked by a decline in the level of activity in the steel industry. Although this trend has been less pronounced since the middle of 1966 and new industries have contributed to economic growth as the year advanced, the rate of expansion in 1966 will have been only slightly higher than in 1965. The rise in real gross national product may have been little more than 2 %, compared with some 1.5 % in 1965.

In spite of the relatively slow tempo at which demand and business activity have expanded, the balance of the economy did not improve in 1966. The situation of over-employment continued on the labour market, and the strains affecting the money and capital market grew more serious, mainly because of the increased calls made on it by the public authorities; the rise in prices and unit costs was hardly any less than in 1965.

On the basis of trends as they appear today and the assumption that in 1967 average exports of iron and steel products will remain as they were in 1966, the real gross national product should expand slightly faster. The main elements in this expansion will no doubt be the exports of the new industries, the growth of public expenditure and a sustained increase in private consumers' expenditure.

The upward movement of prices that is likely to go with this trend will probably still be strong. Those responsible for economic policy will again have to do everything in their power to secure sufficient and balanced economic growth; consequently they will have to aim at reducing the scale of price and cost increases and to ensure that a growing volume of investment is financed out of domestic saving.

1. Balance-sheet for 1966

Following a marked slowdown in 1965, the growth of exports of goods and services again slackened slightly in 1966. The main reason for this development is that foreign demand for Luxembourg's iron and steel products has persistently tended to weaken since the middle of 1964. Yet as a result of the appreciable stimulus provided by exports of the most important of the new industries and by the further rise in exports of services, the growth of total exports in real terms can be estimated at some 3.5 %—a figure which must however be compared with the 4.5 % achieved in 1965. As in the previous year, there was a slight decline in the level of export prices, due mainly to the continued easing in the average prices for iron and steel over the year.

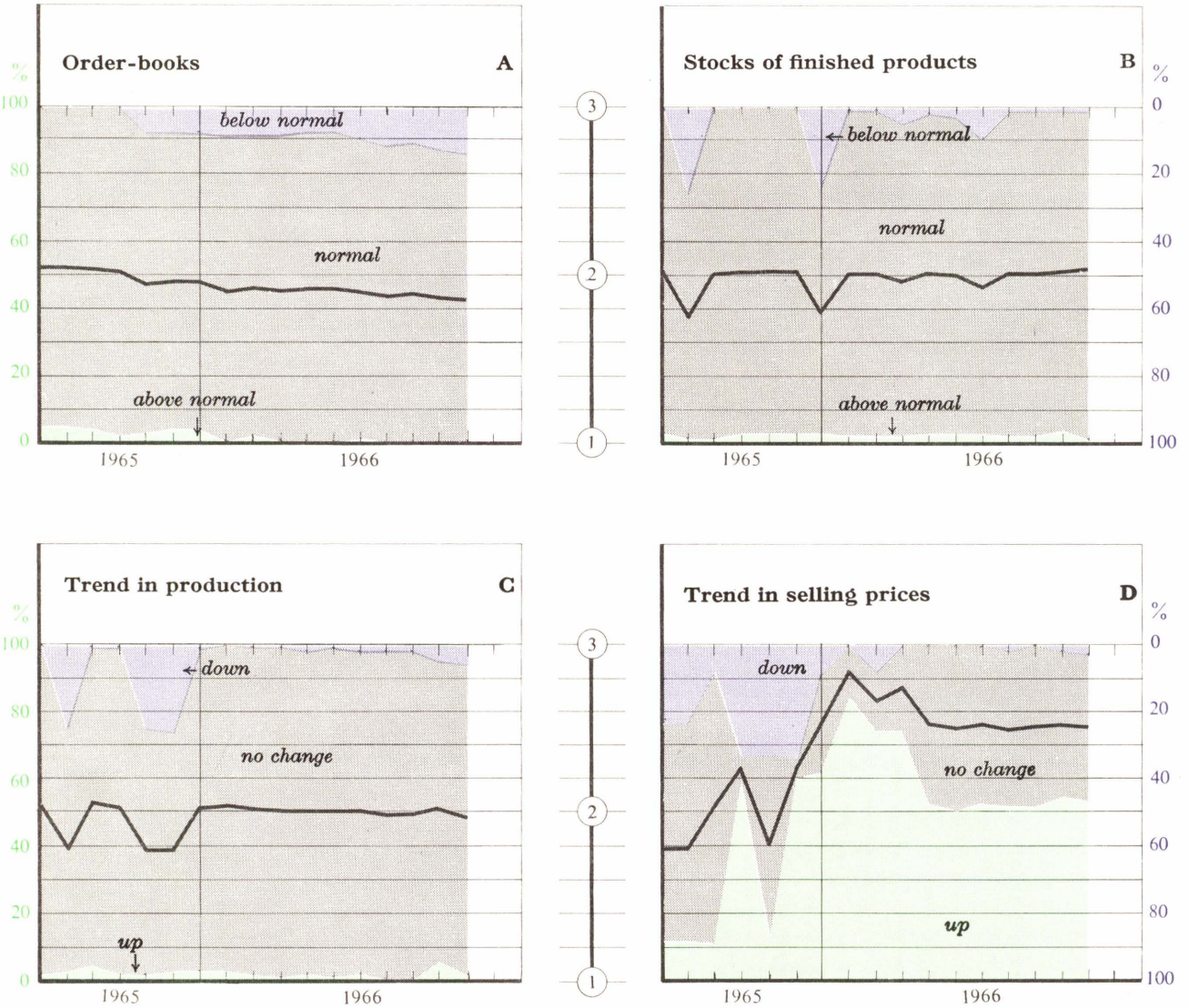
The expansion of domestic demand from final consumers, however, may have been slightly more pronounced than in 1965. On the one hand, gross fixed asset formation appears to have dropped distinctly less. In this context, the investment expenditure of the public authorities, particularly of the central government, played an important role: after decreasing slightly from 1964 to 1965, it went up again in 1966, when its growth in terms of value was probably more than 15 %. Expenditure on housing, however, is likely to have shown only a very slight increase, owing in the main to the stricter terms on which finance has been available from the State savings bank. In addition, expenditure on industrial investment continued to fall, both in the traditional sectors and among foreign enterprises. All in all, expenditure on gross fixed asset formation may have dropped by some 3.5 % (about 6.5 % in terms of volume), compared with a drop of 16 % (18 % by volume) from 1964 to 1965.

The expansion of overall expenditure on consumption, on the other hand, was more vigorous than in 1965, mainly as a result of a faster increase in public spending on goods and services. This rather rapid rise in public outlay was due not only to higher wages and salaries per person employed in the public sector and to the greater number of public servants, but also to an increase both in the volume of goods and services purchased and in their prices, which rose perceptibly.

Private consumers' expenditure continued to grow at a relatively fast pace. In spite of the tendency for business activity to level off, the disposable income of households went up about as fast as in 1965. In this connection, special importance attaches to the appreciable wage increases under the law of 12 June 1965, particularly for night work and for women workers; the impact of this law may have largely offset the definite slackening in the upward trend of the earnings of industrial workers. A perceptibly faster rise in transfer incomes was a further important factor that caused the growth in disposable incomes of households to be about as rapid as in 1965. In these circumstances private consumers' expenditure may again have expanded by almost 7 % in value and about 3 % by volume.

The very modest progress of overall demand and its pattern are the chief reasons why the expansion of domestic supply was very limited. The official index of industrial production may reveal a drop of over 3 % from 1965 to 1966. However, it must be borne in mind that this index does not yet record the rather favourable developments occurring in certain new industries, especially in chemicals. In the aggregate, industrial production for the year may have been slightly higher than in 1965, particularly because in the last months of the year the trend was somewhat more favourable—the main reason being that production in the iron and steel industry was no longer declining. In the third quarter of 1966 the official index was only 3.2 % lower than in the corresponding period of the previous year, compared with 3.9 % and 4 % in the first and second quarters. There was little change during the year in the adjusted figures for building and construction, so that output for the year will have been much the same as in 1965. Agricultural production, however, may have continued to rise slightly.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



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

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

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

After due allowance has been made for numerous uncertainties in the statistics, particularly with regard to value added in the services sector, it still seems that the growth of the real gross national product should be almost 2 %, compared with some 1.5 % in 1965.

Despite the sluggishness of overall demand, the trend of imports showed a slight rise caused by the recovery in purchases of consumer durables. Imports of plant and machinery are also likely to have been distinctly smaller than in 1965. The price of imports continued to rise, perhaps somewhat faster than before.

Demand for and supply of goods and services

	1964 ⁽¹⁾	1965 ⁽²⁾		1966 ⁽²⁾		1967 ⁽³⁾
	At current prices (in Lfrs million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports ⁽⁴⁾	25 616	+ 4.5	+ 3	+ 3.5	+ 3	+ 4.5
Gross fixed asset formation	9 493	— 18	— 16	— 6.5	— 3.5	0
Public current expenditure on goods and services	3 689	0	+ 6	+ 2.5	+ 9	+ 2
Private consumers' expenditure	18 209	+ 3	+ 7	+ 3	+ 7	+ 2.5
Gross national product	30 449	+ 1.5	+ 3	+ 2	+ 4	+ 2.5
Imports ⁽⁴⁾	26 558	— 0.5	+ 0.5	+ 2	+ 4	+ 3

⁽¹⁾ Statistical Office of the European Communities, National Accounts 1955-1965.

⁽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.

The higher cost of imports and the fact that wage rises continued to exceed the advance in productivity were in large measure responsible for the persistence of the upward trend in prices. Nevertheless, the official cost-of-living index rose at a slower pace than before (an estimated 2.6 in 1966, compared with 3.3 % in 1965), the index having overstressed the influence of food prices, which rose more slowly than in 1965 mainly because the reductions made in agricultural subsidies have been on a smaller scale.

The labour market still suffered from over-employment despite a slight decrease in the numbers employed in the iron and steel industry and in mining. Most important among the reasons contributing to this situation were the special requirements of the new enterprises, the insufficient occupational mobility of workers and the shortening of the working week under collective agreements.

There was a distinct increase in interest rates on the money and capital markets, due mainly to the appreciable increase in borrowing by the public authorities and non-residents. By the end of September 1966 government issues totalled Lfrs. 1 100 million, compared with Lfrs. 800 million for the full year 1965.

2. Outlook for 1967

Several factors in both demand from abroad and domestic demand seem to indicate that in 1967 overall demand and the gross national product will show a somewhat more vigorous expansion.

Especially in the light of the latest developments in the flow of orders received, particularly orders from non-member countries, the downward trend of iron and steel production may perhaps come to a halt in 1967. In addition, the exports of other branches will probably continue to rise, although deliveries by the new industries may grow less appreciably than in 1966. Lastly, a slight increase in export prices can be assumed. All in all, exports of goods and services may rise some 4.5 % by volume.

After declining for the past two years, gross fixed asset formation may now remain at the same level, at least in terms of value if not of volume. The expansion of public investment will be more modest than from 1965 to 1966, but it should be sufficient to offset a slight decrease in expenditure on investment by the private sector. Although enterprises in the iron and steel industry will make appreciable cuts in their outlay on extensions, they will continue their efforts towards further rationalization. If there is no major new expenditure on investment by foreign firms, the situation in the other branches of industry is likely to be stable, while outlay on housing may remain at the level reached in 1966.

All this suggests that the level of business activity will certainly remain fairly high and may consequently underpin developments in the incomes of households and of private consumers' expenditure, which will also benefit considerably from the expected growth of transfer incomes. This expectation is justified not only by the budget estimates but also by the law on the reform of old age pensions which is due to come into force during the next few months with retroactive effect from January 1966. Despite this, the total wages bill, will probably rise rather less than before; one factor contributing to this change is that the sliding wage scale may have a somewhat smaller impact than in 1966. Private consumers' expenditure should therefore expand slightly less than in 1966.

The outlook for overall demand and its different components suggests, then, that from 1966 to 1967 the growth of industrial production (value added at constant prices) can be estimated at some 2 %, that of the real gross national product at about 2.5 %. It can also be expected that imports of goods and services will rise slightly faster.

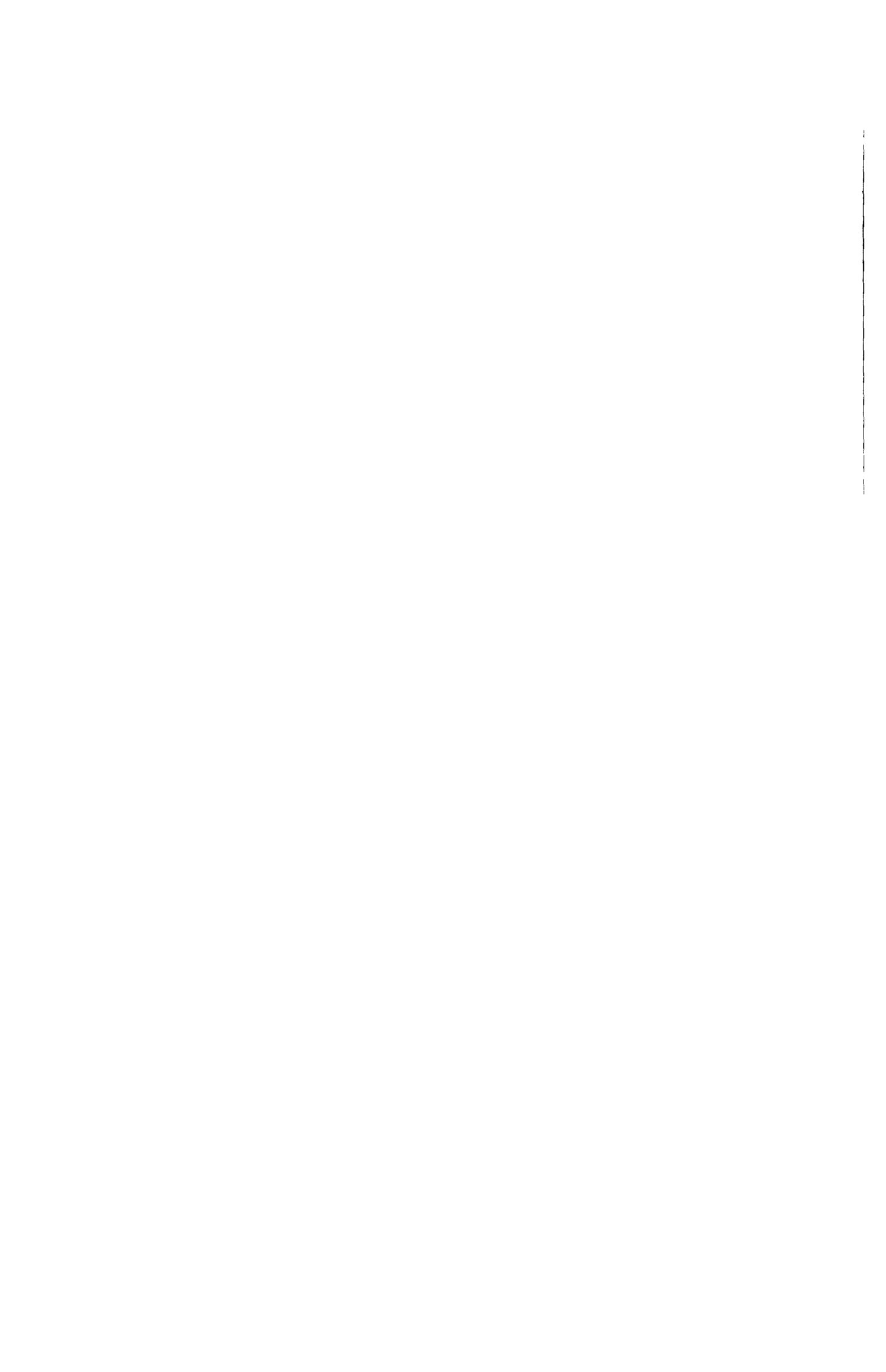
The situation on the labour market will probably not change greatly, as the expansion of domestic production is unlikely to exceed what can be covered by advances in productivity.

The upward trend of prices will probably not slacken appreciably during 1967. There is unlikely to be any considerable change in most of the factors which exercised a major influence during 1966—particularly in the trend of wage costs per unit of output. The weakening that is expected to occur in the upward trend of import prices will be only partially reflected in domestic prices, and only with a certain time-lag. In addition, the policy of reducing agricultural subsidies will probably affect consumer prices for foodstuffs more than in 1966.

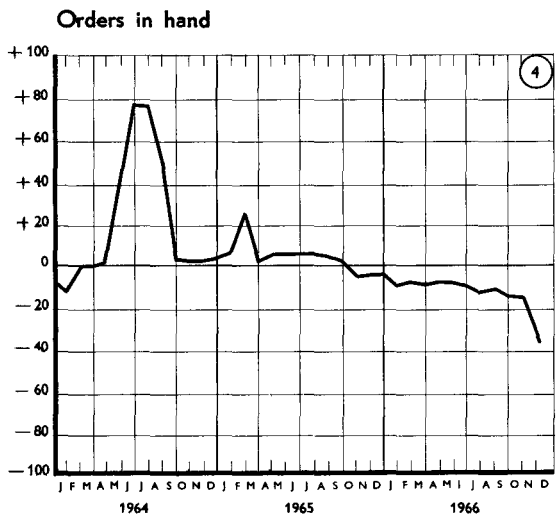
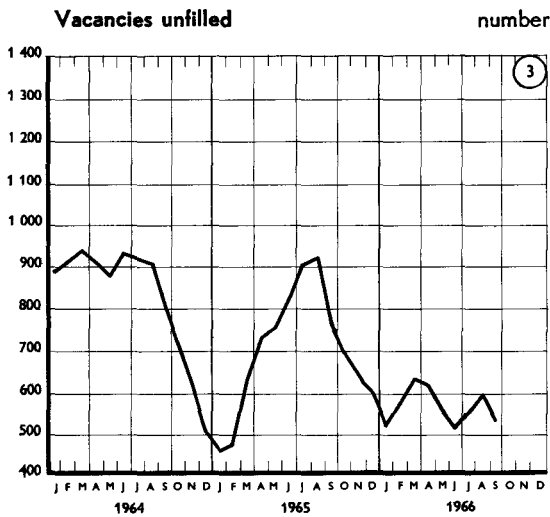
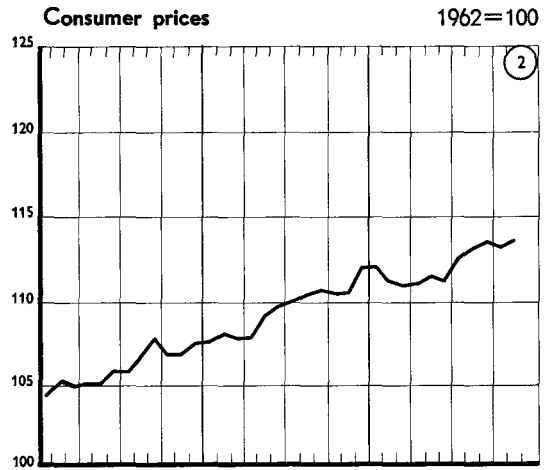
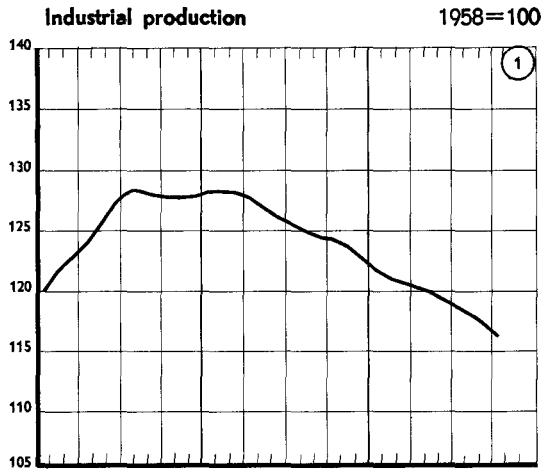
If, then, the prospects of growth in 1967 are perhaps slightly better than in 1966, the same cannot be said of the attempts to stabilize prices and unit costs.

Consequently, short-term economic policy should seek to eliminate internal imbalances and so to improve the conditions of growth whatever may be the importance to be attached to “imported inflation” brought in on the back of import prices—and it certainly is considerable in the case of the Grand Duchy of Luxembourg—the fact remains that the influence of internal factors tending to force up prices and costs should be brought under the strictest possible control by the vigorous use of all available instruments. Here, budget policy ought to play an important role. As part of the “pre-austerity” policy announced by the Government, the estimates for non-investment expenditure given in the draft budget for 1967 should on no account be exceeded. As it is, the total government expenditure shown in the estimates is 7.5 % higher than in the estimates for 1966. The forecast deficit is already so heavy that it probably cannot be covered entirely out of domestic saving. In the circumstances, and in view of the element of uncertainty in the estimated revenue from taxation, the question arises whether the authorities ought not to try to prune the expansion of government expenditure planned for 1967.

It seems, too, that greater restraint in the field of public finances will be necessary if the amount of savings available for financing investment by enterprises is to be increased. Firms have in fact to face a continued increase in wage costs per unit of output. In view of the need to ensure sufficient economic growth and of the practical difficulties of gearing an incomes policy more closely to developments in the economic situation, it seems important that more effective support should be given to industry's struggle against the upward thrust of unit costs.



ECONOMIC INDICATORS



NOTES:

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

Graph 1. Trend curve; estimation established on the basis of indices adjusted by the SOEC for seasonal and fortuitous variations (excluding construction, food, beverages and tobacco).

Graph 2. Source: STATEC. General cost-of-living index.

Graph 3. Index adjusted for seasonal variations. Moving averages of 3 months.

Graph 4. Source: EEC business survey.

Grand Duchy of Luxembourg

TABLE 1: Basic data (1965)

Total area ('000 sq. km.)	2.6
Total population ('000)	332
Density of population per sq. km.	128
Working population ('000)	139
Working population, breakdown by main sector (%):	
— Agriculture	13
— Industry	46
— Services	41
Percentage share of gross domestic product in 1963	
— Agriculture	7.0
— Industry	53.0
— Services	40.0

TABLE 2: Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1958 = 100)	1964	115	117	125	129	131	130	123	122	126	127	125	124
	1965	125	129	121	130	132	129	124	116	125	125	127	121
	1966	120	121	119	122	125	124	119	111	119			
Crude steel production ('000 m.t.)	1964	356	357	375	402	372	389	396	365	391	412	361	383
	1965	333	379	338	392	391	377	397	353	395	392	377	372
	1966	369	354	330	367	353	369	368	346	377	383	365	
Building (1958 = 100)	1964	48	57	83	103	106	109	110	96	98	95	73	63
	1965	48	55	82	103	110	102	105	100	96	93	76	58
	1966	45	53	91	99	101	101	96	95	94	87		
Workers employed in the iron and steel producing industry and in mining ('000)	1964	23.5	23.6	23.7	23.9	24.0	24.0	24.1	24.1	24.2	24.2	24.3	24.3
	1965	24.2	24.1	24.0	24.0	24.0	24.0	24.0	24.0	24.1	24.1	24.1	24.1
	1966	24.0	24.0	23.8	23.8	23.8	23.7	23.7	23.7	23.8	23.7	23.6	
Retail prices (1958 = 100)	1964	106.8	107.6	107.2	107.4	107.5	108.3	108.3	109.2	110.3	109.3	109.3	109.9
	1965	110.2	110.5	110.3	110.3	111.6	112.3	112.6	113.0	113.2	112.9	113.1	114.7
	1966	114.7	113.8	113.4	113.6	114.1	114.9	115.2	115.8	116.0	115.8	116.0	116.5

NOTES

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

Table 1

- Total population at mid-year.
- Breakdown of gross domestic product by factor cost.

Table 2

- Industrial production.
- Steel production. Source : Service central de la statistique et des études économiques (STATEC).
- Construction. Index based on number of man-hours worked. Source : STATEC.
- Workers employed in the iron and steel industry and in mining. Source : STATEC.
- Consumer prices. General cost-of-living index. Source : STATEC.

