



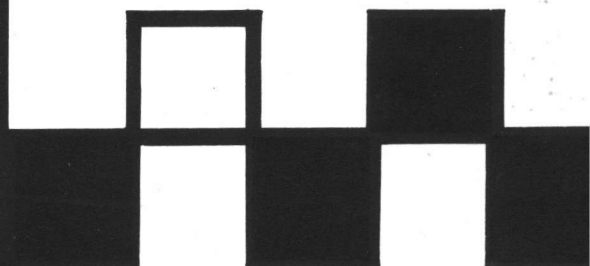
**European  
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**Directorate-  
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for Economic  
and Financial  
Affairs**

**The economic situation  
in the Community**

**3**

**1966**



Quarterly survey

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

**COMMISSION**

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**The Economic Situation in the Community**

**SEPTEMBER 1966**

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**Note :**

This Survey was completed around mid-September 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 number 9-1966 of the "Graphs and Notes on the Economic Situation in the Community" can usefully complete the information supplied here.

## I. THE OVERALL SITUATION

*The considerable expansion of aggregate demand and of domestic supply which had already been noted in the Community continued in the second quarter of 1966 and in the early part of the summer.*

*The growth of effective demand from abroad, especially visible exports to non-member countries, was even more rapid than in the preceding months, largely because purchases by the developing countries were rising faster than before. Customs statistics show that the value of goods exported in the second quarter was some 10.5 % higher than in the corresponding quarter of 1965.*

*On the other hand the expansion of domestic demand began to show signs of weakening, particularly in connection with gross fixed asset formation. Investment in building, for instance, which in the first quarter had benefited from the exceptionally good weather, subsequently expanded more slowly, in part as a result of the earlier speed-up and in part because the expansion of building demand, especially in housing, has been losing momentum in several of the Member States. In France, the vigorous expansion of investment in plant and machinery has, if anything, become more vigorous, while in Italy its progress has been reduced as a result of strikes in the capital goods industries. This situation is one of the reasons why the advances made in these two countries were insufficient to offset the further weakening of the investment boom in the Federal Republic of Germany and a similar though less marked weakening in the Netherlands.*

*Furthermore stock-building, which till the beginning of 1966 had been expanding faster than production, appears to have been slowing up in the last few months; the change is partly a reaction to the easing registered in certain important international raw materials prices, but it is also in part due to financing difficulties.*

Finally, the pace at which private consumers' expenditure was growing has become somewhat more modest, primarily as a result of the more moderate pace at which the total wages bill has been climbing in the Federal Republic of Germany.

The Community's domestic supply expanded further, but here, too, the pace seems to have become somewhat slower, at any rate in the industrial sector; the SOEC index of industrial production (which excludes construction, food, tobacco and beverages and is adjusted for seasonal and fortuitous fluctuations) shows a rise of some 1 % between the first and second quarters, after rises of 1.5 % in the two preceding quarters. For the second quarter the unadjusted index was none the less 6 % higher than a year earlier.

During this time there were slight signs of an easier situation on the Community's labour markets; only in France and Italy were there appreciable increases in the total numbers employed, and in Italy the figure for unemployment was slightly down. There was nevertheless still a considerable shortage of manpower, particularly in the Federal Republic of Germany and in the Netherlands where the number of unfilled vacancies continued to be several times as high as the numbers out of work.

The Community's visible imports from non-member countries have hardly risen, the main reasons being the slower pace at which stocks of raw materials and semi-finished goods were being built up, and the reduction in imports of foodstuffs and defence goods; the total value of imports from non-member countries in the second quarter was none the less 6 % higher than in the corresponding period of 1965. Imports of services appear to have maintained their greater vigour.

Unlike imports from non-member countries, visible trade between the countries of the Community continued to climb steeply. In terms of the value of imports, its year-to-year increase in the second quarter was 13.5 %.

At the beginning of the second quarter the consumer price level was rising faster than before, but towards the end of the quarter and during the summer months the rate of rise eased considerably, especially in the Netherlands, in Belgium and in the Federal Republic of Germany; the relevant indices showed no change or were even slightly down. This was, however, due more to falls in the prices fetched by various foodstuffs than to the trend of demand and costs; the lower prices paid for foodstuffs were caused on the one hand by normal seasonal factors and on the other by the weather, which was not so unfavourable for various products as it had been in 1965, when it had been responsible for prices being marked up quite considerably.

The more rapid growth of exports coupled with a slower growth of imports led to a reversal of the tendency, noticed since the beginning of 1965, for the visible trade balance of the Community to deteriorate; at 385 million u.a. <sup>(1)</sup> the deficit for the second quarter was only half as heavy as in the first. This undoubtedly had a beneficial effect on the current payments position. In addition, there were—parti-

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

cularly towards the end of the second quarter—net inflows of capital, so that the overall balance of payments of the Community will probably have closed with a distinct surplus. At any rate the gross official gold and currency reserves of the member countries rose by 385 million u.a. during the second quarter, after falling 413 million u.a. between December 1965 and the end of March 1966.

In the remaining months of 1966 the economic expansion of the Community should be maintained, although aggregate monetary demand may continue to rise less vigorously than in the early months of the year. The expansion of exports to non-member countries is again likely to be fairly high; but in view of the further weakening to be expected in outlay on investment in the Federal Republic of Germany, overall expenditure on investment in the Community can hardly gather speed, while private consumers' expenditure may rise somewhat less rapidly than in the first half of the year. The impact of stock-building on the growth of aggregate demand is once again likely to be, if anything, negative.

The growth of production in the Community may none the less pick up a little more rapidly, as the rise in prices in the second half of the year will undoubtedly be more moderate than it was in the first half and as, in addition, the balance of payments situation can be expected to improve.

There may nevertheless well be a tendency for the rise in consumer prices to accelerate again somewhat in the final months of the year, as the helpful climatic factors referred to above decline in importance. The rise in prices connected with the business cycle will tend to fade out, particularly in the Federal Republic of Germany and in Belgium; this is not, however, likely to be sufficient to prevent some fresh acceleration in consumer prices.

At the present stage of the stock-building cycle, imports of raw materials will undoubtedly remain hesitant unless there is some change in the present quiet trend of world market prices. This, added to the slower expansion of other domestic elements in monetary demand, will hold back the growth of purchases from non-member countries. As exports can be expected to expand more vigorously, there may well be a further improvement in the Community's trade balance.

Examination of the economic developments that have occurred so far this year and of the latest views on the developments that will occur in the remaining months does not call for any essential change in the forecasts made for the main quantitative results for the full year. In all probability, then, the real gross Community product in 1966 will be some 4.5 % higher than it was in 1965; the external balance, however, might turn out to be higher than previously expected.

For 1967, too, the business outlook is on the whole encouraging. True, the growth of exports from the Community is likely to be less vigorous; the information at present available suggests however that monetary demand within the Community

*will continue to grow at practically undiminished speed, and in view of some easing of the upward thrust of prices coupled with the likelihood that changes in the external balance will be slight, the real gross product of the Community could once again be some 4.5 % higher than in the preceding year. The growth of internal trade within the Community will remain brisk and will continue to make a contribution to economic balance and, by and large, to the promotion of output.*

*Economic expansion in the Federal Republic of Germany may pick up speed again in the course of 1967; in Italy, and perhaps also in France and in the Grand Duchy of Luxembourg, it may for the full year be greater than it was in 1966; in Belgium there may be no change and in the Netherlands there might be some loss of momentum. Total imports from non-member countries are very hard to forecast in view of the latest changes of trend in the stock-building sector, but in 1967 their rise may be somewhat less rapid than in 1966. With exports also likely to be expanding less vigorously, there may well be no great change in the Community's deficit on visible trade.*

*Prices in the Federal Republic of Germany and in Belgium are likely to rise less in 1967 than they did in 1966; in the Netherlands, too, there might conceivably be less advance than before. In all three countries, however, and particularly in the Netherlands, present forecasts suggest that the upward thrust of prices will still be such that there can be no talk of even approximate stabilization. In France, where the upward thrust of prices has so far been relatively modest, there might even be some acceleration in the upward thrust of prices. There is also a risk that the high level of stability achieved in Italy may be upset by fresh pressures on costs and prices.*

*Looked at from the angle of short-term policy, the latest economic developments in the Community and the further outlook suggest that some change in the economic climate is under way and that stabilization policy is beginning to show greater results than hitherto. The Commission does not, however, consider that this could justify any premature relaxation of the efforts to achieve stability and still less any attempt to follow a more expansionary policy. In the countries where there have been inflationary developments—the Netherlands, the Federal Republic of Germany, Belgium and to some extent Luxembourg as well—those responsible for short-term economic policy should rather aim at reinforcing the tendencies that contribute to stability, while in those countries—Italy and France—where the business situation is recovering from a period of weakness, those responsible for policy should seek to keep the growth of domestic monetary demand within those limits beyond which there will be a recrudescence of pressures on prices and costs. This does not mean that the promotion of growth should be unduly neglected. On the contrary, the more short-term economic policy gains or maintains control over the expansion of consumption expenditure, the greater will be the margin for investment—and without sufficient expansion of investment there can be no economic growth in the longer term.*



## A. Recent developments

### 1. Demand

In the second quarter of 1966 and—as far as can be seen from the data available—also in the summer months, the economic trend in the Community was marked by a persistent and appreciable growth of aggregate demand, helped by an increasingly rapid expansion of demand from abroad.

Demand from abroad (in terms of actual exports of goods and services to non-member countries) clearly tended to rise faster than in the preceding months. The value of visible exports alone, after adjustment for seasonal and fortuitous fluctuation, showed a rise of 4 % from the first to the second quarter, against an increase of 1 % between the final quarter of 1965 and the first quarter of 1966. The gross value of visible exports in the second quarter exceeded the figure of a year before by some 10.5 %.

Deliveries to the United States continued to expand with particular vigour, though the rate of growth fell away somewhat. This slight easing would seem to be connected with the temporary slackening in the expansion of private consumers' expenditure in the United States, which since the start of the spring has been reacting to measures taken previously (higher social security contributions, faster collection of direct taxes, restoration of indirect taxes which had recently been reduced). Demand for certain consumer durables, in particular cars and electrical household appliances, was hesitant in the second quarter. On the other hand the trend of the remaining components of monetary demand in the United States probably exerted no restrictive influence on the flow of imports. Capital investment by industry continued to advance at a lively pace despite the bottlenecks that were appearing in the capital goods industry and in spite of a marked increase in the cost of credit. Furthermore, stocks were being built up more rapidly; this, apart from the increase in stocks of unsold cars, was apparently connected with fears of an impending aggravation of shortages of certain raw materials and semi-finished products. Public expenditure continued to expand very rapidly in the period under review, above all direct and indirect military expenditure. Only in the demand for housing may there have been even a slight decline, due mainly to higher costs and scarcity of funds.

On the whole, despite the poor turnover in individual consumer goods industries, which also affected activity in their ancillary industries, industrial production in the United States tended to rise at an almost unabated pace right into the summer. From the first to the second quarter the real gross national product, seasonally adjusted, went up by 0.6 %; the year-to-year growth rate was 6 %, after having reached 6.7 % in the first quarter. The number of persons in employment increased further and reached a new peak in July. The unemployment rate was slightly under 4 % and the markets for skilled workers became even tighter.

There had been hopes, especially in the United States itself, that the temporary relaxation of the pressure on consumers' expenditure would lead to a slackening in the upward movement of prices. Despite the continuing vigorous growth of production—which however did not correspond in every respect to the pattern of demand—and an appreciably greater increase in imports, this hope was not fulfilled. Prices continued to

rise at every stage from producer to consumer. Even the prices of some foodstuffs went up again noticeably towards the middle of the year, and in the steel market a wave of price increases set in. The consumer price index rose by 0.8 % from March to July, by which time it was 2.8 % higher than a year previously.

With imports growing faster than exports, the balance of visible trade, and consequently the balance of current payments, deteriorated further; however, a decline in net exports of capital led to a distinct reduction in the deficit on the overall balance of payments. For the second quarter the deficit was \$163 million, against \$554 million for the previous quarter (seasonally adjusted figures, on a liquidity basis).

The United Kingdom's visible imports from the Community in the second quarter still showed no great response to the measures of restraint; like the visible imports of the United States, they expanded with even more than average vigour. One explanation is the vigour with which consumers' expenditure was still growing in the United Kingdom. Though not as fast as in the first quarter, the rate of growth was still considerable, and it was not till August or September that the new monetary and fiscal restrictions imposed in July began to bite. Before and during the seamen's strike, too, there seems to have been heavier buying of certain items in order to build up stocks, as there were fears that the strike might spread to the dockers. On the other hand, expenditure on fixed asset formation by industry was more and more evidently losing momentum.

From the first to the second quarter industrial production declined, partly it is true as a result of the seamen's strike, which hindered the United Kingdom's exports more than its imports. From June onwards the labour market became distinctly less tight, whereas until then the excessive strains had been one of the main reasons why attempts to establish a policy of restraint over incomes had been largely unsuccessful.

As was to be expected, the seamen's strike had serious repercussions on the balance of trade and therefore on the United Kingdom's balance of payments. In June the surplus of imports over exports was twice as high as in May, and it remained at the new high level in July.

The Community's visible exports to other industrial countries continued on the whole to expand modestly. The trend of exports to the EFTA countries in northern and central Europe reflected very distinctly the general preponderance of those factors which tended to produce a calmer business climate over those which promoted expansion; it is only in Norway that the latter still seem to dominate.

Exports from the Community to the developing countries picked up vigorously in the second quarter, particularly towards the end. The time-lag with which these countries, taken as a group, reacted to an improvement in their foreign currency receipts by increasing their imports from the industrial countries now seems to have been eliminated; on this occasion the improvement has been of particularly long duration and has led to a considerable increase in the developing countries' currency reserves.

Unlike external demand, monetary demand within the Community apparently expanded somewhat more slowly in the second quarter of 1966 and at the beginning of the summer than in the preceding months.

*Visible exports to non-member countries*  
(Values and % change on preceding year)

	1965		1965				1966	
	million u.a. ( <sup>1</sup> )	%	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter	2nd quarter
To all non-member countries :	27 079	+ 12	+ 12	+ 11	+ 14	+ 11	+ 7.5	+ 10.5
of which :								
To industrial countries ( <sup>2</sup> )	17 612	+ 12.5	+ 12	+ 11	+ 15	+ 12.5	+ 9	+ 10.5
including :								
United States	3 425	+ 20	+ 11.5	+ 19.5	+ 25	+ 23.5	+ 22	+ 18.5
EFTA	9 604	+ 8.5	+ 9.5	+ 6.5	+ 11	+ 7.5	+ 5.5	+ 6.5
United Kingdom	2 367	+ 3.5	- 5	0	+ 9	+ 9.5	+ 18	+ 12.5
To developing countries ( <sup>3</sup> )	7 501	+ 9	+ 10	+ 8.5	+ 11.5	+ 6	+ 0.5	+ 8.5
including :								
Associated overseas countries and territories	1 733	+ 5	+ 1	+ 4	+ 8	+ 6	- 3	- 3.5
To other areas ( <sup>4</sup> )	1 966	+ 19	+ 23	+ 24.5	+ 15.5	+ 15.5	+ 20	+ 20.5

Source : Statistical Office of the European Communities.

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

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

(<sup>3</sup>) Class 2 of the Standard Country Classification for Foreign Trade Statistics of the EEC.

(<sup>4</sup>) Class 3 of the Standard Country Classification for Foreign Trade Statistics of the EEC, and other destinations.

Most affected apparently was gross fixed asset formation; investment in the form of building and construction, which had shown a considerable upswing in the first quarter on account of the exceptionally good weather, has since then made only slow progress in the Community as a whole. One reason was the fairly distinct lull on the building markets of several member countries, particularly in the Federal Republic of Germany; this lull in its turn was connected mainly with the growing tightness apparent on the capital markets, with concomitant increases in interest rates, and with a slower expansion in investment expenditure by the public authorities. In the countries concerned it was primarily residential building which suffered. Activity in this sector was relatively weak in Italy too, although this country seems to be experiencing some recovery of investment in construction. In France demand for housing continued quiet after the rush to build in 1965; investment by the public authorities, however, expanded fairly considerably.

Investment in plant and machinery, on the other hand, seems to have increased at the same modest pace as in the preceding months. While in the Federal Republic of

Germany the expansion of expenditure in this field levelled off distinctly, and somewhat less in the Netherlands, in France the upward movement gathered speed; in Italy, too, the upward tendency was maintained although, owing to the strikes in important sectors of the metal working industry, there was some temporary slackening in the rate of expansion.

Investment in stocks seems to have expanded less fast. Whereas previously the rising prices of raw materials and semi-finished products in general caused stocks to be built up out of proportion to the growth of production, from the beginning of spring onwards the trend was quieter because these prices levelled off or even turned downward. Stocks of finished goods generally continued to be built up at more or less the same pace.

Public current expenditure on goods and services continued to expand rather rapidly. There was nowhere any real slackening, such as might have followed anti-inflationary measures or economy measures taken because of financing difficulties.

The expansion of private consumers' expenditure, on the other hand, levelled off slightly in the second quarter. This is due almost exclusively to developments in the Federal Republic of Germany, where the growth of consumption, which until now had been very vigorous, began to flatten out. In the other member countries there was no substantial change of trend. Consumer spending continued to expand distinctly, above all in Italy and France; in Belgium and the Netherlands there was a recovery after the slackening in the first quarter caused by fortuitous factors such as the raising of indirect taxes at the start of the year; particularly in Belgium, however, the underlying trend no longer seems to have been so sharply expansionary as a year earlier.

Apart from certain changes affecting the propensity to save, especially in the Netherlands and Belgium but also in the Federal Republic of Germany, the main influence on the trend of private consumers' expenditure were the developments affecting gross incomes : in the Federal Republic of Germany income from paid employment rose more slowly in the second quarter, and the growth of other forms of income also seems to have been less marked on account of the slacker business situation. In Belgium, however, where the sliding wage-scale came into operation repeatedly, there was still no easing of the upward thrust of wages. In the Netherlands, too, actual wages rose considerably and in some cases the changes in collective agreements were put into operation even before authorization had been given. In France and Italy the expansion of the volume of employment had an accelerating influence on the trend of total wages and salaries, but the pace at which wages per head were increasing did not accelerate. In the Community generally, and especially in Belgium and Luxembourg, transfers of income to households through the public authorities continued to climb sharply. Tax changes in the period under review did not influence the disposable income of households; however, the slightly damping effect of the progressive system of direct taxation was appreciable, especially in the Netherlands and the Federal Republic of Germany; the incidence of direct taxation is heavy and the rate of progression steep, and the tax reductions made the previous year had probably been offset in the meantime by the rising level of money wages.

As is usual in the spring months and even more in the summer, consumers spent more heavily on services (travel and holidays) than at other times; owing to the relatively

high income elasticity of this type of expenditure, the switch was probably once again more marked than in the previous year; it may also have contributed to the fact that purchases of consumer goods, consumer durables in particular, showed signs of falling away, more in one country, less in another. While in France and Italy the growth of consumption was concentrated largely in this sector and though in both countries sales of private cars continued to rise, the rate of expansion was somewhat slower than it had been. In the remaining member countries demand for consumer durables continued to be heavy, but on the whole there was little progress. The number of new passenger cars and estate cars registered in the second quarter did not even reach the level of a year before, one reason for this, in the Netherlands and Belgium at least, being the fortuitous factors repeatedly referred to above—purchases in 1965 in anticipation of the raising of indirect taxes, and the consequent reaction in 1966.

## 2. Production

The expansion of supply within the Community continued in the second quarter and probably also in the summer months; but it was somewhat less fast than in the opening months of the year.

This was because the growth rate of industrial production fell off slightly. The index of the Statistical Office of the European Communities (adjusted for seasonal and fortuitous variations and excluding construction, food, beverages and tobacco) rose from the first to the second quarter of 1966 by about 1 %, after an increase of some 1.5 % from the fourth quarter of 1965 to the first quarter of 1966. Furthermore, the expansion of production in the construction sector slackened in the Community as a whole.

Among the individual industries, production in mining and the aggregate output of the basic materials industries made no great progress. In the June-August period coal output was on the average 5.5 % below the level of the same months in 1965, although once again a part of the output remained at the pit head. The production of iron and steel remained about the level reached in June, July and August 1965. The slowdown in the trend of demand for construction inhibited expansion in the production of building materials. In the chemical industry, however, production in most member countries accelerated and this was probably due mainly to the buoyancy of demand from abroad; the year-to-year growth rate for the Community as a whole rose a full 10 %.

The growth rate of the production of consumer durables and non-durables does not seem to have been maintained in all member countries. In textiles and the car industry, at any rate, expansion in the Community as a whole levelled off somewhat at the beginning of the summer, mainly on account of some levelling off of growth in the Federal Republic of Germany.

The aggregate of production in the capital goods industries also made somewhat more modest progress, largely because in the Federal Republic of Germany output in mechanical engineering and throughout the metal working industry failed once again to rise above the level of a year earlier, while in Italy the output of the metal working industry was held up by strikes. Consequently, the effect of an acceleration of production in France was more than offset in the Community as a whole.

The contribution to GNP made by the services sector, on the other hand, scarcely slackened at all, as far as can be judged from the very fragmentary information available.

Total agricultural production probably continued to grow. Although, according to provisional data, the cereals crop in the Community did not quite reach the rather high level of the previous year, the output of vegetables and fruit was substantially larger than in 1965 and livestock production, in particular milk and beef, expanded quite appreciably.

Owing to the slower expansion of production in manufacturing, the tightness of the labour market in the Community as a whole showed slight signs of easing. There was probably little rise in numbers employed. While in France and Italy there was undoubtedly a further increase in the number of persons employed, at any rate in industry, and in the Netherlands too the number will probably have continued to grow, it is unlikely that in the remaining member countries there was any increase in employment—indeed there was in industry and, in the Federal Republic of Germany, also in building and construction some tendency for the numbers employed to contract.

These trends helped to increase slightly the seasonally adjusted number of unemployed in the Federal Republic of Germany, Belgium, and the Netherlands; in the Netherlands, however, the relatively lively expansion of the labour force was also partly responsible. In France, the number of persons seeking employment showed no tendency to decrease, and may even have edged up, despite the rising number of persons already employed and an even further increase in the number of unfilled vacancies. This was probably due in part to the weak trend in building and construction and to the considerable increase in the labour force. In Italy the expansion of production was so vigorous that the number of unemployed tended to diminish despite the great improvement that is occurring in the present stage of the business cycle.

Developments in the last few months, however, have not produced any essential change in the basic situation of the labour market. In the Federal Republic of Germany and the Netherlands overemployment and labour shortages were general, although there was some change of climate, particularly in the Federal Republic of Germany; in Belgium and France the market was somewhat less tight, but in France the dearth of skilled workers became more and more marked; in Italy underemployment was still widespread.

### **3. The balance of the markets**

The rise in the Community's imports of goods and services from non-member countries probably lost momentum in the second quarter; for visible imports, at any rate, the seasonally adjusted figures show hardly any increase on the first quarter. Compared with a year earlier, however, the value of these imports was up 6 %.

One reason for the slower growth of visible imports may well be the reduced pace at which stocks of imported raw materials and semi-products were being built up in the Community; secondly, purchases of foodstuffs were relatively slack on account of increased

production in the Community; thirdly, the quieter trend of investment, particularly in the Federal Republic of Germany, had a restraining effect; and lastly, government imports into the Federal Republic of Germany (defence goods) decreased appreciably. The trend of imports into France and Italy resulting from the upswing of business in those two countries was not enough to offset these slackening tendencies.

The quieter trend of the Community's demand for raw materials has so far hardly affected the still considerable expansion of imports from the developing countries; but in conjunction with a slowdown in the quantity of capital goods and agricultural products being imported by some member countries, it has had a distinctly restrictive effect on the Community's purchases from the United States. Imports from the EFTA countries increased further; the slower expansion of imports from the United Kingdom, probably caused in the main by the British seamen's strike, was more than offset by an accelerated upswing of purchases in Sweden and even more in Switzerland.

Visible trade between the member countries continued to expand rather rapidly. According to seasonally adjusted figures (based on customs returns), imports increased in value by 2.5 % over the first quarter. The unadjusted figures for the second quarter were 13.5 % higher than a year earlier.

Imports into the Federal Republic of Germany from the rest of the Community, which had still been rising rapidly at the beginning of the year, have since then been visibly affected by the quieter overall demand for imports in that country. Demand in France, on the other hand, has grown appreciably stronger; French imports from Community countries, adjusted for seasonal variations, were 10 % higher in value than in the first quarter and 24 % higher than a year before. The expansion of Italian purchases was maintained, but the pace was slightly slower. The same applies to imports into the Benelux countries, once allowance is made for the effects of fortuitous factors, which in Belgium and the Netherlands influenced the trend of imports from the rest of the Community.

The main beneficiary of the very lively demand from France was Italy; deliveries from that country to France were 35 % higher in the second quarter than a year previously. The appreciable recovery of exports from the Netherlands to the other member countries, after the decline registered in the first quarter, may likewise be due in part to French demand; but it is also partly due to the disappearance of a fortuitous obstacle to exports (foot and mouth disease) which had held up exports in the first quarter. Intra-Community exports from Germany were considerably stimulated by demand not only from France, but also from the Netherlands and—to a lesser extent—from Italy. On the other hand, the slowdown of imports into the Federal Republic of Germany caused exports from France to the Community to cease rising and the growth of exports from the Belgo-Luxembourg Economic Union to be as modest as in the early months of the year.

The developments in intra-Community imports and exports outlined above led in the second quarter to an appreciable deterioration of France's balance of trade with the other member countries. The surplus of the Belgo-Luxembourg Economic Union tended to shrink further, and in the Netherlands the situation recovered to a certain extent.

The trade balance of the Federal Republic of Germany with the other Community countries even showed a slight surplus. Italy's balance did not change substantially.

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

	1965		1965				1966	
	million u.a. ( <sup>1</sup> )	%	1st quar- ter	2nd quar- ter	3rd quar- ter	4th quar- ter	1st quar- ter	2nd quar- ter
From all non-member countries	28 562	+ 6.5	+ 0.5	+ 3	+ 11.5	+ 10.5	+ 13.5	+ 6
of which :								
industrial countries ( <sup>2</sup> )	16 216	+ 5	— 2	+ 3.5	+ 8.5	+ 9.5	+ 15	+ 7
including :								
United States	5 687	+ 4.5	— 8	+ 8	+ 9	+ 9.5	+ 20	+ 2
EFTA	6 893	+ 4.5	+ 4	+ 1	+ 6.5	+ 7.5	+ 9	+ 7
United Kingdom	2 605	+ 1	— 1.5	— 5.5	+ 1.5	+ 9	+ 9.5	+ 4.5
From developing countries ( <sup>3</sup> )	10 522	+ 7	+ 3.5	+ 1	+ 14	+ 10	+ 10	+ 9
including :								
Associated overseas countries and territories	2 046	— 0.5	— 4	— 3.5	+ 0.5	+ 4.5	+ 9.5	+ 12
Central and South America	2 615	+ 6	0	— 0.5	+ 23	+ 4.5	+ 4.5	+ 13.5
From other areas ( <sup>4</sup> )	1 824	+ 18	+ 9	+ 13	+ 22.5	+ 25.5	+ 24.5	+ 21.5

Source: Statistical Office of the European Communities.

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

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

(<sup>3</sup>) Class 2 of the Standard Country Classification for Foreign Trade Statistics of the EEC.

(<sup>4</sup>) Class 3 of the Standard Country Classification for Foreign Trade Statistics of the EEC, and other sources.

Between the first and second quarters there were again fairly vigorous price rises in most of the member countries; particularly affected were consumer prices: in April-May the cost-of-living indices or retail price indices were up 7 % in the Netherlands, 5.2 % in Belgium, 4.5 % in the Federal Republic of Germany, 2.8 % in France, 2.7 % in Italy and 2.6 % in Luxembourg on the corresponding period of 1965. During the second quarter, however, generally from June onwards, and in the following summer months too, most of the indices rose at a distinctly slower pace, if at all. In July-August the



year-to-year growth rates fell back in the Netherlands to 5.3 %, in Belgium to 3.7 %, in the Federal Republic of Germany to 2.9 %, in France to 2.6 % <sup>(1)</sup>, in Luxembourg to 2.4 % and in Italy to 1.9 % <sup>(2)</sup>.

The slackening in the upward movement of consumer prices is due only in part to the business situation. It is also partly the result—to differing degrees in the various member countries—of the disappearance of a fortuitous factor, i.e. the influence on prices of the previous year's unusually poor crop, in particular potatoes and other vegetables; this year's more favourable conditions have resulted in somewhat more normal prices. In addition there was the effect of seasonal price reductions, mostly on the same products. Of course all these movements are temporary features, which must not be confused with a true trend towards stabilization.

There were, however, tendencies that contributed to stabilization, especially in the Federal Republic of Germany, and also in Belgium, where there seems to have been a more or less distinct easing in the pressure exerted by excess demand. In most member countries the trend of world prices for raw materials and semi-products, which had flattened out and was, if anything, inclined to point downwards, also exerted an influence on certain domestic prices. In Belgium and the Netherlands there was a gradual attenuation of the price increases by which the higher indirect taxes introduced at the beginning of the year were passed on to the consumer. In both these countries the authorities considerably stepped up in spring their direct pressure to contain prices, while in France, too, direct price policy continued to play a significant role.

In most member countries producer prices for finished industrial products showed more or less distinct signs of settling down during the second quarter and in the summer months; but in the Netherlands, in the Federal Republic of Germany and, to a lesser degree, in Belgium the pressure of costs, which eased only slightly, led none the less to a number of quite appreciable price increases. In France, the price increases continued to be limited and in Italy the situation remained practically stable. At consumer level the tendency for the prices of finished industrial products to settle down was less noticeable.

Not only in commerce but in the whole services sector throughout the Community prices continued to rise at almost the same pace as before. This applies in particular to the provision of services proper, with Italy the only exception. In the Federal Republic of Germany rents continued to soar, and on 1 April postage rates were raised. In France the rates for certain public services were put up from 1 August.

Under the simultaneous influence of faster growth of exports and slower growth of imports the tendency for the visible trade balance of the Community to deteriorate, which had still been very marked in the opening months of the year, was reversed in the spring. Customs returns show the deficit in the second quarter to have been 385 million u.a., which was only about half as heavy as in the first quarter. This trend in the visible trade balance will probably have been reflected in the total current payments position. As, in addition, there were considerable net inflows of capital, especially towards the end

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<sup>(1)</sup> In July; exclusive of "medical services", where there were fortuitous variations.

<sup>(2)</sup> In July.

of the second quarter, connected in part with a further weakening of the pound sterling, the Community's overall balance of payments may well have closed with a large surplus despite the effect of some special transactions, for instance the raising of IMF quotas. This assumption is supported by the trend of the gross official gold and currency reserves; from March to June 1966 these grew by 385 million u.a., while the net foreign exchange position of the commercial banks seems to have shown scarcely any change.

Transactions with non-member countries in the second quarter, unlike those in the first, had once again an expansionary effect on internal liquidity in the Community. There was a continuous increase of liquidity in Italy and France, and in the Federal Republic of Germany, where the trend in the balance of payments had in the previous quarter greatly reinforced official endeavours to achieve domestic stability, its effect in the second quarter was modestly expansionary.

Cash operations by the public authorities are also likely to have resulted in an increase of domestic liquidity. Except for the Federal Republic of Germany, all Community countries, especially France, showed heavier deficits, which in part were financed by means other than long-term savings. It is true that in Germany the Federal budget showed a cash surplus at the end of the second quarter, but the net assets of the central public authorities as a whole at the Bundesbank diminished, and this helped to expand liquidity. In addition, the deficits in this country were covered partly by monetary means, such as certificates of indebtedness and bank credit.

All in all, the trend of rates on the money market suggests that the summer pressure on bank liquidity has relaxed somewhat. The expansion of bank advances to business customers in the second quarter accelerated appreciably in France, and in the Netherlands and the Federal Republic of Germany it remained quite lively until the spring when, in the Federal Republic of Germany at least, it moderated somewhat. This also seems to have happened in Belgium, in the second quarter at any rate; here short-term credit did not exceed the limit set by the Central Bank. In Italy, where the banks again stepped up their purchases of securities sharply, the expansion of credit continued at first at a relatively slow pace, but began to accelerate towards the end of the quarter.

In the second quarter the capital markets in most member countries still showed persistent tendencies for interest rates to rise, in some cases largely as a result of continuing lively demand from the public authorities and corporations. Nevertheless, various factors came increasingly to the fore which contributed to the stabilization of interest rates: these were the improvement in the balance of payments; the endeavours made by some governments to limit calls on the capital market; in some countries the raising of interest levels, which helped to stem outflows of capital; the adjustment of interest rates on new issues to the higher rates obtaining on the market; the stimulus given to the flow of savings by the high rates of interest on bonds; and the somewhat cooler business climate, particularly in the Federal Republic of Germany.

These factors were particularly noticeable on the bond markets. It was symptomatic that in the Netherlands a State loan recently floated at 7 % was oversubscribed. In the Federal Republic of Germany there was also some improvement in the climate of

the bond market, though there was still no fundamental change. In Italy and France, however, where the long-term interest rates were still in varying measure below those ruling in other member countries, the slightly rising trend has not yet come to a clear halt.

The volume of business on the equity markets in the Community continued to be relatively small in the second quarter and in the summer months. The downtrend in Wall Street, which is probably in the main of psychological origin, and the uncertainties surrounding the pound were hardly likely to diminish the caution of investors. Recently, however, the equity markets have been showing a very fair degree of resilience. It is evident that the selling of securities by America has slackened, probably on account of the falling prices of shares in the United States; institutional investors from Europe have made a number of investments. Furthermore, the quite good outlook for profits in several member countries may in itself have helped to support the market.

## B. Outlook

The economic outlook for the Community as a whole up to the end of 1966 is one of appreciable expansion of domestic and foreign demand and also of production.

Demand from abroad (in terms of actual exports of goods and services to non-member countries) will certainly continue to expand in the next few months, at least where the Community's visible exports are concerned; for the full year 1966 growth in this particular sector may be as high as some 9 % in value—as was predicted in the last Quarterly Survey.

Exports to the United States may again grow more quickly in the second half of the year than in the spring, in conformity with the trend of business now becoming visible there. There is likely, in particular, to be a fresh acceleration of private consumers' expenditure once the slightly inhibiting effects of the measures taken at the beginning of the year have faded. The rise in gross incomes can also be expected to become, if anything, steeper than it has been. As consumption expands, car purchases in particular will probably rise sharply again from the autumn onwards, when new models appear. Public expenditure will continue to stimulate the growth of overall monetary demand vigorously, mainly because of increasing military expenditure, which seems to be expanding faster than was expected. Lastly, the steadily favourable trend of profits offers firms the possibility of continuing to increase their expenditure on fixed asset formation as planned, despite the increasing cost and tightness of credit. The measures recently announced by the President to damp down the investment boom, for example the reduction of tax incentives for investment, are hardly likely to influence the trend of actual outlay this year. On account, however, of the growing difficulties that are hampering deliveries by the American capital goods industries, further orders will have to be transferred abroad if the programme of investment is to be completed without cuts. Only the growth rate of investment in stocks, which is of little importance to the Community's exports, might decrease in the months to come and expenditure on house-building, too, could decline slightly.

The trend of demand outlined here will probably continue to be accompanied by a rapid growth of production in the United States, but the growth will not be fast enough. The optimum technical production capacities have already been exceeded in many cases, and reserves of fully fit manpower, available at the right place and with the requisite skills, are exhausted. A persistent rise in prices and in imports is to be expected, perhaps with a further deterioration in the balance of visible trade. On the other hand, there could be larger inflows of capital, in connection with the tightness of liquidity and the appreciably increased interest rates on the American capital market, so that the deficit in the overall balance of payments for 1966 may not grow so much as might have been expected.

The business trend in the United Kingdom, unlike that in the United States, will be marked more and more by the effects of the policy of restraint, which was intensified in mid-July by further measures intended to withdraw £500 million per annum of purchasing power from domestic demand. These measures took the form mainly of stricter conditions governing credit, higher taxes and charges, restrictions on public investment expenditure and a further raising of bank rate. In addition, the Government requested powers, which it obtained in the middle of August, to activate if necessary the "voluntary"

price and incomes freeze decided upon in July. The new stabilization programme will be strengthened between now and the end of the year by the deflationary effects of the selective employment tax (SET), which has been levied since September. Taken together, these measures will certainly lead to a further damping of industrial investment and, secondly, to a progressive reduction of the pace at which private consumers' expenditure is expanding. At best the growth of production in the second half of the year will probably be very small; for the whole of 1966 the growth of the gross national product in real terms is hardly likely to exceed 1.5 %.

In these circumstances a very distinct slowdown in the expansion of the United Kingdom's imports, if not an actual reduction, must be expected in autumn, especially as intended purchases of finished and semi-finished products may be postponed until after the removal of the import surcharge at the end of November, and this would have an additional restrictive effect. No doubt the trend of exports from the Community, as from other areas, will be influenced by these factors.

The latest information on the trend of business activity in the remaining industrial countries outside the Community suggests that certain tendencies to slacken in some countries and to accelerate in others may balance each other out to such an extent that their total imports, including those from the Community, would continue to advance at the same modest pace as before.

Purchases from the Community by the developing countries, on the other hand, will probably expand faster during the rest of the year than in the first six months; this would correspond to the greater readiness shown of late by these countries to use their growing foreign exchange receipts to increase their imports, especially of industrial products, instead of replenishing their official reserves further.

Unlike the trend of demand from abroad, the expansion of the Community's internal demand in monetary terms may continue to slow down somewhat between now and the end of the year; most marked will be the slackening in the rise of expenditure on fixed asset formation. To judge from the figures for starts and dwellings under construction, expenditure on house-building will probably cease to grow appreciably. Public expenditure on construction appears rather more clearly set for growth: fairly vigorous expansion in France, and probably in Italy too, should largely offset any loss of momentum in the Federal Republic of Germany and elsewhere. Expenditure on industrial and commercial building may also make good progress. In the Community as a whole, however, the expansion of investment in building will undoubtedly lose a little more of its dynamism. So too will expenditure on plant and machinery, since the more rapid expansion expected in France and Italy may not suffice to offset the slacker trends that are sure to persist in the Federal Republic of Germany and—albeit to a lesser degree—in the Netherlands too.

It is always particularly difficult to predict the future trend of investment in stocks, but it can at any rate be assumed that outlay on stocks of raw materials and semi-products, and particularly of those items which are imported, will continue to lose momentum.

The expansion of consumers' expenditure may also be expected to slacken further, though only slightly. While the information at present available offers no grounds for looking forward to any real easing of the rapid increase in public expenditure on goods and

services in the Community as a whole, the growth of private consumers' expenditure may well prove once again to have been somewhat slower, although in France perhaps, and doubtless in Italy too, there should even be some acceleration in the rate of expansion, which in both countries is already quite considerable. Against this it can be expected that the slowdown in the Federal Republic of Germany will continue, that the rate of expansion in the Netherlands will be somewhat more modest, and that in Belgium growth will be relatively slow. It must be pointed out, however, that the probability of some slight slackening in the growth of private consumers' expenditure in the Community does not mean that the volume of private consumption will expand more slowly; on the contrary, the slower rise of consumer prices suggests that it will if anything accelerate somewhat.

The disposable income of households will continue to increase considerably: perhaps even faster in France and Italy than before, more slowly in the Federal Republic of Germany. In France and Italy the total number of hours worked may increase more sharply again and hourly wage-rates will—where this is possible—rise somewhat faster towards the end of the year, following the impending revision of numerous wage agreements; in Italy the current wage negotiations could lead to big changes in wage structure aggravating the wage drift. In the Federal Republic of Germany some further easing in the upsurge of total wages and salaries is expected, and in Belgium too the trend of private incomes may become somewhat more moderate owing to the further slackening of business activity. In the rest of the member countries no significant changes are to be expected.

In contrast with the expected trend of aggregate monetary demand, the growth of supply from Community sources may even accelerate slightly. One of the reasons has already been pointed out in the comments on the foreseeable trend of private consumers' expenditure: namely, that in general the upward thrust of prices will become more moderate and that demand in terms of volume will consequently grow more rapidly. A further reason is that the growth of imports will probably be slow, and it is therefore possible that the expansion of industrial production in the second half of 1966 will be somewhat faster than in the second quarter; the likelihood that this speed-up will occur is improved by the probability that the factors of production will be relatively high—a probability that is increasing even in those member countries where until now labour has been extremely short.

The Community's imports, as already stated, are expected to expand only rather modestly, so it is possible that the recovery of the Community's visible trade balance will continue in the second half of 1966.

With the gradual ending of the seasonal and fortuitous reductions for certain crop products that have been possible this year thanks to better production conditions, the pace at which the general price level in the Community is rising can be expected to increase, especially in the final months of the year. The rate, however, will probably remain lower than it was up to and including part of the second quarter of 1966, for the rise in prices due to current developments in the business situation can still be expected to level out slightly during the rest of the year. The slowdown will be confined in the main to the Federal Republic of Germany and Belgium, where the slackening in the expansion of demand will probably make it rather difficult to pass on to the buyer the

increase in wage costs, which has till recently been very considerable. In the Netherlands, on the other hand, where there will certainly continue to be sharp wage increases, there is little likelihood of the economic situation easing enough to damp down appreciably the still considerable upsurge of prices. The relatively high elasticity of supply still prevailing in France and Italy, where reserves are still available on the labour markets, makes it rather improbable at present that there will be a decisive change in the trend of prices in these countries; nevertheless, it is not impossible that in both countries, particularly France, certain tendencies contributing to a faster rise may begin to be felt towards the end of the year.

Economic developments since the beginning of the year and the above prospects for the rest of the year confirm by and large the quantitative forecasts published in Quarterly Survey 2/1966 on the trend (in terms of volume) of supply and demand and of their chief components for the whole of 1966. It is still likely that the gross Community product in real terms will grow by about 4.5%. Industrial production (as defined for the index of the Statistical Office of the European Communities, i.e. excluding construction, food, beverages and tobacco), may expand by a full 6%. The external surplus, however, will probably be larger than had been expected.

*Community product and expenditure* <sup>(1)</sup>

	1963	1964		1965		1966 <sup>(2)</sup>	
	At current prices in '000 million u.a. <sup>(4)</sup>	% change on preceding year					
		Volume	Value	Volume	Value	Volume	Value
Gross Community product	252.0	+ 5.8	+ 10.2	+ 4.1	+ 7.6	+ 4.5	+ 8
Private consumption	155.4	+ 4.4	+ 8.3	+ 4.3	+ 7.7	+ 4.5	+ 8
Public current expenditure	36.3	+ 2.4	+ 8.9	+ 4.3	+ 9.8	+ 3	+ 8
Gross fixed asset formation	57.7	+ 8.2	+ 13.0	+ 3.3	+ 5.8	+ 4	+ 6.5
Balance exports <sup>(3)</sup> less imports <sup>(3)</sup> (in '000 million u.a. current prices)	+ 0.5		+ 1.4		+ 2.8		+ 3.2

<sup>(1)</sup> Community aggregates based on official exchange parities.

<sup>(2)</sup> Commission forecasts.

<sup>(3)</sup> Goods, services and factor income.

<sup>(4)</sup> 1 u.a. = 1 unit of account = 0.888671 gm. of fine gold = US \$1 at the official exchange rate.

Note:

(a) The difference between the figures for product and those for expenditure is accounted for by movements in stocks.

(b) The 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 on the sole responsibility of the Commission.

As far as can be judged at present, aggregate demand in the Community may expand in 1967 as fast as in 1966, although demand from abroad in the coming year may lose some of its dynamism.

The latter point may apply as much to purchases by the United States as by others, especially if the overheating in the American business situation is tackled on a more permanent basis. Unless one of these conditions is fulfilled, it must be expected that the rapid expansion of consumption, which is not held in check sufficiently by the progressive incidence of the normal tax on incomes, will persist, especially as collective wage agreements in some major industries are due to be renegotiated at the end of 1966 and in 1967. At the same time, however, there may be a levelling off in the expansion of industrial investment; according to business surveys, investment expenditure planned for 1967 was still very high (17 % increase), but the measures recently announced by the President in the matter of tax rebates and depreciation for tax purposes will probably have a restrictive effect. Public expenditure may well continue to grow vigorously, at any rate in the financial year 1966/67 (i.e. until June 1967) despite the recently proposed economy measures. But there are signs that, at latest when the necessary increase takes place in the estimates for the armed services, the Government may raise both income tax and corporation tax. The slackening that is perhaps to be expected in domestic business activity will no doubt also influence the trend of imports, though perhaps not so strongly, since even a slightly less dynamic domestic demand could, because of the over-utilization of production capacity attained in the meantime, prove to be too fast in relation to the elasticity of supply.

In the United Kingdom, the sheaf of restrictive measures already taken for 1967 promises to have quite appreciable effects on the trend of domestic demand. With employment tending to decrease and with a brake on the growth of incomes, private consumption will probably be listless. Industrial investment in plant and machinery will no doubt decline despite the refunds and subsidies which from next spring on are to be paid out of the selective employment tax fund to manufacturing industries. It is only expenditure by the public authorities which may, even after the proposed reduction in investment expenditure, still provide appreciable support for overall domestic demand. All in all, the growth of the real gross national product from 1966 to 1967 will probably be of the order of 0 to 1 %, and a temporary decline during the year does not seem to be beyond the bounds of possibility.

In the circumstances it is unlikely that demand in the United Kingdom will stimulate exports from the Community in 1967. The removal of the import surcharge will probably lose much of its significance owing to the slowdown of domestic demand, and it may be only sufficient to delay and mitigate somewhat the weaker tendency to be expected in British imports.

At present it is unlikely that there will be any substantial change in the trend of purchases from the Community by the remaining industrial countries taken together. On the other hand it is certain that a distinctly faster upswing of imports into the developing countries can be expected, at least on a year-to-year comparison. The somewhat weaker



trend of world prices which has been observed for some time still does not suggest that the developing countries' propensity to import, which has only recently begun to grow, is likely to relapse in the near future; their foreign exchange reserves have risen appreciably and their current earnings are likely to be supported by the growing volume of the goods they export to the industrial countries.

The growth rate of internal demand in the Community in 1967 is not likely to differ much from that for 1966.

The growth rate of fixed asset formation in the Community as a whole may be approximately the same as in 1966. There will, however, still be certain variations in trend from country to country. In Italy and France the available data on investment projects (backlog of orders in the capital goods industries, business surveys), and also the stage of the business cycle in these countries, suggest that industrial investment will expand considerably. The corresponding information for the Federal Republic of Germany, on the other hand, suggests that certain tendencies conducive to weakness will persist at least until the beginning of next spring. Subsequent recovery, however, of the propensity to invest is not unlikely in this country, especially if account is taken of the various favourable factors; these include the direct stimulating effects of the faster growth of exports and of the improvement in the balance of current payments; the improved liquidity position resulting from the changed trend in the balance of payments and, possibly, the easier situation that might ensue on the capital market; the somewhat larger profit margins, the intensification of competition and the resulting urge to rationalize. Recovery of the propensity to invest would not, of course, influence actual investment until the second half of 1967 or even towards the end of the year. In the Netherlands the tightness of the money and capital markets, the persistent upward thrust of costs and the prospect of somewhat slower growth also suggest that there will be some slackening in the trend of investment. In the Belgo-Luxembourg Economic Union industrial investment will probably expand only modestly.

The expansion of investment in construction (apart from industrial building, which generally reacts to the same influences as investment in plant and machinery) will probably not be very considerable in 1967. To judge by the latest trend of house-building permits granted in the Federal Republic of Germany and in France, growth in the housing sector will in the coming year at best be weak. In Italy, however, the present tendency for residential building to recover may establish itself as a vigorous trend.

For lack of sufficiently detailed information on the budget forecasts for 1967 the Commission is not yet in a position to make a sufficiently exact forecast of the trend of public investment in 1967. What is known of the broad lines to be followed in the various budgets suggests that investment by the public authorities will continue to grow quite rapidly in France and will perhaps accelerate somewhat in Italy; in most of the remaining member countries, on the other hand, it is to be feared that the endeavours to economize called for by budget policy will hit mainly this sector, where expenditure would then expand more slowly or not at all.

A similar lack of information prevents a sufficiently accurate forecast of the trend of public expenditure on goods and services, but in any case it will continue to expand vigorously.

It is already known that in most member countries the overall expenditure to be included in the government budgets will again expand considerably in 1967, unless the preliminary estimates now being prepared or under discussion are revised. In all Community countries except the Federal Republic of Germany these preliminary estimates are at least 10 % higher than those for 1966. The growth rates are smaller if the estimates are compared with the probable outturn for 1966. But just as in all member countries cash expenditure in 1966 will have been higher than had been proposed in the estimates for that year, it would be prudent to reckon that in 1967 cash expenditure may again turn out to be higher than was laid down in the budgets.

The rate of expansion of private consumers' expenditure may, for the Community as a whole, be approximately the same as in 1966. Should the rate be somewhat slower in monetary terms, the effect on the trend in terms of volume will be offset by a slightly slower upward movement of consumer prices; the volume of private consumers' expenditure may, for the fourth time running, again rise by about 4.5 % over the year as a whole. This medium-term regularity of the expansion of consumption in the Community in terms of volume is noteworthy; it shows that the fluctuations in the growth of consumption have been very largely offset by the differences in trend between one country and another.

The trend of private consumers' expenditure will continue to vary from one country to another in 1967. In the Federal Republic of Germany and in the Belgo-Luxembourg Economic Union, it will at least begin by expanding less rapidly, while in France and Italy it will still grow vigorously and perhaps even a little faster than before. It is still rather uncertain whether the expansion of private consumers' expenditure in the Netherlands will moderate, especially as the proposed tax changes have not yet been set out clearly. It has, however, been decided to implement at the beginning of 1967 the second stage of tax reductions on incomes and wages, and this will help to accelerate consumers' expenditure. It is not yet known for certain how far indirect taxes are to be raised during the year to offset these reductions. Such measures, however, would not hold down consumer expenditure, but would help to raise prices, and only in this way limit the growth of consumption in terms of volume.

As regards the trend of household incomes in the Community, it may be assumed that in the Federal Republic of Germany the tendency for increases in agreed wages to level off and for the gap between the actual wages and agreed wages to narrow will moderate the upward movement of the total wages bill for some time yet. In Belgium too, household incomes can no doubt be expected to rise more slowly as the labour market eases a little and the sliding wage scales come into play less frequently. In France and Italy, on the other hand, mass incomes may expand more rapidly in connection with the expansion of economic activity. It is still not certain whether the slightly slower growth

of business activity in the Netherlands forecast for 1967 will be reflected in a corresponding slackening in the upward movement of wages.

These revised prospects for the trend of demand in the Community still do not call for amendment of the forecasts on the gross Community product in 1967 made in the last Quarterly Survey. The Commission maintains its view that growth from 1966 to 1967 will be approximately the same as from 1965 to 1966, that is, about 4.5 %.

On account of the recent reversal in the Community as a whole of the trend in stocks of raw materials—mainly as a consequence of the quieter trend of world prices—it is particularly difficult to predict how the Community's imports will develop in 1967. It is conceivable, however, that the expansion of internal demand and production in the Community will show little change in relation to 1966 and will lead to a further appreciable increase in purchases abroad, especially as the downturn of the stock-building cycle should come to a stop about the middle of 1967. If at the same time the expansion rate of exports slackens somewhat, the trade balance (as defined for customs purposes) is unlikely to show any significant change.

It is also very difficult, of course, to forecast the trend of prices, mainly because important decisions remain to be taken on economic and financial policy, particularly in the sphere of taxation, and on social policy and wages. Nevertheless, there are sufficient reasons to assume that prices will continue to rise sharply, above all in the Netherlands; the rate of increase could be somewhat slower than in 1966, it is true, but it will probably still be the highest in the Community. A somewhat slower rise in prices can probably be expected in both the Federal Republic of Germany and Belgium, one factor being the easing of strains in the economic situation and on the labour market; in Belgium further factors are that no general and very appreciable increases in indirect taxes are planned for 1967, as they were for the beginning of 1966, and that the sliding wage scales are coming less and less frequently into play. In France and Italy the price trend—very modest in both countries, but especially so in Italy—could rise again rather more sharply as a result of the vigorous upswing of business activity.

The likelihood that the level of prices will continue to rise in some member countries—less rapidly than before, it is true, but still too vigorously—and that in others their upward movement may gather speed again is of course the main problem facing those responsible for short-term economic policy in the Community. This is, for instance, evident from the comments made in July 1966 by the Short-term Economic Policy Committee on the preliminary economic budgets for 1967; the Committee's memorandum is reproduced at the end of this chapter.

In accordance with its established practice, the Short-term Economic Policy Committee undertook at the beginning of July an examination of the member countries' preliminary economic budgets for the coming year and of the relevant comments and suggestions put forward by the Commission. It concluded that this time it would be of special importance for the authorities of the member countries to apply "a suitable combination of economic policy instruments" in order to combat the continued upward

movement of prices and costs or to avoid the emergence of new price strains due to economic expansion. The Committee once again drew attention to the vital importance of an effective incomes policy in the current situation of most member countries. The Committee's memorandum then indicates in detail the lines which should be followed by each member country, particularly in budget policy and in monetary and credit policy.

The Commission prepared its own analysis of the situation and its own forecasts, drew on the work done by the Committee of Experts on Economic Trends and the Committee of Experts on Economic Budgets, and consulted the Short-term Economic Policy Committee and the Monetary Committee; then at the beginning of July it submitted to the Council a proposal for recommendations to Member States concerning short-term economic policy in the second half of 1966 and the decisions to be taken early in 1967. The Council was asked to examine the proposal and to adopt the recommendations before the summer recess; in view of its tight programme of other urgent work the Council was unable to comply.

In substance, the content of the Commission's proposal corresponded in large measure with what was published in the last pages of Chapter I of the Commission's Quarterly Survey No. 2/1966 on "The economic situation in the Community", where the Commission gave its views on the requirements for a co-ordinated short-term economic policy.

Subsequent developments and information received on measures that have been taken or are to be taken within the Community and outside—in short, the most recent analysis of the situation and the prospects as they appear today—call for certain changes in the appraisal of the current economic situation and for modifications in some of the specific advice and proposals put forward by the Commission. In the Commission's opinion there is, however, still no reason for any basic change in the lines that should be followed in short-term economic policy or in the use to be made of the most important policy instruments. The essence of what had been said in the last Quarterly Survey—with which the Short-term Economic Policy Committee has really agreed in the memorandum referred to above—still holds good.

It holds good despite the fact that in some member countries the economic climate has cooled down a little further than had been foreseen, especially in the Federal Republic of Germany. This in turn will no doubt exert a healthy influence on the development of the economic situation in those member countries (Italy and France) which are at present experiencing an upswing in activity. The elimination of the expansionary influences which have been emanating from Germany will undoubtedly make it easier to contain the rise of overall monetary demand in these countries than would otherwise have been the case.

For the appraisal of short-term economic policy at Community level the latest economic developments and their foreseeable trend mean that there has been an appreciable improvement in the conditions for stabilizing prices and unit costs; what they do not mean is that stabilization has been attained, much less secured. As already pointed

out above, no one should be deceived by the stability of the consumer price indices in the summer months, as this was partly due to seasonal or exceptional factors. Any far-reaching relaxation of the anti-inflationary measures at present in force would certainly not be appropriate, let alone a policy on more expansionary lines than at present. In those member countries (the Federal Republic of Germany and Benelux) where the boom has been levelling off, on the contrary, short-term economic policy should, by and large, continue to have a damping effect until really satisfactory results have been obtained on prices, unit costs and current payments. Where overheating has shown little sign of cooling down (Netherlands), the policy of restraint should be made more effective; and in those member countries which are at present experiencing an upswing in activity—Italy and France—the expansionary impact of budget policy should be gradually reduced as the state of the economy improves.

The need to tighten up budget policy in the Federal Republic of Germany and in Belgium is as great as ever. The aggregate deficit on the budgets of the various public authorities needs to be reduced by slowing down the growth of expenditure—current expenditure rather than outlay on investment—or by raising current revenue, or by both these means; and there should be no financing of any deficits from resources which are not long-term domestic savings. Another reason why the authorities, especially in the Federal Republic of Germany, should tighten up budget policy is that the balances of payments have recently been having a far less restrictive effect on domestic liquidity than before or have even helped to expand it once again with the result that there is a tendency for the credit and capital markets to ease; the first signs of this are already discernible, even without any relaxation of credit policy measures, and it is a development which could certainly be accepted in view of the present tendencies of industrial investment; but a further increase in liquidity, such as could result from an easing of credit policy, does not yet seem justified.

Of course, any easing in the liquidity situation brought about by developments in the balance of payments should not immediately be used by the authorities to maintain their deficits at a high level or even to increase them; there seems to be a danger of this in Belgium in particular, where the scope for expenditure under the extraordinary budget is appreciable and where spending under this heading is generally geared to the level of liquidity on the money and capital markets.

In Belgium it is particularly important that the authorities, regardless of the funds that could be raised on the markets, should reduce the overall deficit by measures which improve the balance of the country's ordinary budget, so that the Government itself shall as far as possible do some saving and consequently be able to finance part of its extraordinary expenditure from its own resources. More funds would then be available on the market for non-inflationary financing of growing industrial investment. A similar recommendation holds for the Federal Republic of Germany, where a reduction in the deficit and the consequent reduction in the calls made on the capital market by the public authorities would also free more capital for financing industrial investment (including residential construction).

At the time when this report is being prepared, serious efforts are being made in both these countries to adapt budget policy more closely to the needs of short-term economic policy or to the financial situation. In Belgium it has at least been possible to avoid a deficit in the preliminary estimate for the ordinary budget, although this was thanks to probably rather optimistic forecasts of receipts and to certain revenue items being counted twice owing to a change in budgetary accounting decided upon long ago. Despite this limited success, the expansion of current expenditure in Belgium (most of which affects consumption directly or indirectly) still seems to be too vigorous.

In the Federal Republic of Germany, the draft budgets provide for growth rates of expenditure of over 8 % for the Federal Government (including the "shadow budgets"), about 6.5 % for the Länder and about 7 % for the local authorities, the comparison being between the estimates for 1967 and the estimated outturn for 1966 <sup>(1)</sup>; the aggregate financing deficit for these budgets will not be smaller than in 1966, though less than in 1965. One achievement is that though the bids made by departments were at first substantially higher, considerable cuts were made. It is regrettable, however, that in Germany they should have been made largely in expenditure intended directly or indirectly for investment. Nothing can be said yet on the balance of the Federal budget, as the Federal Government's share in receipts from the income and wages tax for 1967 has not yet been fixed. The situation is similar in the Länder. That better co-ordination is required is clearly shown by the fact that in the budgets being prepared for 1967 the Federal Government assumes that its share of the receipts from the income and wages tax will be maintained at the present level, while the Länder assume that this level will be reduced. It is therefore urgently desirable that the laws on stabilization of the economic situation be passed without delay. These laws provide not only for certain improvements in the range of instruments of economic policy, but also for better co-ordination between Federal Government and Länder of budget policy and borrowing arrangements; the provisions on co-ordination should be implemented immediately, so that they apply to the 1967 budgets. This action should be accompanied in this country, as in Belgium, by further efforts to curb the growth of expenditure.

In Germany and Belgium the restrictive character of credit policy should be maintained for a while at least. This does not mean of course that complete inflexibility is advisable. It is conceivable that, if developments in the balance of payments led to easier conditions on the money and capital markets, and if a less avid demand for borrowed money moderated the expansion of credit, interest rates might show some propensity to fall; if such a situation arose, its existence might be confirmed—or recognized—by a change in bank rate. Likewise, the maintenance of quantitative ceilings for the expansion of short-term credit to business customers would no longer be indispensable if total outstanding credit remained for a time below the ceiling. A less strict monetary and credit policy could, of course, be considered if budget policy were tightened up sufficiently.

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<sup>(1)</sup> This does not take into account expenditure in 1966 amounting to DM 1 000 m. which will be paid to the United States for purchases of defence equipment in that country and the DM counterpart of which will be obtained by borrowing on the home money market.

In the Netherlands, where there is still no sign of any distinct easing of the considerable strains which have beset the economy for nearly three years, the re-establishment of domestic equilibrium probably requires further efforts, especially as there is reluctance here, despite the persistent upward trend of costs and prices, which has slackened only slightly, to give up the further appreciable cut in income tax planned for the beginning of 1967; this is the second stage of a reduction decided upon some time ago—the first was implemented in mid-1965. If the budget policy of the public authorities is to help stabilize prices and costs (and this is still very necessary in the Netherlands), the expansion of public expenditure must be strictly limited in 1967; should this not suffice, additional income must be obtained from taxation. The Government's efforts seem to be aimed in this direction, but it is regrettable that measures taken to curtail expansion will cut rather deeply into investment. The Government also intends to speed up the collection of direct taxes. This too will hardly restrict the growth of expenditure on consumption, but it will affect the ability of firms to finance their own investments. Finally, the authorities apparently intend to raise indirect taxes once again. All in all, the situation seems to be still rather precarious, although the Government's draft budget is said not to affect the business situation in either direction: the deficit budgeted for 1967 should turn out to be appreciably smaller than the probable deficit for 1966. It is, however, noteworthy that the latter—according to estimates—will be roughly twice as large as provided for in the 1966 budget, and that in 1967, as almost always in the past, the estimates may again be exceeded, especially as the budget seems to assume unduly low wages in the private sector. In the circumstances the Netherlands, unlike other countries in which some relaxing of curbs on the money and the capital markets might be tolerable, could find it advisable, at least for the time being, to maintain its restrictive monetary and credit policy in as effective a form as possible.

In Italy and France, where overall demand is expected to expand faster than in 1966, the main task of the authorities responsible for short-term economic policy is manifestly to ensure that the sharp rise in demand is contained within appropriate limits, so that in France the tendency for prices to settle can continue, and in Italy the degree of stability achieved may be maintained. The latest developments and the outlook for 1967 confirm the view that after all these Governments should perhaps apply a somewhat less expansionary policy in 1967 than is apparently being planned. Otherwise there is a risk that the upward movement of prices may regain strength.

In France, to judge from the draft budget, the growth of expenditure proposed for 1967 (some 10 % higher than in the budget for 1966) will be fairly sharp. The growth rate is smaller when the expenditure planned for 1967 is compared with the outturn estimated for 1966, which exceeds the original budget figures (mainly because of unexpended balances carried forward from previous years) and if it is assumed that in 1967 there will be little if any such overstepping of the budget figures; but such an assumption suffers, of course, from the uncertainty of the factors involved. In the circumstances, therefore, there is a chance that the financing deficit which has faced the Government in its execution of the 1966 budget may recur or even increase in 1967. The increased calls which the Treasury will be making on private savings could aggravate the financing situation of private firms, which is already difficult and likely to remain so. The conse-

quence may be either that the welcome upswing of investment by private firms, which is now in the initial stage, is restricted too sharply or that too large a share in the financing of such investment is done on bank credit; this second alternative could engender further inflationary symptoms. The trend of bank loans to commerce and industry over the last few months seems to show that the shift towards the banks is already beginning. If the necessary tightening up of budget policy were not ensured in the course of the practical implementation of the budget, credit restriction would have to be reimposed within a short time.

Similar problems have to be faced in Italy, though here the elasticity of production is still very high and there therefore seems to be little danger of inflation. In Italy the current increase—and that planned for 1967—of public expenditure directly affecting or indirectly promoting consumption is certainly too fast, while investment expenditure is making rather hesitant progress. In addition, a considerable part of the persistent and very heavy deficit continues to be financed by recourse to the money market. But when account is taken of the private sector's need for long-term resources with which to finance the current revival in its own investment, too heavy a burden is being placed on the savings of the other sectors by the claims being made on them by the public authorities, who are seeking funds to cover their own expenditure or that of public sector enterprises. In addition, a measure has recently been discussed in Italy which would limit, relatively at any rate, industrial self-financing, namely a considerable reduction in the share of social burdens assumed by the State.

An attempt should therefore be made in Italy, too, to limit more strictly the expansion of public current expenditure on goods and services which, despite efforts made by the Government, is still considerable, and thus to reduce the total deficit in 1967 more appreciably than is being planned in the budgets. The partial financing of the deficit by direct or indirect recourse to the central bank could then be progressively reduced; this is all the more advisable since the liquidity of the banking system is in any case still very high, mainly because of the balance of payments surpluses. A sharp acceleration occurring in the expansion of credit would no doubt call for the closest attention on the part of the authorities responsible for monetary and credit policy. Otherwise a process could start off which sooner or later would be bound to assume inflationary proportions.

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At its meeting on 28 July, the Council adopted a recommendation to the Member States that they should "take certain measures for improving statistics on the current economic situation". This recommendation was based on a proposal which the Commission had submitted to the Council as far back as June 1965. During the preparatory discussions in the Committee of Permanent Representatives and its sub-committees, the text subsequently adopted by the Council certainly underwent some modifications; there is no doubt, however, that the recommendation represents an important step towards the



improvement of statistical reference material required for the analysis and the co-ordination of short-term economic policy at Community level. Those Member States which still have leeway to make up in connection with statistics on the current economic situation, particularly Italy, Belgium, Luxembourg, and in certain respects France too, would themselves benefit if they followed the recommendation, of which the text is given as an annex to this Survey.



**Opinion on the preliminary economic budgets for 1967**

Brussels, 28 July 1966.

1. At its meeting of 12 and 13 July 1966 the Short-term Economic Policy Committee examined the preliminary economic budgets for 1967 and the problems of short-term economic policy foreshadowed by tentative estimates for the coming year.
2. The Committee notes that the outlook for economic growth, employment and the balance of payments is in general good. On the other hand, the upward trend of prices and production costs, which has continued for a number of years, is still causing grave anxiety in most countries of the Community, although it has lost momentum in some of them.
3. According to the preliminary economic budgets for 1967, Community exports should rise as rapidly in 1967 as in 1966. As long as no important change occurs in the world political situation, the increase of exports to the United States and the other industrial countries should be smaller, but Community exports to the developing countries will rise more rapidly.
4. Monetary demand within the Community should also increase in 1967 at approximately the same rate as in 1966. A somewhat slower development of private consumers' expenditure, mainly attributable to a slowing down of its expansion in Germany, should be largely offset by a stronger upward trend of gross fixed asset formation, particularly in France and Italy.
5. Under these circumstances, the real gross national product of the Community is expected to rise by some 4.5 %, the same rate of growth as for 1966. The position should ease in member countries where a fairly severe shortage of labour has persisted in 1966. Italy's position in the labour market should remain fairly comfortable despite a certain drop in unemployment. According to estimates for 1967 made by the Commission, labour needs should increase considerably in France and lead to strain in at least some sectors; but French experts feel that the labour market will on the whole remain free from strain.
6. Since the brisk expansion of demand within the Community is likely to continue, imports from non-member countries may be expected to increase vigorously

in 1967 too, in any case more rapidly than exports. As a result the Community's merchandise trade balance and current account are likely to deteriorate again. As in 1966, this trend should, however, remain within relatively moderate limits.

7. According to the preliminary economic budgets the upward movement in consumer prices in all Community countries should tend to slow down, nevertheless, it may still be quite considerable in most countries, particularly the Netherlands and Belgium. A slower upward price trend would, however, not be wholly due to purely business factors : it is assumed that normal weather will mean that the prices of some foodstuffs will not be forced up unduly. In the Committee's view, some caution is required in the assessment of expected price increases—experience has shown that in recent years forecasters have tended to underestimate the scale of price increases.

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8. The Committee concludes that the problems of short-term economic policy likely to arise in 1967 differ only slightly from those arising at the beginning of 1966 as outlined in the opinion of 7 Mars 1966 on the economic budgets for that year. The stabilization of price and cost levels per unit of output should be the most important aim of short-term economic policy in most countries of the Community; in Member States at present enjoying a calmer price climate, economic expansion should be prevented from causing further strain in prices.

9. For this purpose, the governments of Member States should use a suitable combination of economic policy instruments. In this connection, the Committee wishes to stress once again the importance of an effective incomes policy, which is a particularly powerful instrument for reconciling a satisfactory economic growth and a high level of employment with relative price stability.

In the countries still only at the beginning of the move back towards stability, the incomes policy would be the more effective if backed in coming months by an adequately restrictive monetary and budget policy designed to relieve the tendency to strain in these countries.

An effective incomes policy should mean that employers and employees in association with the authorities would sign contracts or conventions on the desired development of the specific income categories. In the view of the Committee, special efforts should be made in respect of wage policy, since wages increased very much more rapidly than production last year in most countries.

Moreover, the authorities of the countries where there are sliding wage scale clauses should investigate in association with employers and employees how these clauses can be adapted to mitigate the disadvantages of certain indexing methods.

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10. In Germany the restrictive policy should be maintained since the handling of budgetary expenditure by the public authorities taken as a whole has continued to have an expansive rather than a restrictive effect on the economy in the early months of 1966, even though the impetus from the federal budget has been distinctly weaker. It is the Committee's view that efforts must be continued to reduce the budgetary deficit of the public authorities as a whole. Care should be taken first and foremost to restrict federal budget expenditure in 1967 so that borrowing on the capital market can for the most part be avoided. Moreover, the federal authorities should call upon the Länder and local authorities, whose budgets imply considerable recourse to credit, to adopt similar methods. In this connection, prompt adoption of the Stabilization Law by the legislative authorities would be particularly welcome.

In the field of credit policy, the monetary authorities should maintain the existing restrictions as long as undue strain on the labour market persists and until the trend of prices shows a distinct loss of momentum.

11. In the Netherlands, too, the development of public finance is boosting domestic monetary demand. It is true that the certain indirect taxes increased at the beginning of 1966 are curbing demand, but the expenditure of the public authorities has continued to climb sharply. The latest restrictive measures introduced, which are in any case quite mild, are unlikely to influence the budget trends for 1966 to any appreciable extent. It would therefore be desirable to limit the expansion of public expenditure severely in the 1967 budget. Should the impact of the budget on the economy prove so strong however (as a result of the combination of a rise of expenditure and the planned reduction of certain direct taxes) that the recovery of equilibrium is impeded, further taxation measures would be unavoidable. In view of the scale of local authority expenditure, the central government should also endeavour to reduce the financing deficit of these authorities.

The monetary authorities have recently further tightened up their credit policy. If budget policy does not play its proper restrictive role and if as a result the sharp rise in prices and costs continues, economic equilibrium can only be recovered by means of a very severe contraction of liquidity, in other words inevitably by fits and starts. This would also mean that the rate of growth of the Dutch economy would be much lower.

12. Despite a considerable tax increase at the beginning of 1966 the net contribution to demand from the Belgian central budget has not diminished, since expenditure continues to mount sharply. The budget deficit in 1966 should be much the same as in the previous year, chiefly because of the still very rapid expansion of consumption and transfer expenditure.

In view of the steep rise in prices and costs it would be advisable nevertheless to cut back the budget contribution to demand again in 1966 and also in 1967. Thus it is the Committee's opinion that the authorities should apply particularly severe standards when making their estimates for 1967. Moreover the remarks in section 11 concerning the budgets of local authorities and the expansion of credit also apply *mutatis mutandis* to Belgium. A better equilibrium of public finances also appears to be essential to permit the rise in interest rates to be slowed down and to provide an adequate volume of capital

for the expansion of private investment, which is essential to the expansion of production and the improvement of productivity.

13. The economic prospects for 1966 in the Grand Duchy of Luxembourg are relatively unfavourable in view of the conditions in the world steel market; they may, however, slightly improve in 1967. If the other Community countries, in particular Belgium and Germany, are able to keep upward price trends within bounds, this will have a good effect on the level of prices in Luxembourg because of the country's heavy dependence on imports.

Private consumption and the cost of living will in particular be considerably influenced by public finance operations. Consequently a cautious budget policy should be pursued in 1967.

14. In France the budget policy for 1966 is approximately in line with current economic requirements : central government income and expenditure will virtually balance out for the full year. On the other hand, the social insurance accounts will show a deficit and the local authorities will have a considerable need of finance. Although the current outlook does not give cause to fear a change in the relatively stable price conditions, the public authorities should leave open the possibility of modifying the rate of actual expenditure if there should be a recurrence of strain during this year. At the same time the policy for promotion of public investments and directly productive industrial investment should be continued.

The trend of credit demand should be watched particularly carefully; should it gather further momentum, the monetary authorities should, in the Committee's opinion, consider the case for the re-introduction of a system of credit restriction designed to prevent undue expansion of liquidity.

15. In Italy budget measures are at present serving to boost domestic demand. The central government's budget deficit will be higher than in 1965. In view of the higher rate of economic expansion, the Committee is of the opinion that the authorities should gradually scale this deficit down. It would also be advisable gradually to restrict the financing of the deficit from short-term funds and to prevent an excessive increase in the already very abundant liquid resources.

Another point in favour of a cautious budget policy is that a steady upward trend in private investment is an important prerequisite for the maintenance of expansion. To prevent excessive official borrowing on the capital market from draining off too much available capital and forcing interest rates up and to prevent the increase of direct productive investments from being inhibited, the growth of public expenditure must be kept within limits compatible with a balanced expansion.

16. In so far as the above-indicated policies are in fact implemented, the Belgian and Netherlands authorities will be able to relax the measures adopted in May 1966 to tighten up prices controls. In France also a further easing of price control would be desirable.

17. Finally, the Committee indicated the instruments likely to promote balanced economic development in the long-term and which—adapted according to country and situation—might be more fully applied in the Member States: promotion of savings activity, combating of restrictions on competition, closer supervision of prices in markets on which competition is not perfect, promotion of mobility of labour between sectors and trades. Should the upward trend of prices gather pace, the authorities should also consider making selective reductions or suspensions of customs duties.

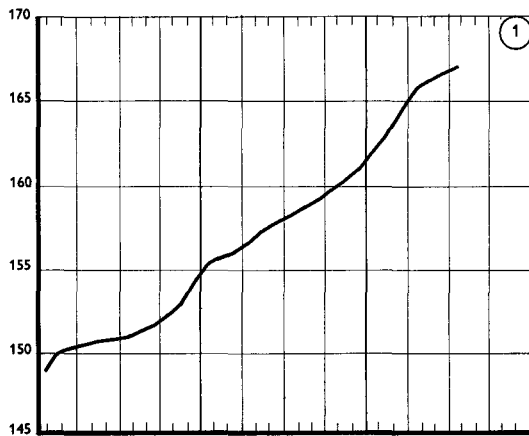




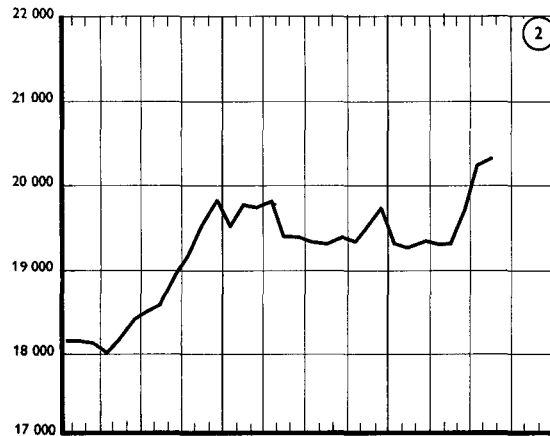
## ECONOMIC INDICATORS

Industrial production

1958=100

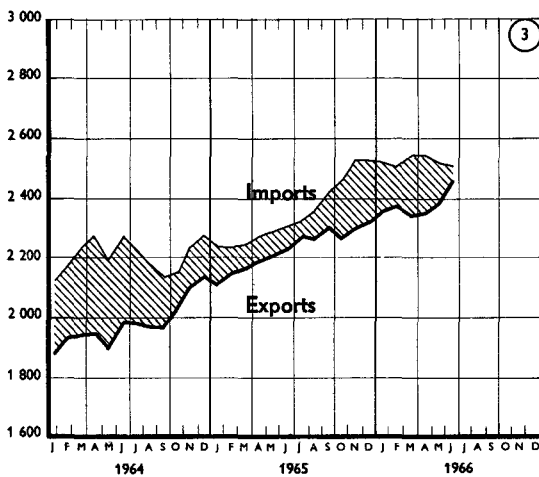


Gold and foreign exchange reserves million u.a.



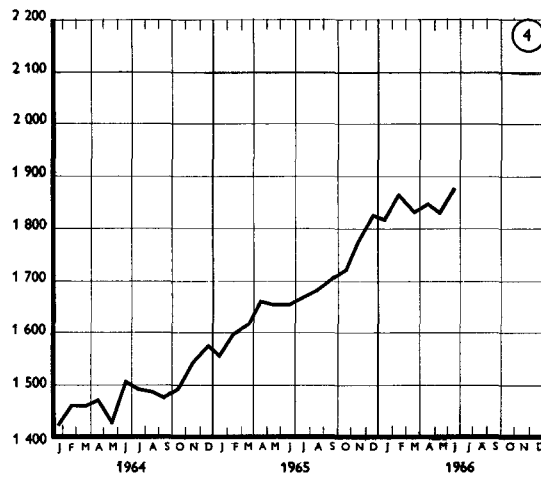
Trade with non-member countries

million u.a.



Trade between member countries

million u.a.



## 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 1964 GNP
	1959	1960	1961	1962	1963	1964	1965		
Gross Community product	5.2	7.8	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	6.3	6.2	6.3	5.9	4.4	4.3	144	61
Gross fixed asset formation	8.2	10.7	10.0	7.1	5.1	8.2	3.3	164	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	4.3	6.8	4.4	4.3	3.2	4.6	3.0	134	—

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	173	173	173						
Imports from non-member countries (cif, million u.a.)	1964	2 288	2 168	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	2 368	2 380	2 352	2 404	2 156	2 386	2 443	2 558	2 754
	1966	2 516	2 367	2 732	2 525	2 563	2 622						
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	2 289	2 380	2 367	2 649
	1966	2 153	2 179	2 567	2 372	2 451	2 502						
Balance of trade (million u.a.)	1964	- 397	- 308	- 278	- 342	- 326	- 288	- 201	- 155	- 55	- 18	- 125	- 169
	1965	- 307	- 22	- 8	- 196	- 131	- 160	- 56	- 159	- 97	- 63	- 191	- 105
	1966	- 363	- 188	- 215	- 153	- 112	- 120						
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	1 442	1 576	1 801	1 630	1 661	1 691	1 735	1 437	1 734	1 871	1 812	1 933
	1966	1 654	1 790	2 037	1 858	1 902	1 968						

## 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. 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 second quarter and the summer months the expansion of overall demand continued to slacken and the tendency for excess demand to contract therefore also persisted. This began to affect the labour market and prices, without—so far—putting an end to the labour shortage or even arresting the upward trend of prices. A pause in the rise in the cost of living was partly due to special temporary factors.*

*Demand and production are now going through a phase of slower expansion but there are no symptoms of an economic crisis; structural weaknesses are, however, becoming more clearly evident. Stabilization is curbing growth, but there is no danger that expansion will cease, much less give way to a decline.*

*On the contrary, the growth rate for 1967 could well show a further increase, were it only because exports will have risen faster: this will also ease the monetary situation. A prerequisite for the maintenance of equilibrium in this process is an economic policy still—at least for the time being—aimed at stabilization. In particular, the authorities must continue to curtail the expansion of public current and transfer expenditure so as to cut back further the overall deficit on the budgets. This would also free a larger amount of savings for non-inflationary financing of industrial investment.*

### 1. Recent developments

The expansion of overall monetary demand slowed down further in the second quarter and, as far as can be seen at this stage, was still doing so at the beginning of the autumn. Slacker domestic demand, was the decisive factor here: exports of goods and services (foreign demand) made fairly marked gains, in part precisely because domestic demand was flagging, but also because demand from important customers of Germany rose sharply.

Merchandise exports in particular continued their advance in the second quarter. Foreign trade statistics show year-to-year increases for the second quarter of about 13 % (value) and 11 % (volume). Exports for July were 11 % up in value on the same 1965 figure. Increased deliveries to the other EEC countries, particularly Italy and France, a sharp increase in exports to the United States and brisker sales to the developing countries were the main factors in export expansion.

The tendency for domestic demand to slacken has continued and become more widespread. Gross fixed asset formation, affected first and hardest by this trend was generally running at a fairly low level in the second quarter. Even so, the volume of

investment in plant and equipment would appear to have been 3 % greater than at the corresponding time in the previous year. The clearest signs of the quieter trend of capital investment since the middle of last year were revealed by the position in the mechanical engineering industry, whose domestic sales figures in the second quarter were only 4.6 % higher than a year earlier, and by the slower expansion of imports of capital goods, which had previously climbed sharply. The investment boom is, then, over, and the main reasons for this have already on several occasions been analysed in some detail in these Surveys : narrower profit margins have deterred managements, as have the scarcity and increased cost of other funds for financing rising investment in fixed assets; businessmen have also had doubts, partly prompted by cyclical factors, with regard to market prospects and are not over-anxious to embark on schemes for additional plant.

Investment in building, which had soared in the first quarter thanks to the fine weather, was subsequently marked as a whole by the slacker underlying trend which had already been observable earlier.

The overall movement of stocks also provided no expansionary stimulus. In particular, a more cautious line appears to have been taken again with regard to stocks of raw materials and semi-manufactures. Manufacturers' stocks of finished goods also seem to have built up further. In the retail trade, too, there were signs of increasing pressure of stocks, due to slight decline in sales.

Since the spring, consumers' demand has in fact been increasingly affected by the tendency for the investment boom to lose momentum. This does not, of course, apply to public current expenditure, the rate of increase of which doubtless did not slacken appreciably. On the other hand, the rise in private consumers' expenditure, which was still vigorous in the early months of 1966, has since lost momentum. Retail sales in the second quarter were 5.8 % up on the same 1965 figure, whereas in the first three months of 1966 the year-to-year growth rate had been over 10 %. It should, however, be borne in mind that the contrast is exaggerated to some extent by the Easter shopping rush falling at different times and by the fact that the trend of other consumer expenditure headings, especially services, remained fairly expansionary.

The slackening of the growth in consumption is mainly attributable to the slower rise in incomes; this, however, has now had a more direct effect on private consumption, whereas in the first quarter consumers had reacted to smaller incomes improvements mainly by saving less : the rise in total gross wages and salaries slowed down appreciably in the economy as a whole, the year-to-year growth rate by the second quarter having been only about 7.5 %. At the same time the amounts withdrawn from their businesses by self-employed persons would appear to have risen only moderately, so that altogether the disposable income of private households showed a distinctly weaker upward trend than previously. However, the savings ratio declined again in the second quarter.

The moderation of the expansion in monetary wage and salary incomes is mainly due to the tendencies towards an easing of the labour situation which, although at first scarcely perceptible in the labour returns, had in fact been evident for some time in the



firms themselves. These tendencies have now also been reflected in the statistical series. The adjusted trend for the number of new vacancies reported has dipped sharply. The number of persons employed in industry and the building and civil engineering sector has also declined faster than before. In industry the reasons for this lay—apart from the reduction in the number of workers in the mining sector—mainly in the contraction of the labour force in the iron and steel producing industry and the building-materials industries. For the first time in many months there has been a slight increase in the seasonally adjusted number of unemployed persons. All of this, however, has not yet brought the labour market back to normal. The unemployment rate [the number of unemployed as a percentage of the total number of employees (employed and unemployed) at the end of July was 0.4 %, which must be regarded as very low even if the seasonal element (not eliminated in this case) is taken into account.

A further slight slowdown in the rate of growth of domestic production was the reaction to the slackening of the expansion in overall demand.

Industrial production especially showed only a very slight upward trend from the first quarter to the second. According to the Federal Statistical Office's index of production per working day, it was only 3.2 % higher in the second quarter than in the same quarter of 1965. In some capital goods industries the underlying trend of output continued downward. In general, however, there was no further appreciable aggravation of the decline of output from these industries. In the consumer goods industries, on the other hand, a very rapid rate of expansion of production seems to have given way to a slower growth rate.

Agricultural production, however, (although admittedly it can hardly be regarded as being, on the whole, sensitive to the general economic trend), showed an improvement on last year. Even though the harvest prospects were in some cases impaired by the wet summer, the cereal harvests, in particular, and also the crops of potatoes and vegetables, turned out better. Output of livestock products also appears to have improved on the 1965 results.

The reaction of the adjusted trend of imports of goods and services to the slackening of the expansion in overall demand, although substantial, was by no means as pronounced as the overall import figures suggest. According to customs returns, by the second quarter the year-to-year increase in merchandise imports was only 4.7 % in value and 2.6 % in volume. One reason was the remarkably small volume of imports of foodstuffs in this quarter owing to the increase in domestic farm production; secondly, imports on government account were very low. On the other hand, while purchases of semi-manufactures showed a downward trend (adjusted) and raw material imports rose only slightly, in both cases as a result of the general slackening of activity, commercial imports of manufactures nevertheless continued to rise at an appreciable rate—admittedly not as quickly as hitherto, but considerably faster than domestic output. Lastly, tentative reports on the holiday period indicate that the imports of services in the form of expenditure on holidays abroad increased substantially.

Despite what has so far been an almost uninterrupted rise in costs, however, the lighter pressure of excess demand does already appear to have begun to moderate the movement of prices. The index of industrial producers' prices had not risen further since May; in August it was 1.5 % above the August 1966 figure. True, this was partly attributable to declining world prices for goods at initial processing stages, whereas upward pressures on prices were still appreciable for goods at the later processing stages. Indeed, consumer prices, apart from seasonal variations, continued to rise at the former brisk tempo. The appreciable slowdown of the rise in the cost-of-living index in the summer months—the index in August having been “only” 2.9 % higher than the figure for August 1965—was mainly due to the improved supply position for farm produce, especially of crop produce, compared with last year. Excluding food, beverages and tobacco, the rise in the index over last year increased to as much as 4.3 %.

As a result of the export and import trends described above there was a further appreciable improvement in the trade balance (merchandise). According to the foreign trade statistics, the trade surplus in the second quarter was DM 1 400 million, compared with DM 800 million and DM 600 million in the two preceding quarters.

This movement of foreign trade led to a considerable improvement in the current account, although this is burdened by substantial transfers, primarily reparation payments and remittances made by foreign workers to their home countries. Despite continued heavy net expenditure on services, the current payments deficit fell to DM 406 million, or two-fifths of the first quarter's deficit. In the second quarter of 1965 the deficit was DM 2 600 million.

The surplus on capital movements (excluding the changes in the commercial banks' net foreign exchange holdings but including the statistically unclassifiable residual item) remained high in the second quarter; it amounted to DM 600 million, despite the fact that in May payments to increase Germany's IMF quota and its share in the capital of the IBRD entailed the export of DM 438 million (the balance of Germany's transactions with these institutions). The capital inflow was reflected, in turn, in a large surplus in the residual item of the balance of payments, which can in fact be regarded as largely representing unrecorded capital movements. There have apparently been further speculative capital inflows (in connection with the sterling crisis), as well as considerable borrowing abroad.

Thus the overall balance of payments in the second quarter closed with a small surplus which was reflected in a rise of DM 170 million in the Bundesbank's net gold and foreign exchange reserves and a slight deterioration in the net foreign exchange position of the commercial banks.

The influence of the balance of payments on bank liquidity in the second quarter was again expansionary, all the more so because the afore-mentioned transactions with the IMF and IBRD were financed by the Bundesbank. In addition, the official cash transactions added substantially to the banks' funds, and the rise in the note and coin circulation was relatively small. Altogether the banks' freely disposable liquid funds declined

in the second quarter by DM 400 million—a smaller decline than in the first quarter (DM 2 600 million), despite the continued rapid expansion of bank lending. The rise in credit to commerce, industry and individuals has not, however, been as fast recently as it still was in the first quarter. This is partly because bank liquidity has so far been tight, but it might already be partly attributable to the slower expansion in demand for credit, directly and indirectly connected with the current less buoyant trend of investment.

At all events, the tendency of interest rates in the money markets was slightly downwards in the summer, and even bond prices rallied a little. Lastly, improvements in share prices were also probably not altogether unconnected with the trend of liquidity; they doubtless also reflect the fact, however, that recent profit tendencies, and especially business prospects for the foreseeable future, are not assessed anything like as unfavourably as might be concluded from many statements made in business circles and in the press.

## 2. Outlook

Overall demand will probably continue to slow down between now and the end of the year and also in the early months of 1967.

Demand from abroad seems likely to remain the main component of overall demand for the time being, continuing to make an appreciable contribution—if anything even stronger than hitherto—to business activity. For one thing, the power of absorption of several major foreign markets is growing further owing to the very brisk expansion of demand and economic activity in those countries. Secondly, German industry's export effort and ability to deliver the goods are increasing as the expansion of domestic demand slackens. The amount of foreign orders coming in, which was about 15 % greater in the second quarter than in the corresponding period last year, points to a rise in exports in the coming months. The upward trend of orders from abroad has again been most pronounced in the capital goods industries; recently, however, the consumer goods industries, too, have been stepping up their export drive appreciably.

Outlay on gross fixed asset formation will probably continue—though rather hesitantly—at the present high level. Although there does not appear to have been any further deterioration in industry's propensity to invest, even a return to conditions more conducive to capital investment could no longer affect the actual outlay for that purpose this year. Expenditure on equipment is thus hardly likely to show any further fundamental upward movement, and may even mark time. At all events, the decline in the domestic orders received by the capital goods industries continued into the summer months.

The expansion in expenditure on building, too, will make only a modest contribution in coming months. In this sector, order books have been shortening since the spring. There has been marked restraint in the placing of orders for public building, especially by the Länder and municipalities, which have run short of funds. In isolated cases the financing difficulties have even led to the postponement of building project already started.

In the housing sector, orders placed have recently, for the first time in three years, shown only a slight rise.

The expansionary trend of public current expenditure will probably not slacken much, especially as the implementation of wage and salary increases already granted to public employees is due before the end of the year.

In coming months the tendency for the expansion of private consumers' expenditure to slow down is likely to gain some strength, particularly as a lower growth rate for the production of consumer goods is now an additional factor helping to ease the labour situation and thus to moderate the upward movement of wages. But there is certainly no likelihood of a decline in private consumption. There are many signs that consumers' expenditure will continue at about the present rate.

In view of this development of demand, the growth in production in the coming months will be small. It will probably not cease altogether, though, especially as imports of goods and services (apart from seasonal variations) will slow down more and more. Merchandise imports, in particular, will increase only to a modest extent in the coming months.

The loss of momentum in the upward movement of prices might become a little more pronounced. For one thing, the reduction in the pressure of excess demand is setting increasingly narrow limits to the introduction of price rises to offset higher costs. Secondly, costs themselves are tending to rise somewhat more slowly. Lastly, price conditions in the consumer goods market should improve further owing to the more favourable trend of foodstuff prices compared with last year. There will, however, certainly be no genuine price stabilization yet; appreciable upward price tendencies will persist and the general trend will remain unsatisfactory. The main reason for this now is that there is a time-lag in the slowing-down of the rise in costs and that in this phase of the business cycle experience shows that, even in the face of slackening demand, business men still try for a while to pass on cost increases to the customer.

In view of the slower growth of imports and the rapid expansion in exports, a heavier surplus on the trade balance can once again be expected. In the last months of the year the surpluses in respect of merchandise trade may well already become large enough again to offset the deficits in the other items of the current balance of payments.

Economic developments so far and the latest forecasts of trends between now and the end of the year remain, for the most part, in line with the forecasts published in the last Quarterly Survey (2/1966) for the results for the whole of 1966 in comparison with 1965. Despite minor changes in individual items (which will involve, among other things, an increase in the "external contribution") the increase in the real gross national product can still be put at about 3.5 %.

As to the probable course of economic activity in 1967, there is no reason substantially to modify the lines of development indicated in the last Survey. Although the outlook in the present transitional phase of the business cycle is admittedly very uncertain, many factors suggest that the pace of economic expansion will quicken again in the course of 1967. Demand from abroad will probably continue to expand rapidly and exert an increasing expansionary effect on business activity as a whole. This is all the more likely as growing exports combined with what is likely to be a slacker trend of imports and the resultant continued improvement in the current balance of payments will increase the liquidity of the money and capital markets after a period when liquidity has been scarce. Added to this there is a tendency for profit margins to widen again, due to the slower upward cost movement and the trend of sales. All this could lead to a further change in investment conditions in the course of 1967, with capital spending thus lending renewed support to the expansion of domestic demand. The extent to which the tempo of domestic economic activity will quicken again in the coming year naturally also depends largely on economic policy. At present, at all events, the Commission's staff think it possible that there may be a slight acceleration of the growth in the real gross national product, which could well rise by about 4 % for 1967 as compared with 1966.

*National product and expenditure*

	1963 <sup>(2)</sup>	1964 <sup>(2)</sup>		1965 <sup>(2)</sup>		1966 <sup>(3)</sup>	
	At current prices (in DM '000 million)	% change on preceding year					
		Volume	Value	Volume	Value	Volume	Value
Gross national product	377.6	+ 6.6	+ 9.6	+ 4.6	+ 8.5	+ 3.5	+ 7
Imports <sup>(1)</sup>	70.0	+ 10.7	+ 11.8	+ 14.3	+ 17.5	+ 5.5	+ 7.5
Private consumption	215.9	+ 5.3	+ 7.8	+ 6.3	+ 9.8	+ 4	+ 7.5
Public current expenditure	59.2	— 0.1	+ 4.5	+ 6.4	+ 12.8	+ 1.5	+ 6
Gross fixed asset formation	95.3	+ 11.8	+ 14.5	+ 6.5	+ 8.8	+ 2.5	+ 5
Exports <sup>(1)</sup>	75.0	+ 9.6	+ 11.4	+ 6.6	+ 9.1	+ 9.5	+ 11.5

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> Federal Statistical Office "Wirtschaft und Statistik", No. 3/1966.

<sup>(3)</sup> Commission forecasts.

*Note:*

(a) The difference between the figures for product and those for expenditure is accounted for by movements in stocks.

(b) The 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 on the sole responsibility of the Commission.

The unmistakable underlying tendency for excess demand to contract is improving the prospects of a reversion in the foreseeable future to a balanced and yet sufficiently high rate of economic growth. To exploit and promote opportunities in this connection is at present the main task facing those in charge of economic policy.

The policy pursued must on no account aim at checking—perhaps prematurely—certain trends, inevitable after the inflation of the past few years, which are due to cost and price stabilization—namely lower industrial investment, slower expansion of demand, and weaker economic growth. It would be a mistake to attempt to counter these trends by, for example, relaxing credit restrictions or maintaining the unduly expansive budgetary policy.

Despite some misgivings, there is no danger of tendencies in the economy of the Federal Republic assuming the proportions of a deflation crisis. Even a modest temporary decline in industrial investment would not be such a serious disadvantage as is sometimes asserted. For it should not be forgotten that nowadays all comparisons are made with a level of capital expenditure—that of the first half of 1965—which was the result of an inflationary investment boom. Moreover, allowance must be made for countervailing forces emanating from the economies of the importing and competing countries and exerting an expansionary influence on the German economy. Lastly—and there can hardly be any doubt about this, despite all the activity in the field of public budgetary policy—public expenditure in 1967 will again make a definitely expansionary contribution to the domestic economy.

The foregoing remarks should not, of course, be interpreted to mean that permanent stabilization of the trend of capital investment would be welcome. On the contrary. In the first place, there is undoubtedly a heavy backlog to be made up in the field of public capital projects; in this sphere, too, considerable technical production capacity is not fully employed. It is therefore very regrettable that the efforts to curb public expenditure and the shortage of funds are clearly eroding public capital outlay instead of, as would be more appropriate from the point of view of short-term economic policy and economic growth, curbing the expansion of expenditure which directly or indirectly increases consumption. Secondly, of course, industrial investment, too, should attain once again a higher rate of growth in the fairly near future.

For all these reasons, there is still a need for efforts to curb the expansion of public expenditure, or reduce the overall deficit of the public authorities, as well as for measures to adapt the pattern of expenditure. Without such efforts the tendencies towards stabilization of costs and prices would also be insufficiently effective. Cost and price stabilization, however, is not only desirable for general reasons of economic policy but is also necessary in order to enable the Federal Republic to re-attain a satisfactory position on current account. One should not be deceived by present improvements; they are mainly due to differences in the pull exerted by demand—which has increased in some countries (the United States, Italy, France) and decreased in Germany—and do not yet

reflect any appreciable restoration of competitive power. Stabilization of costs thus remains an urgent requirement. This, too, incidentally, is a factor tending to support industrial rationalization investment.

In this field of monetary and credit policy there is still no reason to relax the measures adopted, which have only recently begun to produce the desired effect on credit expansion : a relaxation would be made use of not so much by industry, to which more cash is now in any case becoming available, owing to the improvement in the balance of current foreign transactions and the cash deficits of the public authorities, as by the public sector, which would take advantage of it to increase its spending more than would otherwise be possible : were it only because of the relatively close interrelationship in the Federal Republic between bank liquidity and the state of the capital market, any easing of credit policy would immediately lead to a renewed rise in public borrowing.

Admittedly, this state of affairs could change if the draft stabilization law now under discussion were quickly passed by Parliament and if its clauses concerning the overall control of the expansion of the public authorities' expenditure, and in particular those concerning the limitation of their recourse to the credit and capital markets in the light of considerations of economic policy (thus not only in relation to the degree of scarcity of such funds), were implemented as early as in 1967. Unfortunately, apart from the possibility of withdrawing additional tax depreciation concessions granted for new investment, there is no clause in the bill enabling excess demand to be contained through tax increases introduced by a simplified procedure.

It is clear that the more efficiently a policy of reducing the public authorities' demand for credit is implemented, the more funds become available for the non-inflationary financing of industrial investment. The business community would certainly not neglect this opportunity.

Managements who have got the right feel of the market should now abandon an approach to sales based on rising prices and concentrate on expanding the *volume* of sales. Some of the difficulties attendant on crises might beset certain industries if managements were obstinate in passing on in higher prices all present or even past cost increases; in that event falls in sales would be inevitable. On the other hand, stable prices or even price reductions could lead to real expansions in sales, which would definitely bring in better profits. At the same time the trade unions, too, must adjust themselves to the new economic situation; this can still lead to genuinely satisfactory increases in real wages, provided that the transition to a "quantity boom" is not rendered impossible by excessively large rises in monetary wage costs.

### **3. The economic situation in West Berlin**

In the second quarter economic growth in West Berlin slowed down once again. Whereas in 1965 the real gross product still rose considerably faster than in the Federal

area, there was an appreciably more marked slackening in its rate of growth this year; in the second quarter it was approximately the same as that for the Federal area.

There was a marked acceleration in the rise in exports; their year-to-year rate of growth (value) rose from 7.5 % in the first quarter to nearly 16 % in the second. On the other hand, deliveries to the Federal area increased only slowly, being barely 5 % higher than a year earlier, compared with a 9 % year-to-year improvement for the first quarter.

The total of gross fixed asset formation in the second quarter was still considerably higher than in the corresponding period of last year. This was primarily attributable to a vigorous expansion in investment in building, hamstrung in the first quarter by bad weather. Capital expenditure in industry, on the other hand, seems to have settled again at a high level after its sharp upsurge last year.

The tendencies for the expansion of private consumers' expenditure to slow down—discerned some time ago—persisted. Retail sales in the second quarter were 4 % higher than in the corresponding period last year.

In the labour market, for the first time for quite a long period, there were fewer vacancies than there had been a year earlier. Nevertheless, there has been no easing of strain. The number of unemployed remained considerably lower than that of vacancies and reached a new low at the end of July.

There was a further slackening in the rate of growth of industrial production. With a year-to-year increase of over 4 %, however, it was still somewhat faster than in the Federal area. The output of the electrical engineering industry, in particular, rose very sharply. There was a decline in production, on the other hand, in the mechanical engineering industry. The growth of production of consumer goods would appear to have gathered a little momentum again in the second quarter.

The deficit in the merchandise trade balance with the Federal area, at DM 176 million, was somewhat smaller in the second quarter than in the corresponding period of last year.

The rise in prices has slackened slightly in recent months. Even so, the cost of living index for July/August was still 4 % above its level a year earlier.

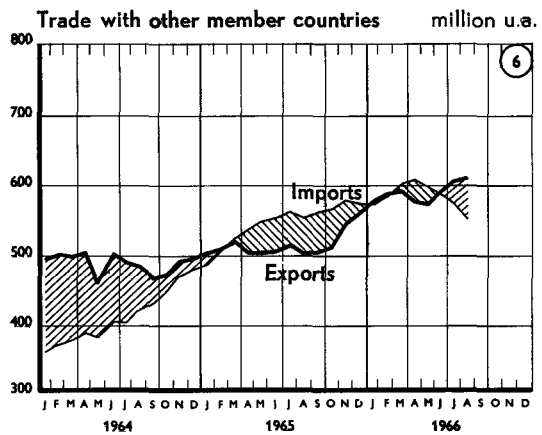
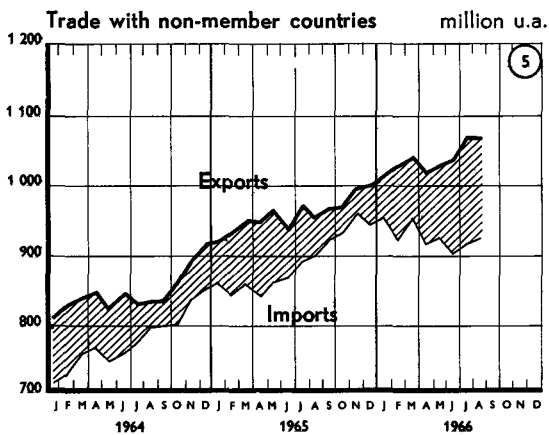
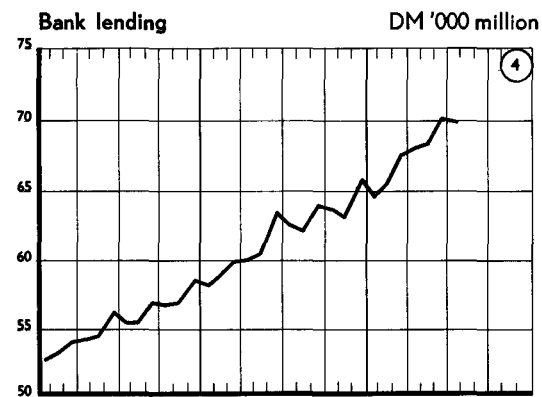
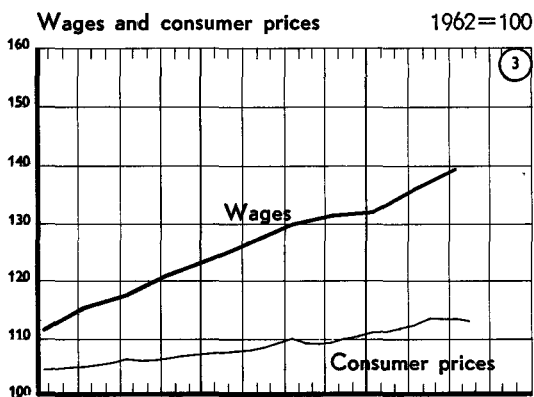
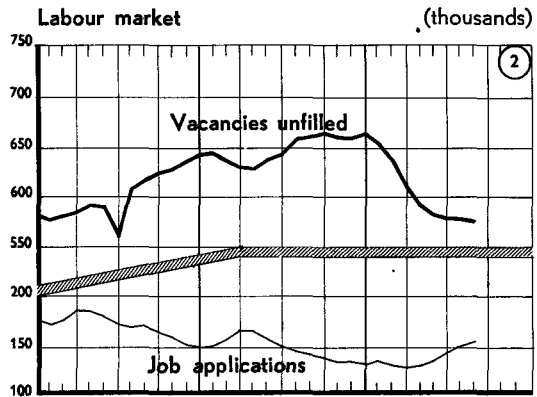
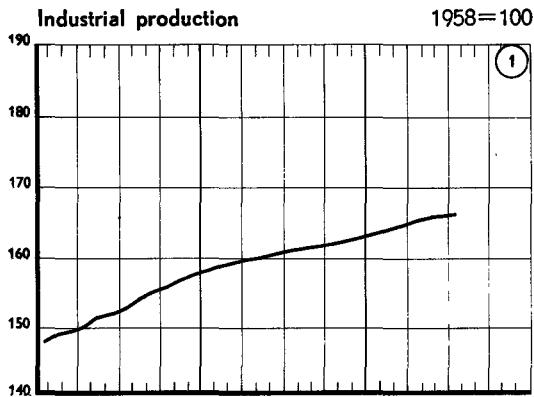
The economic outlook for the coming months points to continued, but slower, economic growth. The state of industrial order books has been deteriorating for some time. The total of new orders booked in the second quarter was 7.3 % lower than a year earlier, mainly owing to a pronounced dip in orders received by the mechanical engineering



industry. It should, however, be borne in mind in assessing the figures for orders that in the second quarter of 1965 there was a concentration of public orders, whereas this year, owing to financing difficulties, the volume of orders placed by public authorities was smaller.



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)	7 601

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 1964 GNP
	1960	1961	1962	1963	1964	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	3.2	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	64.4
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	6.3	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	203	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	11 338	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	16.8	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	168	168	153	144					
Total orders received (1958 = 100)	1964	160	164	171	185	165	178	177	154	181	192	185	179	
	1965	166	173	193	190	188	182	180	165	197	200	196	188	
	1966	173	178	216	193	193	188	176	169					
of which:														
	home orders	1964	153	158	168	182	163	174	177	154	179	190	181	172
	1965	161	167	193	188	185	178	176	164	196	198	192	177	
1966	163	170	208	186	185	178	169	161						
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	214	233	
1966	211	213	250	227	230	234	207	211						
Building: number of permits issued (DM '000 million)	1964	2.49	2.58	2.39	3.34	3.32	3.62	3.32	3.87	3.72	4.01	3.55	3.51	
	1965	2.68	2.61	3.25	3.61	4.04	3.85	4.45	4.39	4.27	4.17	3.31	3.77	
	1966	2.95	2.97	4.00	3.75	3.85	4.03	4.15						
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					
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	1 534	1 606	
	1966	1 446	1 397	1 635	1 476	1 541	1 544	1 478	1 449					
Total visible exports (million u.a.)	1964	1 240	1 289	1 362	1 423	1 231	1 350	1 368	1 172	1 329	1 487	1 390	1 533	
	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					
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					
Official gold and foreign exchange reserves (million u.a.)	1964	7 012	7 206	7 114	6 968	6 921	7 158	7 049	7 024	7 059	7 052	6 944	6 969	
	1965	6 604	6 702	6 800	6 825	6 436	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					
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						

## 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*

- Source : Statistisches Bundesamt. Wirtschaft und Statistik.
- 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

*In the spring and the summer months the French economy experienced vigorous expansion which was increasingly supported by the capital expenditure of the business sector. These trends are probably still a feature of the situation today. Production and employment are rising, and are accompanied by an increase in the incomes of households, which as a result are stepping up their spending on goods and services appreciably.*

*This advance in the level of business activity has so far remained fairly well balanced. Already, however, there are renewed indications of potential threats to the price level which stem from the fact that the expansion of demand is likely, if anything, to become even more rapid in 1967 while supply may become less elastic. Furthermore, whereas up to the present the labour market situation has been characterized by a steady and appreciable expansion of the labour force and largely for this reason has not been subject to general strain, in the coming months wages and wage costs may resume a more marked upward trend as a result of the frequent shortage of properly skilled workers and the geographical lack of mobility in the existing reserves of manpower.*

*Consequently, the most important task before those responsible for short-term economic policy is to counter such dangers in good time and thus ensure the continuance, as long as possible, of growth without strains. One aspect of this task is the need for continued care in the handling of public budgets, which is as important as intensification of the measures designed to improve the country's economic and financial structure.*

### 1. Recent developments

The very vigorous expansionary trend of overall demand continued in the second quarter and doubtless also throughout the summer, with the emphasis shifting somewhat to domestic demand and, within this, to investment.

Exports of goods and services increased further, but in relation to the preceding months the pace was rather slower. Even so, according to the foreign trade statistics, the average value of the goods exported during April-June was about 12 % higher than in the corresponding period of last year, while for July-August the rise was 10 %. The growth in demand from the other EEC countries—mainly from the Federal Republic of Germany—appears to have slackened slightly for the time being. Exports to non-member countries, on the other hand, developed rather more briskly; in particular, sales to the franc area registered a vigorous recovery.

The rate of expansion of domestic demand has remained very high in recent months. The rise in gross fixed asset formation by enterprises has probably become even more vigorous than before. The more rapid improvement in the production and the imports of equipment points to a distinctly greater propensity to invest on the part of private industry in particular, this being probably attributable not only to the various fiscal incentives and the generally improved profits situation, but also increasingly to the fuller utilization of existing capacity and to growing confidence in a continuance of the present upswing. While the capital investment projects of public enterprises were pursued according to plan and the Government's outlay on fixed assets rose, if anything, faster than before, investment in residential building, especially the privately financed sector, advanced very slowly. The total number of dwellings completed in the second quarter was only 2 % greater than in the corresponding period of the previous year; in spite of this, the number of unsold dwellings rose further, so that the number of housing starts was reduced, being 9.5 % lower than in the second quarter of 1965.

Investment in stocks probably again gave a stimulus to overall demand. Not only does the replenishment of stocks of raw materials and semi-manufactures seem to have continued, but stocks of finished goods also appear to have increased further, mainly owing to increased stocks being held by traders in view of the expansion of final demand.

The rise in consumer expenditure continued at a rapid tempo. To judge by the growth in government expenditure under the ordinary budget, the rate at which public current expenditure is increasing may even have quickened appreciably during the last few months. The expansion of overall private consumers' expenditure remained very brisk. True, the increase in sales of motor-cars, measured by the number of new vehicles registered, showed a distinctly slacker trend. The sales of department stores and the large chain stores, too, were only about 5 % higher in the second quarter than they had been a year earlier. It should, however, be borne in mind that car sales had previously risen extraordinarily sharply, and that this expansion could hardly continue without interruption. Furthermore, demand for other durable consumer goods, which had previously been at a relatively low level, appears to have become brisker. Lastly, it seems likely that an increasing proportion of the spending of households was accounted for by forms of selling other than retail trade (the only kind covered by the statistics) or by services.

The continuing expansion in private consumers' expenditure was probably due solely to the renewed rise in incomes; the proportion of the available income of households that went into savings seems to have remained more or less constant. There was even a slight acceleration in the upward movement of wage and salary incomes. While the rise in the index of hourly wage rates for private trade and industry between 1 April and 1 July was, at 1.45 %, not quite so large as that recorded for the preceding three-month period, when it was 1.65 %, the level of employment rose more rapidly than hitherto. There has been a very substantial increase, especially in industry, in the number of persons employed during the last few months, there having been very little margin left for a further extension of actual working hours. Altogether, wage and salary incomes in the second quarter will probably be found to have been over 8.5 % greater than a year earlier.



The other incomes of private households, and especially the incomes of self-employed persons, may also have increased considerably.

The expansion in overall demand was still met without any great difficulty, thanks to a corresponding rise in supply.

Agricultural production was on the whole adequate. Admittedly, crops appear to have fallen short of the extraordinarily good harvests of the previous year, partly owing to a reduction of the areas cultivated (wheat, sugar beet) and partly owing to bad weather (wine, fruit). Output of livestock products, however, rose very substantially compared with 1965.

The expansion of industrial production continued at the previous rapid rate. According to the seasonally adjusted INSEE Index (excluding construction), it increased from the first to the second quarter by about 2 %; in comparison with the second quarter of 1965 it showed a year-to-year growth rate of 8 %. There was, however, a shift in the factors responsible for this upswing, as a result of differences in the pace at which the various components of demand were developing and in part, also, of differences in the reserve capacity available in the various industries. There was a certain slackening of growth in the output of certain major consumer goods industries (motors and textiles), but a distinct acceleration in many basic materials industries and, above all, in nearly all branches of the capital goods industry.

The rise in building output, on the other hand, was again only hesitant, since the slackening of activity in the housing sector was not quite compensated by the increased demand for public works and for commercial and industrial building. According to the INSEE Index, total building activity in the second quarter was only 3 % greater than in the corresponding period of last year.

The rise in production led, more than hitherto, to further recruitment of labour. In the main, however, the additional demands were met, especially in the industrial sector, without increased strain on the labour market, at least when the situation is taken as a whole. The main factor contributing to this was the recent very substantial increase in the labour force. True, the number of vacancies notified showed a further upward trend during the second quarter and beyond; but the number of persons seeking employment also rose slightly further during the period.

The very vigorous growth in imports of goods and services showed hardly any signs of slackening. The volume of merchandise imports, as calculated on the basis of the customs returns, was about 12.5 % greater in the second quarter and about 11 % greater in July-August than in the corresponding periods of last year. While imports of foodstuffs showed a downward trend, imports of raw materials and semi-manufactures went on expanding vigorously, and foreign consumer and capital goods, apart from motor-cars, also continued to sell at a rapidly quickening tempo on the domestic market.

The trend of prices, at least up to the middle of the year, remained relatively moderate. According to the INSEE Index, which covers 259 articles, the cost of living

again rose between March and July by only about the same percentage as in the preceding four months and also no faster than in the corresponding period of last year, namely by barely 1 %, leaving out of account the repercussions during those periods of delays in the renewal of contracts between the social health insurance service and the doctors. The rise in the cost of living <sup>(1)</sup> in comparison with July 1965 was 2.6 %. Nevertheless the impression remains that the underlying upward trend of prices of finished industrial goods, especially clothes and household items, was rather more marked in recent months and that the prices of private services rose at least as rapidly as before, while foodstuffs prices went up at a lower rate.

The tendency for the deficit on visible trade to increase has become somewhat more pronounced since the spring; according to customs returns, it amounted in April-August to FF 1 311 million (as against only FF 490 million in the corresponding period of 1965). As this deterioration was mainly observable in trade with countries outside the franc area, it was probably also reflected in the current account of the balance of payments. It is likely, on the other hand, that the balance on capital account will have closed, in contrast to the corresponding period of last year, with a substantial surplus, not only because there was no advance repayment of debts this year, but also as a result of capital inflows during the period of renewed weakness of the pound sterling. The gross foreign exchange reserves of the monetary authorities increased from the end of March to the end of August by FF 1 933 million; in contrast to this rise, net claims on the International Monetary Fund <sup>(2)</sup> and the net foreign exchange position of the commercial banks underwent little change during this period, whereas a year earlier it was precisely these two items which showed a very substantial improvement, while the gross official foreign exchange reserves rose by only FF 150 million.

The net inflow of foreign currency made a somewhat larger contribution to domestic liquidity than hitherto. It was, however, lending by the banking system to business and private borrowers which contributed most to greater liquidity: the amount of credit outstanding at the end of June was 13.9 % greater than a year earlier, while short-term credits alone showed a year-to-year expansion of almost 15.8 %. The financial transactions of the public authorities also made a distinct contribution to expansion in the second quarter, whereas in the previous quarter they had (if the effect of certain transactions in *Caisse des Dépôts et Consignations* paper carried out between the Treasury and the Central Bank is included) still tended to reduce liquidity. Cash outlays by the Treasury, partly on account of credits carried forward from previous years and partly as a result of considerable advances to the social insurance system, rose at a much higher rate than before, while receipts went up much more slowly, so that the financial deficit to be covered by the Treasury, which had been only FF 2 600 million in the period April-July 1965, must this year have risen by more than half. In addition, the transactions with *Caisse des Dépôts et Consignations* paper, which could have helped once again to restrict the rise in liquidity, were on a very limited scale.

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<sup>(1)</sup> Excluding the item "medical services".

<sup>(2)</sup> Apart from the payment to the Fund, equivalent to FF 244 million, made in August in respect of the quota increase. ~~1965~~

The money market was under considerable strain nearly all the time; although the minimum reserve ratio was very flexibly applied on the end-of-month settlement dates, the banks were obliged to borrow considerable sums from the Banque de France. Rates for day-to-day money showed an upward trend; the discount rate (3.5 %) was exceeded at times by more than 1.35 %.

On the capital market, where funds had not been particularly abundant in the first quarter, a substantial volume of issues were again floated in the subsequent months; these totalled FF 4 650 million, compared with FF 3 960 million in the second quarter of 1965. On this market, too, interest rates showed a further rise, and this forced the authorities to improve the rates offered on new loans in the public sector.

## 2. Outlook

The forecast for future developments indicates that in the short term, i.e. up to the end of 1966, there will certainly be a continuance of the vigorous expansion in demand, while the growth in supply will lose little of its elasticity.

Conditions abroad are likely to go on providing very strong stimuli to production and employment. While exports to the rest of the EEC area may possibly expand at a slower rate for a while—at least until there is a sustained recovery in imports by the Federal Republic of Germany—sales prospects are likely to improve in non-member countries, especially the United States and the franc area.

Domestic demand will also increase further, and possibly even at a slightly quicker rate.

While the programmes of public undertakings and the central Government in any case provide for steadily increasing expenditure on building, plant and machinery up to the end of the year, there are many indications that the propensity to invest of the private sector is still expanding steadily. At all events, an INSEE survey carried out in June shows that private industry has substantially stepped up its investment plans for 1966 since the spring; it proposes to invest 6 % more (in money terms) than in 1965, whereas only in March the proposed increase was still 4 %. There will therefore undoubtedly be a further vigorous expansion in total expenditure on gross fixed asset formation, even if expenditure on housing again proves to be sluggish—as can well be expected in the light of the poor trend in the number of building permits being issued and the relatively small number of starts registered.

Furthermore, the conditions for a persistent—and perhaps even somewhat more rapid—rise in private consumers' expenditure appear to be present. Employment will undoubtedly increase more steeply than hitherto, not only because existing production capacities are being more fully used, but even more because an increasing number of new installations is now reaching the stage where production can start. The trend of wages may reflect rather more markedly the increased demand for additional labour. Fur-

thermore, certain social benefits (especially family allowances) were increased in the summer or early autumn. Lastly, in view of the higher level of activity in trade and industry and the trend in the prices paid to agricultural producers, there is also likely to be an appreciable increase in the incomes of the self-employed.

With overall demand showing so high a degree of buoyancy, there is sure to be a further vigorous growth in domestic production. Certain physical limitations may, however, come more to the fore than hitherto, if not yet generally, at least in certain sectors of the manufacturing industry, for in the last few months there has been a sharp rise in utilization of technical capacity in industry. In the middle of the year one-third (in March it was only one-quarter) of the businessmen regularly questioned by the INSEE stated that bottlenecks (primarily in technical equipment and not so much in the supply of labour) were preventing them from further stepping up their output. Another quarter reported that a further increase in output would at least be difficult to achieve.

In these circumstances a steady increase in imports, especially of manufactures, can be predicted. The tendency towards a deterioration of the current account in the balance of payments might become somewhat more pronounced in the last months of 1966.

There is furthermore some possibility of a rather more marked rise in prices, after adjustment for certain seasonal and fortuitous fluctuations which may occur in the prices of a few crop foods and other items. Not only were there a number of "autonomous" increases in charges for public services on 1 August (gas, electricity, telephone and certain other postal charges), but there are also signs of a slight accentuation of the upward trend of prices for finished industrial goods; the higher prices are in part the result of rising costs due to the above-mentioned increases in charges, to the simultaneous raising of the social insurance contributions paid by employers and to the tendency now emerging for the gap between the rise in wages and the rise in productivity to widen again, and in part they stem from the demand situation, which is making it possible to widen profit margins beyond what is required for passing on cost increases, at least where this is not prevented by official price policy. Lastly, the alignments of producer prices involved in the establishment of the common agricultural market might lead to a slight rise in the prices of certain foodstuffs at consumer level although, in view of the present margin between producer and consumer price levels, this is not absolutely necessary.

Analysis of the economic developments that have occurred so far this year and of the outlook for the remaining months leads to conclusions which tally substantially with the quantitative forecasts for the full year 1966 published in Quarterly Survey No. 2/1966. In particular, the estimates for the growth of real gross national product (about 5.5 %) and of the main components of its utilization are still valid.

The outlook for 1967, too, is one of continued expansion of demand at a brisk, perhaps even somewhat accelerated, pace; at the same time, however, there might be a more pronounced diminution in the elasticity of domestic supply, so that there is a possibility that certain difficulties may come to the fore again.

*National product and expenditure*

	1963 <sup>(2)</sup>	1964 <sup>(2)</sup>		1965 <sup>(2)</sup>		1966 <sup>(3)</sup>	
	At current prices (in FF '000 million)	% change on preceding year					
		Volume	Value	Volume	Value	Volume	Value
Gross national product	396.0	+ 5.9	+ 9.9	+ 3.4	+ 6.0	+ 5.5	+ 8.5
Imports <sup>(1)</sup>	54.9	+ 12.4	+ 14.9	+ 3.6	+ 4.0	+ 11.5	+ 12.5
Private consumer's expenditure	256.9	+ 4.7	+ 8.3	+ 3.2	+ 5.9	+ 5	+ 8
Public current expenditure	53.4	+ 4.8	+ 9.9	+ 2.3	+ 4.8	+ 4	+ 7.5
Gross fixed asset formation	79.6	+ 11.8	+ 15.9	+ 5.3	+ 8.4	+ 6	+ 8.5
Exports <sup>(1)</sup>	56.6	+ 7.7	+ 10.8	+ 10.9	+ 11.6	+ 9	+ 10.5

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> Rapport sur les comptes de la nation de l'année 1965, Ministère de l'Economie et des Finances, Paris.

<sup>(3)</sup> Commission forecasts.

*Note :*

a) The difference between the figures for product and those for expenditure 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 member countries, but they are established and published on the sole responsibility of the Commission.

Additional impetus is likely to be provided not so much by demand from abroad, even though world economic conditions should on the whole remain favourable, but primarily by the expenditure of business firms and the public authorities. The latest information available confirms and gives greater precision to the observations to this effect made in Quarterly Survey No. 2/1966. On the basis of an INSEE business survey, for example, it can now be assumed that in 1967 private industry will increase its gross fixed asset formation by 7 to 9 % more than in the current year, when the rise will have been about 6 % over 1965; and the Government's budget for 1967 provides for increases in ordinary and extraordinary expenditure which, again, are considerably above those approved for 1966. All in all, it appears certain that there will be a faster rise in employment and in incomes and thus also an expansion of private consumers' expenditure which, even if a further increase should occur in the propensity to save, is likely to be greater than in 1966, especially as certain tax reliefs have been decided on for persons with low incomes and certain other categories.

Domestic production will probably not be able to keep pace as well as hitherto with such an expansion of overall demand. Nevertheless, the Commission considers it quite

possible that 1967 will again show a growth of about 5.5 % in real gross national product. Imports are likely to maintain their steep upward trend.

Heavier calls on the factors contributing to production, on the lines indicated in this forecast, would probably not be compatible with the further stabilization that is being sought. Short-term policy must therefore be aimed at keeping the expansion of demand strictly under control; at the same time, all measures designed to remedy the structural lack of elasticity of certain markets should be intensified.

With regard to the first of these two tasks, special importance naturally attaches to the public authorities and their budget policy. According to the Government's draft for the 1967 budget, as compared with the corresponding proposals for 1966 <sup>(1)</sup>, the assured government outlays are to rise a great deal more rapidly than before—by 11.6 %, against a mere 7 % in the budget for 1966. This would mean an increase in government expenditure not only substantially in excess of the growth in real gross national product, but also in excess of the expected rise in money terms (about 8.5 %)—in a year in which boom conditions will in all likelihood prevail in any case.

It should, however, be emphasized that the structure of the expenditure planned for 1967 is guided by the requirements of short-term economic policy (and even more, it must be said, the aims of the Fifth Plan), since planned expenditure on investment in the civilian sector (especially on scientific research) shows an increase of about 25 % over 1966, against corresponding figures of 10.4 % for current administrative expenditure and 6.8 % for military outlays. A second point is that over against these assured items of expenditure there are assured revenue items which, partly as a result of the general upswing, are expected, despite reductions in certain taxes, to rise appreciably faster than before (the rise is estimated at 10.4 % in the budget proposals for 1967, against 6.6 % in the estimates for 1966).

However, the surplus on the ordinary budget will be lower than for 1966 (about FF 3 000 million, compared with FF 3 800 million). A financing deficit on the overall budget (which includes extraordinary capital expenditure and grants), was eventually avoided only by a further "debudgetization" (removal of social housing grants from the budget accounts), by pegging at approximately their present level the capital investment loans made to public undertakings, which are being told to resort to increases in their charges, and by the Government's refusal to give further subsidies to the social insurance system, for which a change in health insurance benefits and contributions is envisaged. Furthermore, certain expenditures which are already planned were not included in the budget estimates, as they are in due course to be financed from the proceeds of a special loan.

In executing this budget the authorities responsible have of course a means of controlling and adjusting the demand stimulus given by the public purse to production,

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(1) As the lay-out of the 1967 budget is again different from that used for the previous year, the data given in the following paragraphs have been calculated on an approximately comparable basis in order to avoid as far as possible the misinterpretations which might result from a rigid comparison of the individual budget items for 1966 and 1967.

employment and incomes. In this connection the authorities should ensure that the budget appropriations are not exceeded in the way they have been exceeded so far this year. The additional revenue which will probably accrue—especially if prices rise more than expected—could then be used to meet other Treasury financing needs or to reduce indebtedness to the banking system.

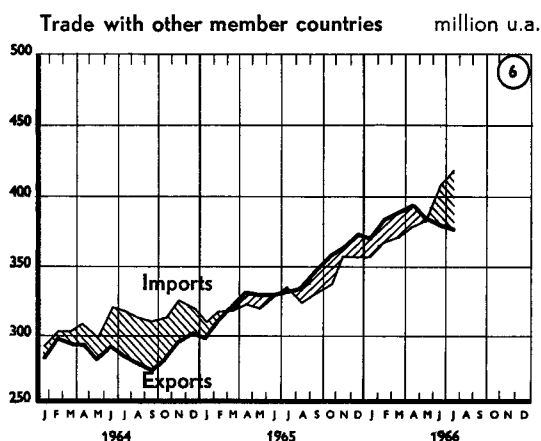
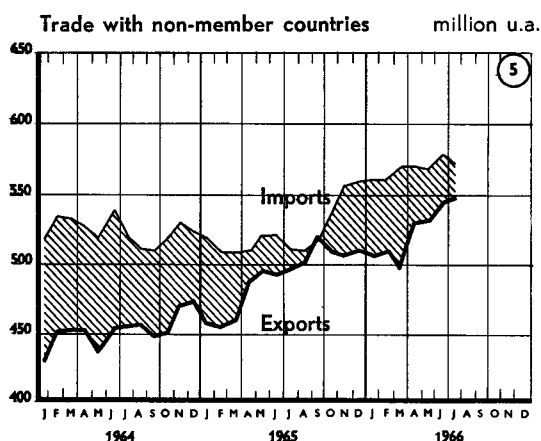
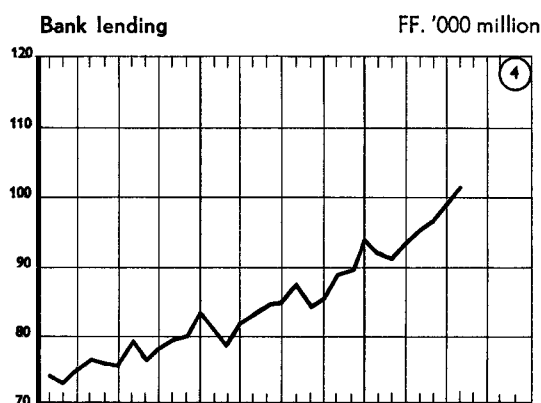
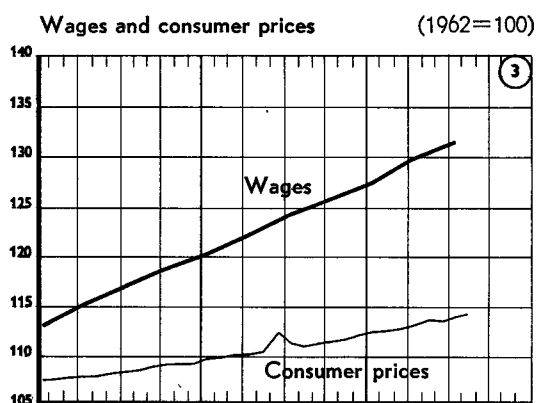
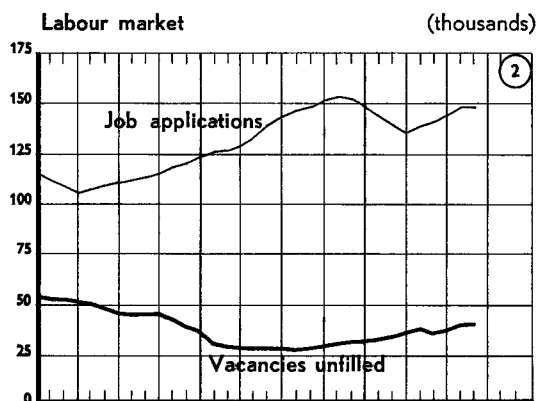
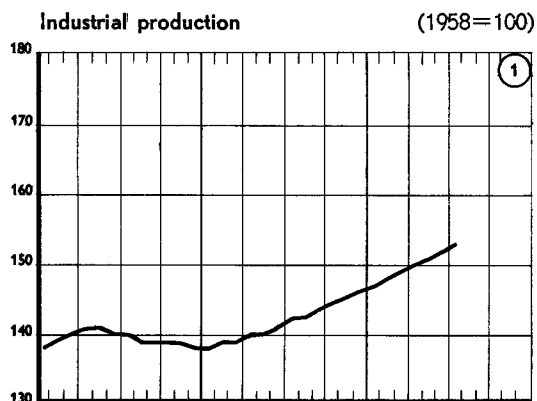
This would support the monetary authorities' efforts to prevent too great an increase in the liquidity of the economy with the least possible reduction in the volume of loans granted to enterprises for financing increased productive capital investment. But if budget policy has a very expansive effect, the monetary authorities will undoubtedly soon have to take preliminary steps to curb the expansion of credit once more.

The elasticity of the markets is already benefiting in industry from integration and amalgamation; this process should be further encouraged by the government authorities not only because it can increase the ability to compete with large-scale concerns abroad, but also because of the effect it can have in increasing supply and reducing costs for buyers at home. On the other hand, the progress being made in the equally necessary task of modernizing and rationalizing the machinery of distribution is in no way comparable. Much remains to be done in this field, particularly in shortening the distribution channels of agricultural products. Finally, special urgency attaches to the efforts to eliminate the acute difficulties or even bottlenecks which occur on the labour markets owing to the inadequate training and geographical immobility of the available manpower. An important and welcome step in this direction was the approval by the Government in mid-August of an "Outline Law on Vocational Training", which is designed to improve the training possibilities for youths between 15 and 21 years of age; this law provides for the setting up of a "National Council for Vocational Training and Social Advancement" and for the creation of a fund which will draw most of its resources from the proceeds of the increased "Apprentices Tax" on enterprises.





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 Crédit. 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 1964 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			
<b>Visible exports</b>										
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	+18.3	+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
<b>Exports of food, beverages and tobacco</b>										
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
<b>Exports of raw materials and manufactures</b>										
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
<b>Visible imports</b>										
Total	- 9.2	+23.3	+ 6.3	+12.3	+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
<b>Imports of food, beverages and tobacco</b>										
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	+ 3.9	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
<b>Imports of raw materials and manufactures</b>										
Total	- 7.1	+28.7	+ 8.5	+10.9	+13.8	+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	144	146	146	148	129	91	142	151	156	158
	1966	150	156	158	158	158	161						
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	(48.7)	(43.9)					
Private consumers' expenditure : turnover of department stores (1958 = 100)	1964	189	178	197	199	209	203	206	183	225	249	213	330
	1965	211	181	204	228	219	223	232	199	258	244	236	352
	1966	216	193										
Total visible imports (million u.a.)	1964	861	846	883	930	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	1 093	994	1 002	1 063	929	780				
Total visible exports (million u.a.)	1964	731	751	763	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	873	1 023	947	916	960	952	729				
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	- 62	- 75	- 47	- 86	- 103	+ 23	- 51				
Official gold and foreign exchange reserves (gross, million u.a.)	1964	4 481	4 494	4 477	4 533	4 680	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			
Money supply (FF '000 million)	1964	147.7	146.6	148.6	148.6	149.0	152.1	156.3	154.8	155.2	155.8	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	175.7	177.3	177.7	182.1	186.4					

## 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 the second quarter of 1966 demand from abroad accounted for an increased part of the continued rapid expansion of overall demand; the acceleration in the growth rate of exports has in fact been notable. While private consumers' expenditure went on rising as fast as ever, the increase in outlay on gross fixed asset formation, which has shown an upward trend since the middle of last year, may temporarily have slackened somewhat. This loss of momentum is, however, probably attributable solely to the effect of special factors, namely delivery difficulties due to strikes in the industries producing plant and machinery; it was also probably limited in extent, mainly because there has apparently been some revival of investment in building.*

*Production increased faster than before. Prices for the most part remained stable, as is usually the case during the phase of rising activity at present being experienced in Italy.*

*As for the future, overall demand and production can be expected to go on rising rapidly, while prices should for the time being remain relatively stable. In the rather longer run, however, the possibility of a threat to the hard-won price stability cannot be ruled out, if the pace of expansion becomes so fast as to create the conditions for a further appreciable rise in wage costs per unit produced.*

*The main aim of short-term economic policy in the next few months and in 1967 should be to obviate such a development. This would mean pursuing a budget policy designed to bring about a gradual reduction in the deficits of the public authorities and in the extent to which these deficits are financed by short-term borrowing, while at the same time maintaining the policy of support for investment—in other words, it would be necessary to curb progressively the very rapid expansion of outlays which contribute, directly or indirectly, to consumption.*

### 1. Recent developments

In the second quarter and apparently also in the summer months, the expansion of overall demand continued at a rather rapid rate; the rise in demand from abroad would even appear to have quickened.

Exports of goods and services increased appreciably faster, after a period of slower expansion. The value of merchandise exports (as defined for customs statistics) was 13.8 % higher in the second quarter than it had been a year earlier. There was a particularly marked expansion in exports of machinery, of other equipment and of means of transport. Exports to the other countries of the Community showed a larger rise than those to non-member countries. The statistics of the Foreign Exchange Office show

that earnings from exports of services, in which an important part was played by the expenditure of foreign tourists in Italy, continued to increase rapidly.

Domestic demand in money terms, on the other hand, may have risen somewhat less quickly than in the first quarter. There are in fact many indications, with regard to expenditure on gross fixed asset formation, that actual outlay on plant and machinery was rather hesitant in the second quarter. However, the production statistics, on which this impression is partly based, doubtless give too unfavourable a picture of the economic situation, since it was just in the iron and steel industry and in metal processing that strikes led to very heavy production losses. But the underlying trend of investment in plant and machinery is likely to have remained decidedly expansionary. One significant pointer in this direction is provided by the results of the EEC business surveys.

Investment in construction doubtless remained at a relatively low level, but there are increasingly numerous signs that some recovery is under way in this field. For example, there has been a further marked rise in public works : their value in April-May (no more recent data are yet available) was 17.5 % higher than a year earlier, as against 11 % in the first quarter (source : ISTAT). Doubtless in part related to this, there was in the second quarter a very sharp increase in cement production the seasonally adjusted level of which was, according to ISCO, 12 % above the admittedly very low level of the first quarter. Furthermore, it would appear that demand for building loans, both at reduced interest rates and on normal terms, rose considerably. Lastly, it is evident that the trend of employment in the building sector rose again from the first to the second quarter : the compensatory payments from the wage equalization fund to workers on short time in the construction industry declined more than is seasonally normal for the quarter and for July; in addition, ISTAT's quarterly sample surveys showed that the number of building workers in employment in July was 54 000 higher than in April (against a decline of 12 000 over the same period last year).

The growth of investment in stocks probably slowed down in the second quarter. At any rate, the build-up of stocks of raw materials and semi-finished goods appears to have slackened, while the stocks of finished goods held by industry showed a further downward trend.

There was undoubtedly a further large rise in consumption expenditure. The current expenditure of the Government appears to have risen particularly fast : at all events, there was a substantial rise in the wage and salary payments made by the Treasury in the second quarter. The trend of output and foreign trade in the consumer goods sector indicates that private consumers' expenditure also went up rapidly. According to ISCO, the seasonally adjusted monthly average output of industrial consumer goods in the second quarter was almost 6 % greater than in the first. Domestic purchases of passenger cars, seasonally adjusted, again rose by nearly 12 % between the first quarter and April-May (source : ISCO). To judge by the results of the monthly EEC business surveys, there was also a distinct increase in demand from households for textiles and clothing.

The main factor behind this development of private consumers' expenditure appears to have been a correspondingly vigorous expansion of incomes. There was probably a further appreciable rise in non-wage incomes, and total wages and salaries also doubtless increased appreciably. There would appear to have been an appreciable increase in the total number of hours worked. The number of hours worked per head has again risen by comparison with the preceding months, and there was also a rise, although relatively small, in the number of persons in paid employment. There was, it is true, a smaller increase in minimum contractual wages and salaries (including family allowances and the increases due to operation of the sliding wage scale, which came into play again on 1 May); the rise from the first to the second quarter was only about 0.5 %. However, as has been happening for the last two years or so, actual hourly wages and salaries have probably gone up more than the contractual rates.

The ISTAT sample surveys show that the number of wage and salary earners rose from April to July by 178 000 or 1.5 %, as against an increase of only 33 000 or 3.0 % a year earlier. Attention should also be drawn to a slight downward trend in the number of persons employed in the services sector; in view of the special conditions in Italy, this might possibly point to a relatively marked upward trend in employment in the more productive sectors.

There was a further large fall in the number of workers on short time, which in July reached its lowest level since 1963; in that month, at 246 000, it was more than 40 % lower than a year earlier (source : ISTAT). The fact that the number of working hours lost for which assistance payments were made from the wage equalization funds showed a more than seasonal decline from the first to the second quarter also points to an increase in the average working hours per person in paid employment.

After a temporarily more than seasonal increase in the winter due to special factors, the number of unemployed slowly declined in the subsequent months. In April, when it stood at 665 000 (3.4 % of the labour force) it was a full 1 % lower than a year earlier (source : ISTAT). There appears to have been a further moderate decline in the number of unemployed in the summer months.

The outstanding feature on the supply side was a continuation and acceleration of the seasonally adjusted rise in industrial production in the second quarter, even though more working hours were lost through strikes during that period than in the first quarter. Seasonally adjusted ISCO figures based on the ISTAT index put the increase from the first to the second quarter at over 4 %. The level of the unadjusted index for the second quarter was no less than 11 % above the corresponding level a year earlier.

The fastest rises in production during this period were in transport equipment and cement. In the metal-processing industry, on the other hand, the seasonally adjusted level of output during the period was low, owing no doubt to the fact that this branch of industry was particularly hard hit by the strikes.

While output in the building sector appears to have recovered somewhat, there seems to have been an appreciable further rise in production in the services sector. There was also a continuation of the slow growth in agricultural production.

Imports of goods and services, too, increased further in the second quarter, although the growth of visible imports at least would seem to have been slowed by special factors. Customs returns show that the value of these imports, however, was again well above their value of a year earlier, with a rise of 17.3 % (the rise in volume was about the same). Thus, with a time-lag of about one year on the corresponding development in industrial production, imports rose again for the first time above the peak they had reached before the economic recession began in 1964.

This slackening in the upward trend of merchandise imports was mainly attributable to some levelling off in the imports of fuels, semi-manufactures, plant, machinery and foodstuffs. It affected mainly, perhaps even exclusively, goods from non-member countries. Imports of services, on the other hand, appear to have experienced a further rapid rise.

Prices remained for the most part stable in the second quarter. Indeed, the index of wholesale prices declined somewhat from May onwards, and were 0.7 % lower in July than in March. Wholesale prices for capital goods moved further upwards until May; but during the next two months they marked time. Wholesale prices for auxiliary materials and for consumer goods weakened slightly in the second quarter. In consumer prices, too, there was little movement, although owing to the continued rise in the prices of services these did not yet come completely to a standstill. In July the levels of both the wholesale price index and the retail price index were 1.9 % above the level for the corresponding month of 1965.

The tendency towards a deterioration in the trade balance seems to have given way in the second quarter, though probably only temporarily, to a movement in the opposite direction. The deficit on trade (defined as for customs statistics) was only Lit. 37 000 million during this period. Since at the same time the net receipts from services (especially tourist earnings and remittances from Italians temporarily working abroad) again increased substantially, and since there was a smaller deficit on capital movements than in the early months of the year, the balance of payments surplus rose considerably from the first to the second quarter, reaching Lit. 125 000 million. As a consequence there was now an increase in the net official gold and foreign exchange reserves which was practically equal to this surplus, since hardly any short-term funds were exported by the banks. The net reserves of the monetary authorities again increased considerably in July (by Lit. 147 000 million), and there was probably a further appreciable, though somewhat smaller, rise in the following month.

Thus, in contrast to the first months of the year, developments in the balance of payments tended once again to increase the liquidity of the banks. An influence in the opposite direction was exerted by the continuing rise in the value of notes in circulation and, though only on a relatively small scale, by the cash transactions of the Treasury.



As the slight growth in bank lending tended if anything to slacken somewhat in May (though it picked up again in June), the banks again used a large part of the net addition to their funds for the purchase of securities. The final result was a further decline in bank liquidity, both in absolute terms and in relation to customers' deposits, which went on rising rapidly.

Largely owing to the purchases of securities by the banks, the security market remained on the whole in a position to absorb fresh paper in the second quarter, although no longer to quite the same extent as in the two preceding quarters. The main operations on the bond market consisted in the disposal of substantial amounts of government paper and securities issued by government-controlled undertakings. There was an interruption, probably temporary, in the slight upward trend of the net interest rates. Share prices dropped further in April and May, but subsequently recovered somewhat.

## 2. Outlook

The prospects for the economy up to the end of the year remain clearly expansionary. It looks, however, as if the contribution which demand from abroad makes to the expansion of overall demand will be rather more significant than was assumed a few months ago, while in domestic demand hampering factors may continue for a while to prevent the rise in investment from getting into full swing.

Demand from abroad is in fact likely to go on increasing rapidly, especially as the world economic outlook has, if anything, become more expansionary still. As the upturn in investment expenditure may at first proceed at a fairly moderate pace, supply should also be sufficient to allow for a concomitant and vigorous rise in exports. Prises in Italy, unlike those in most other countries, have for the most part been stabilized, and delivery periods are still relatively short; these two factors promise brisk export activity in the coming months. Italy's competitive position in world markets should also be strengthened by the improved export credit terms which can be expected in the near future. The results both of the EEC business surveys and of the recent "Forum" survey carried out by "Mondo Economico" support the assumption that exports will remain buoyant.

The forecasts also point to a further rise in domestic demand. With regard to gross fixed asset formation, however, there is some uncertainty about investment in building. Nevertheless, there are many indications that the forces of expansion will gradually gain ground in this sector: the availability of ample funds; the impetus likely to be given both by the measures adopted last autumn to encourage housebuilding and the proposal that the rent freeze shall be gradually discontinued from 1 January 1967; the stimulating effect which the probable further acceleration of expenditure on plant and machinery should have on the propensity to build in the commercial and industrial sector; and the prospects of an expansion in public works. At all events, plans both for housing and for commercial and industrial building showed a further upward trend in the first five months of 1966, the year-to-year rates of increase over the corresponding figures for last year having been 24 % and 49 % respectively.

Investment in plant and machinery should rise more quickly again in the second half of 1966 after the disappearance of the fortuitous factors by which it was hampered in the first half of the year. Factors pointing to a distinct upward trend of such expenditure are the continuing need to rationalize and the fact that the profit situation has recently been improving, while the supply of credit has been ample. In any case, the flow of domestic orders received by the industries producing capital goods would appear to have further increased.

Consumption expenditure again appears likely to expand vigorously. This applies both to public consumption—at any rate the budget estimates for 1966 provide for a substantial increase in current expenditure—and even more to private consumers' expenditure. The latter can in fact be expected to receive a further strong stimulus from the trend of incomes. Hourly wage rates will probably rise appreciably in the second half of 1966, and their rate of increase may accelerate towards the end of the year, if the wage negotiations which have already been in progress for some time in major sectors of the economy (primarily the metal-processing and foodstuffs industries) have been concluded by then; in addition, there is every indication that the growth in the volume of employment should continue; and lastly, there is likely to be a further distinct rise in non-wage incomes.

In view of these prospects for the trend of demand, production will doubtless go on increasing at a rapid rate in the second half of 1966. In particular, industrial production (excluding building) is likely to make good progress. The tendencies revealed by the results of the monthly EEC business surveys are in any case clearly upward. The prospects for building production also now appear more favourable.

The increase in the total number of hours worked may for a while still be due largely to a rise in the average number of hours worked per person. The possibilities in this direction will, however, probably soon be exhausted, and there should therefore be a further decline, though possibly a slow one, in the number of unemployed.

Imports will doubtless resume their rapid expansion, though not at such a rapid rate as a year earlier. It is nevertheless probable that the underlying tendency for the trade balance to deteriorate will come to the fore again.

In view of this outlook, and provided agricultural production develops normally, prices should for the time being remain quite stable. Nevertheless, despite the great elasticity of supply at present displayed by the economy, an unduly rapid rise in labour costs might, in conjunction with other factors, cause prices to come under some pressure again towards the end of the year.

Less because of these prospects than of developments which took place in the second quarter, partly under the influence of special factors, the quantitative forecasts given in the last Quarterly Survey for the main aggregates for the full year 1966 now require a few slight adjustments. In particular, the estimated year-to-year growth rate of gross fixed asset formation has been somewhat reduced, while that for demand from abroad has

been increased. The forecast for the growth in real gross national product has also been revised slightly upward, to about 5 %.

*National product and expenditure*

	1963 <sup>(2)</sup>	1964 <sup>(2)</sup>		1965 <sup>(2)</sup>		1966 <sup>(3)</sup>	
	At current prices (in Lit. '000 million)	% change on preceding year					
		Volume	Value	Volume	Value	Volume	Value
Gross national product	30 193	+ 2.7	+ 9.7	+ 3.4	+ 7.1	+ 5	+ 7.5
Imports <sup>(1)</sup>	5 438	— 5.1	— 2.7	+ 0.9	+ 2.1	+ 16	+ 18
Private consumers' expenditure	19 281	+ 2.3	+ 8.1	+ 2.1	+ 6.0	+ 5	+ 7
Public current expenditure	4 101	+ 4.0	+ 13.6	+ 3.7	+ 11.6	+ 5	+ 12
Gross fixed asset formation	7 150	— 6.5	+ 0.7	— 8.2	— 6.8	+ 4	+ 5.5
Exports <sup>(1)</sup>	4 753	+ 11.6	+ 15.4	+ 19.9	+ 20.1	+ 13	+ 14

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> ISTAT : I conti nazionali dell'Italia — Nuova Serie — Anni 1951-1965.

<sup>(3)</sup> Commission forecasts.

*Note :*

a) The difference between the figures for product and those for expenditure is accounted for by movements in stocks.

b) The 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.

For developments in the Italian economy beyond the end of the year, that is, in the outlook for 1967, there is no reason substantially to modify the outline given in the last Quarterly Survey. Demand from abroad will probably continue to increase appreciably, although merchandise exports will doubtless be less buoyant than in 1966, and the expansion of domestic demand will continue at a rapid pace, with investment expenditure by enterprises probably playing a larger part. The extent to which investment expenditure will pick up in relation to consumption will, however, depend in no small measure on the economic and financial policy pursued by the authorities. With regard to the trend of production, the Commission still forecasts a growth in real gross national product of 5-6 %.

These prospects, which do not differ—or which show only shades of difference—from those apparent three months ago, and the conclusions to be drawn from them, confirm what was said in the previous Quarterly Survey regarding the requirements of short-term

economic policy. At most, the need to shift the emphasis of the expansion of demand a little away from consumption and towards investment has become even more evident.

From an overall point of view it must still be recommended that the expansionary effect of the deficit on public budgets should be gradually reduced in line with the rise in overall demand, production, employment and incomes. To this end the deficit should be cut down and at the same time the proportion not financed out of genuine savings by the other sectors should be decreased. Otherwise there is a danger that the expansion of domestic demand in money terms will be so rapid that it will contribute to a reappearance of cost and price tensions.

In particular, budget policy should take into account the need to give further encouragement to investment, especially in any form which leads quickly to rises in productivity; this means that the relevant lines of expenditure must be maintained or even expanded, and existing or even further losses of revenue accepted. Conversely, the necessary reduction of the overall stimulus provided by the budgetary deficits will be achieved only if appreciable cuts are made in the expenditures and reliefs which directly or indirectly encourage consumption—particularly as it was just these expenditures which were sharply increased last year and as private consumers' expenditure is in any case expanding briskly.

A reduction of the deficit on public budgets appears desirable from the point of view of capital market policy also, if the calls which enterprises make on the capital market are not to be thwarted by the excessive demands made on that market by the public authorities (in the widest sense). This danger is particularly serious today, when managements are considerably more dependent on the capital market than they were a few years ago.

It would still appear advisable to apply a rather loose credit policy. It is necessary, however, to ensure that the liquidity of the economy does not rise too rapidly and that it can, if necessary, be curbed quickly enough to prevent the emergence of new inflationary tendencies from this quarter.

Lastly, the greatest importance continues to attach to incomes policy. For should the authorities not succeed in preventing the rise in cost incomes from accelerating afresh, not only would the tendency to price stabilization which has just been established with so much effort probably give way to renewed tensions but, in addition, fresh dangers might arise to threaten investment activity and longer-term economic growth.

The Government has in recent months taken or prepared a number of major measures connected with its short-term economic policy. These include a bill for the improvement of export credit and guarantee terms, one important aim of which is to support the export efforts of small and medium-sized firms. Another bill provides for the continuation and broadening of the existing provisions concerning interest subsidies and capital grants for medium-sized and small industrial enterprises. A law has also come into force which will provide assistance for the underdeveloped regions of northern and central Italy.

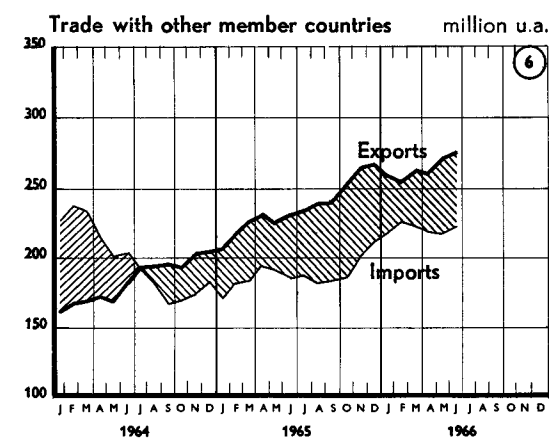
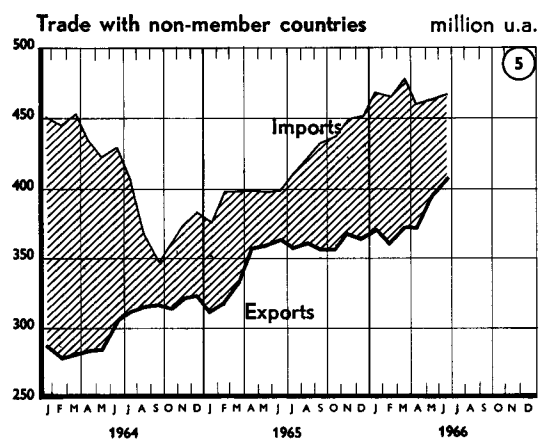
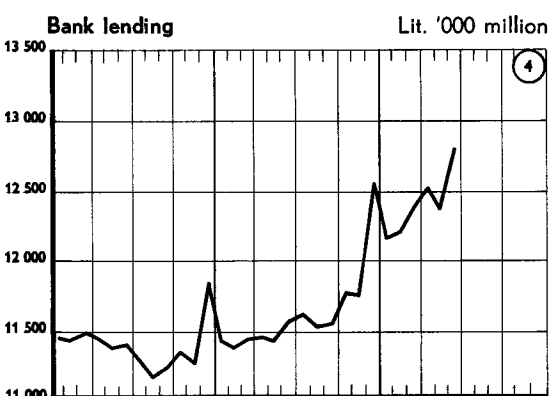
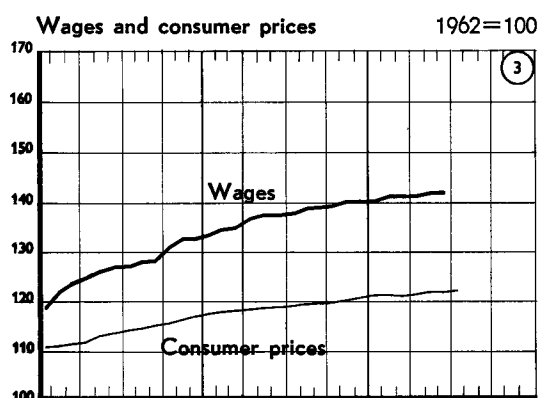
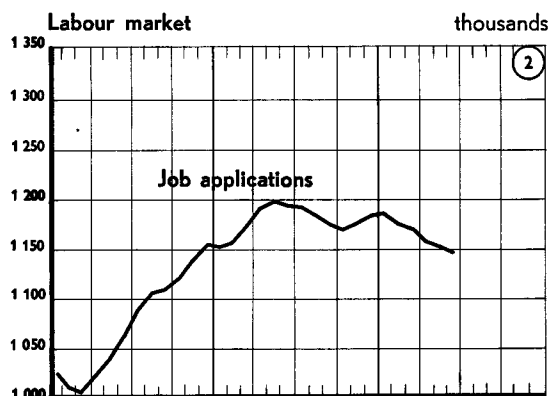
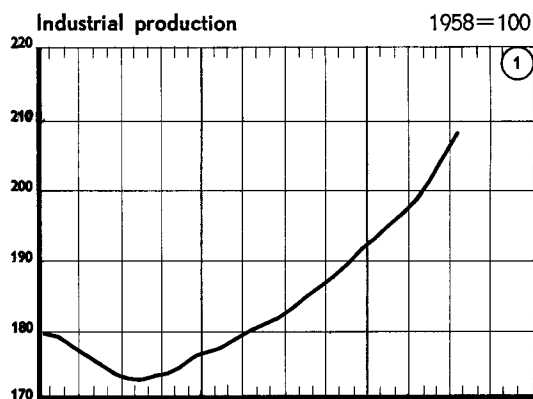
The Government has also presented the budget estimates for 1967. These put expenditure 11.7 % higher than the estimates for 1966, and revenue 9.3 % higher. The deficit is estimated at Lit. 1 165 000 million, compared with a deficit of Lit. 892 000 million in the estimates for 1966. If account is also taken of the government expenditures which are financed outside the budget, that is, directly by borrowing on the capital market, the overall deficit for 1967 works out at Lit. 1 851 000 million, or about Lit. 130 000 million less than that for 1966.

In preparing the budget estimates for 1967, the Government has endeavoured to make allowance for the requirements of short-term economic policy. In particular, the planned increase in current expenditure—in other words practically all outlays that affect consumption—is smaller than that which was estimated for 1966. It is true that the rate of increase for 1967 is fully 14.5 %, but this figure is considerably swollen by the fact that different methods of accounting have been adopted, since—by a change which makes a welcome move towards the principle of an all-embracing budget—the new expenditure estimates include items which for 1966 are still financed outside the budget. The change, incidentally, affects in equal measure the growth rate of planned capital expenditure, which works out at 5.3 %.

Nevertheless the budget estimates for 1967, like their predecessors, do not seem to be entirely consonant with the needs of short-term economic policy. First, the planned reduction of the deficit is very small; secondly, the forecast of additional tax revenue on which it is partly based appears decidedly optimistic. Moreover, even making allowance for the change in accounting technique referred to above, the growth in current expenditure implicit in these figures is undoubtedly still too rapid, especially when compared with the corresponding development of capital expenditure. Lastly, experience has shown that the Government's actual cash transactions will probably deviate in greater or lesser degree from the figures voted. Even if—and this is hardly likely—the deviation should have the effect of “correcting” the trend of these cash transactions in the direction required by short-term economic policy, this is unlikely to change the basic trend towards an unduly rapid increase in current expenditure. The question therefore arises whether this expansion of expenditure could not be reduced in the course of the further discussions on the budget estimates.



## 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 1964 GNP
	1959	1960	1961	1962	1963	1964	1965		
Gross national product	6.5	6.3	7.8	6.2	5.5	2.7	3.4	145.3	—
Industrial production	9.5	10.7	8.7	9.1	6.8	1.8	3.1	161.3	—
Total imports	11.8	37.3	14.6	16.4	22.4	- 5.1	0.9	240.1	15
Private consumers' expendi- ture	4.7	5.9	6.9	6.3	8.9	2.3	2.1	143.2	62
Public current expenditure on goods and services	4.4	4.0	4.8	5.4	5.1	4.0	3.7	136.0	15
Gross fixed asset formation	9.8	17.0	11.1	8.8	6.9	- 8.2	- 7.4	141.1	20
Total exports	18.4	18.9	16.2	12.3	6.9	11.7	19.9	263.0	18
Gross national product per capita	5.8	5.7	7.2	5.5	4.7	1.8	2.5	138.3	—
Gross national product per person gainfully employed	5.7	6.5	7.6	7.3	7.2	2.9	5.3	150.8	—



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
<b>Visible exports</b>										
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	2 883.3	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
<b>Exports of food, beverages and tobacco</b>										
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
<b>Exports of raw materials and manufactures</b>										
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	38.8
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
<b>Visible imports</b>										
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
<b>Imports of food, beverages and tobacco</b>										
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	385.5	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
<b>Imports of raw materials and manufactures</b>										
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	181,9	178,6	181,5	175,4	191,6	139,8	187,9	191,1	189,7	190,7
	1966	184,8	182,2	204,2	193,8	208,4	195,6						
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	136,3	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					
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	284	318	296	241	330	354	319	542
	1966	313	231	275	313	(315)	(333)						
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						
Total visible exports (million u.a.)	1964	475,7	452,0	414,8	505,1	444,2	532,1	546,6	454,9	533,4	538,8	500,5	532,8
	1965	514,1	562,1	583,0	613,6	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						
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	- 23,4	- 25,0
	1966	-144,3	- 64,2	- 14,9	- 55,8	+ 4,8	- 8,2						
Official gold and foreign exchange reserves (net, million u.a.)	1964	3 154,1	2 958,7	2 748,3	2 728,9	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	4 336,4	4 337,6	4 404,2	4 433,8	4 537,3	4 772,8					
Money supply (Lit. '000 million)	1964	11 058	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							

( ) 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 *assegni*) issued by the Central Bank and of other banks and credit institutions.

## D. The Netherlands

*All the elements of demand contributed, though in different degrees, to the continued expansion of overall demand in the second quarter and in the summer months. Resources were somewhat less overloaded than previously, mainly owing to a certain decrease in the rate of growth of expenditure on fixed asset formation, as well as to the considerable progress made in production and productivity, together with cyclical stock movements and special factors. The current balance of payments tended to recover; the relatively strong upward movement of costs and prices continued, but proved to be less vigorous, especially in the late spring and summer, than in the first quarter.*

*It does not appear likely that changes in the economic situation, either in the next few months or during 1967, will be sufficiently fundamental to justify expectations of even a relative stabilization of unit costs and prices. There may be some further slackening in the rise in capital expenditure, but the expansion in consumer expenditure seems likely to slow down comparatively little, particularly since the labour market is likely to remain very tight. Production will be able to increase less vigorously than in 1966. Some improvement in the current balance of payments may indeed take place, but prices are likely to rise still further, largely owing to the upward thrust in production costs, which shows only slight signs of slowing down.*

*These prospects indicate the lines that will determine short-term economic policy; the first aim of budgetary measures must be to exert a real braking effect on the expansion of public expenditure, especially where such expenditure does not create fixed assets, and so to reduce the overall budget deficit; in this way a further easing of the labour market could be achieved, the upward movement of cost incomes inhibited and support for the tendency to greater stability reinforced.*

### 1. Recent developments

In the early spring at all events the expansion of overall monetary demand continued at a brisk rate. The same is probably true of the summer, when the seasonally adjusted figures are considered, although once again the dips which the holidays cause in the graphs for major indicators were more marked than in the preceding year.

External demand as measured by actual exports of goods and services, which was somewhat hesitant in the first quarter, largely as a result of special factors, appears to have experienced a distinct revival in the second quarter. This is true at least of visible exports, for which the total figures had been particularly affected in the first quarter by the special factors just referred to (chiefly foot and mouth disease). Customs returns show that in the second quarter the value of these exports exceeded that for the same

period of the preceding year by nearly 11 %, whereas in the first quarter the annual rate of increase had been no more than 3 %. In July and August, however, exports were only 8.5 % above those of a year earlier.

The recovery in the growth of visible exports between the first and second quarters was almost wholly a result of higher deliveries to other Community countries, which received a special impetus from the disappearance of the inhibiting factors referred to above; there was little change in the rate of increase of sales to non-member countries.

Exports of services, too, appear to have increased faster in the second quarter than in the first.

The rapid expansion of domestic demand in money terms continued. Expenditure on gross fixed asset formation, seasonally adjusted, appears once more to have risen appreciably, although it seems that financing difficulties are increasingly slowing down the expansion of public expenditure on investment, particularly public works, and although the upward trend of total expenditure on housing probably remained at the slower pace which had already been visible in the first quarter. Capital expenditure by enterprises, on the other hand, remained buoyant. It is true that there was some decline in the rate at which expenditure on plant and machinery was rising, but on the other hand capital expenditure on industrial building appears to have been rising faster.

On the whole the impetus given by investment in stocks appears to have diminished slightly.

Thus, although total investment demand has not perhaps been rising as rapidly as hitherto, the expansion of consumer expenditure has speeded up again. To just what extent this holds good for public current expenditure on goods and services is not clear from the available information; but there is no doubt that a strong upward trend has continued, bringing it to a level which, notwithstanding certain economy measures, will mean that over the year as a whole the budget will be appreciably exceeded.

At all events private consumers' expenditure again grew at a faster rate after the slight slackening observed in the first quarter. According to the CBS Index, the amount expended under this head in the second quarter was a good 11 % above that for the corresponding period of the previous year. However, since the level of prices rose by no less than 6.5 %, the year-to-year growth rate by volume was lower, at 4.7 %. The renewed acceleration of the expansion of consumption in the second quarter was particularly noticeable in consumer durables.

This trend in consumption is partly explained by special factors, in particular fluctuations in the proportion of disposable private incomes saved. These fluctuations resulted from the increases in indirect taxation which took place at the beginning of 1966 : there was a wave of speculative buying and a decrease in the savings ratio towards the end of 1965, a reduced propensity to purchase with a correspondingly steeper rise in the savings ratio during the first quarter of 1966, and then a revival of purchases and a decrease in the savings ratio as the dominant trend reasserted itself in the second quarter.

But incomes, too, were rising fast. There was, it is true, a gradual weakening of the expansionary effects on net incomes of the reduction of taxes on incomes and wages implemented in the middle of 1965. Nevertheless the total wages bill once again rose considerably, even though somewhat more slowly, and this was due not only to the persistent rise in employment but even more to the continuance of steep increases in wages and salaries. It is noteworthy that wage increases due to sliding wage clauses incorporated in several wage agreements in the previous year contributed to this development for the first time. Between March and June the standard all-industries wage index rose by only 0.8 %, compared with an increase of 1.5 % in the same period of the preceding year, but this does not sufficiently reflect the still very marked upward trend of real wages and salaries, because approval for a number of newly concluded wage agreements had been held up by the authorities, who had in May set an upper limit of 7 % for wage and salary increases; it appears that in this index no account is taken of increases in wage scales which have not been approved. Furthermore, the total amount of holiday pay has risen appreciably this year.

The quite considerable growth of domestic demand continued. Industrial production again expanded appreciably between the first and second quarters when, according to the CBS Index, calculated in terms of gross output per working day, it was a full 6.5 % higher than in the same period of 1965. In the building sector the year-to-year growth rate was probably even higher, and the same is probably true of services.

Lastly, there was an increase in agricultural production. Initial estimates suggest that both crops and livestock production were heavier than in 1965. The real increase for the full year may be approximately 3 %.

Increased productivity again made a comparatively large contribution to the increase in production. Together with the considerable increase in the labour force, this resulted in a further tendency for the situation on the labour market to ease. There was a slight increase in the number of unemployed, seasonally adjusted; in July the unemployment ratio (defined as the ratio of the unemployed to the total labour force), seasonally adjusted, was 1 %, compared with 0.9 % in the first half of the year and 0.8 % in 1965. In spite of this, the number of vacancies notified in July 1966 was still 117 000, or three times the number of those unemployed, which was 39 000. The position therefore remained distinctly tight, even though there are unmistakable signs of a certain change in the climate of the labour market.

Imports of goods and services seem to have slackened somewhat. Visible imports, in particular, remained on the high plateau already reached in the first quarter. In the second quarter they were nevertheless some 10 % in volume and 11.6 % in value above the level of a year earlier. In July-August the volume of imports was only 4.5 % higher than in the corresponding months of 1965, but this appears to be mainly due to the increase that has occurred since last year in the fluctuations due to holidays.

The weakening trend of imports observed in the second quarter affected mainly imports of capital goods and raw materials; it was probably due in part to the slackening

in the growth of expenditure on plant and machinery, and also no doubt to special factors which will have had only a transitory effect. Imports of consumer goods again rose rapidly.

The basic trend of prices was still upwards, but it has been masked since April by a fall in food prices, partly seasonal and partly due to the harvest of some important agricultural products having been better than in 1965; since May these factors have been reinforced by the effects of the more stringent direct price measures imposed by the Government. The prices of finished goods, which had increased sharply in January, showed a further slight rise in May. For the reasons mentioned, however, the cost-of-living index rose by only 0.8 % between March and July, compared with an increase of 2.5 % in the same period of the preceding year. The average level of the index in the second quarter was 6.5 % above that a year earlier, and in July 5 %.

In the second quarter exports again expanded strongly while imports showed a more hesitant tendency, and this eliminated the marked tendency, observed since summer 1965, for the current balance of payments to deteriorate. Notwithstanding some deterioration in the terms of trade, the deficit on visible trade, as shown by customs statistics, fell from Fl. 1 696 million in the first quarter to Fl. 1 045 million in the second but it was still appreciably higher than the Fl. 891 million for the second quarter of 1965. As there was also an improvement in other current items, the deficit on current payments showed an appreciable improvement compared with that for the first quarter (Fl. 345 million instead of Fl. 805 million). Since in addition capital movements, which closed the first quarter with a heavy deficit, were again in surplus, the deficit for the second quarter in the overall balance of payments was only Fl. 164 million, compared with Fl. 786 million in the first quarter. The Central Bank's gold and foreign exchange holdings decreased by Fl. 132 million, and the net foreign exchange position of the commercial banks deteriorated by Fl. 32 million.

The impact of the balance of payments on domestic liquidity was consequently much smaller than previously. Furthermore, the cash transactions of the public authorities, whose financing deficit was again very high and was no doubt once more met partly by short-term borrowing, must have had a further expansionary effect. Until April at least bank advances to business customers also continued to expand; short-term bank lending in particular, after seasonal adjustment, showed a clear rise, with the result that the penalty deposits made by other banks with the Central Bank, calculated on the basis of the amount of credit outstanding in May, reached a new high point for the year at Fl. 212 million, though later they fell back to a level slightly below that of a year earlier.

In spite of these developments outside the banking system, the liquidity situation came increasingly under strain. On the money market there were insistent demands for liquid funds, bank liquidity having after all evidently come under pressure because of factors such as the balance-of-payments deficits and the large expansion in bank lending. The capital market too was affected by factors such as the heavy demand for capital coming from the public sector. The strain on available funds resulted in a sustained rise in both short- and long-term interest rates.

This rise in interest rates has, however, slowed down since June; one reason may well be the improvement in the balance of payments, where the capital movements item is likely to have responded to the higher internal interest rates; at times in fact, the rise in interest rates ceased altogether. Public loans which have been floated since June have been very well taken up, especially the Government bonds issued in August, which for the first time bore a nominal interest rate of 7 %.

## 2. Outlook

The tempo of expansion of overall demand in money terms may abate somewhat until the end of 1966, but it is likely to remain comparatively rapid.

The pace at which exports of goods and services, especially visible exports, have been growing is unlikely to rise again. According to the results of a business survey carried out by the CBS, managements have of late no longer been so regularly more optimistic about the development of export orders than when previously questioned. Some slowing down may be caused by the tendency for imports into the Federal Republic of Germany to ease, and still more by the expectation that imports into the United Kingdom will come under pressure; these two countries account for a considerable proportion of exports from the Netherlands (approximately 36 %). This might offset to some extent the continued buoyancy of exports to countries such as the United States, France and Italy. Moreover, there is unlikely to be much expansion in exports to the other Benelux countries.

The rate of expansion of domestic demand in money terms is however expected to slacken somewhat—and this could mean that there will be a relatively marked increase in the quantity of goods available for export.

Expenditure on gross fixed asset formation will show an appreciable further increase, but the pace will be slower than before. Both the shortage of finance and the savings programme introduced by the Government last May will slow down the growth of total public expenditure on investment. Furthermore housing will continue to be less buoyant than in 1965; indeed, the demand for unsubsidized housing may even decline as a result of increased tightness of the capital market and the rising rates of interest. The latest figures on the number and value of house-building permits issued seem to confirm this assumption.

These trends, together with the productivity increases, may lead to an easier situation on the building market, and it may again become possible to treat somewhat more generously applications from enterprises wishing to build. In view of the backlog of potential demand, such applications have already benefited from the freer granting of permits, and this in turn provides some support for investment in plant and machinery; at all events, information on the flow of orders booked by the capital goods industries up to the first quarter showed that the earlier recovery was being maintained. All in all, the trend of fixed asset formation by enterprises, at least in industry, appears still to be

strongly upward, though considerable differences are likely to appear between firms in different sectors and of different sizes. Owing to the upward trend of prices, to considerably improved productivity and to the continued expansion of credit, funds appear unlikely to be quite so difficult to obtain as has been sometimes assumed, at least for the immediate future.

Investment in stocks, particularly of raw materials and semi-manufactures, may show some further decline, partly for cyclical reasons, partly because of the quieter trend in world prices.

Public current expenditure will undoubtedly continue to rise at a rate which, though brisk, may be somewhat slower than hitherto as a result of the economy measures introduced in the spring—in particular a temporary stop on recruitment for the civil service and cuts in military expenditure.

Some slowing down in the rate of expansion of private consumers' expenditure is to be expected for a while, inasmuch as there was, for reasons set out above, a sharper rise in the second quarter than in the first. Nevertheless the underlying trend will continue to be sharply upward, even though the total number of hours worked is unlikely to rise as fast as in the corresponding period of 1965. Moreover, disposable incomes will again feel the full effects of progressive rates of direct taxation. The rise in actual wages and salaries was and still is considerable, even since in May a statutory limit of 7 % per annum per head was set to the increases in hourly wage rates. Transfer incomes are also continuing to expand rapidly; nor, in view of the very limited improvement in the general price situation and the buying that may occur towards the end of the year in anticipation of tax changes, is personal saving likely to do much to slow down the expansion of consumer expenditure; indeed, it is if anything more likely, from the autumn onwards, to work in the opposite direction.

Because of these developments in demand, domestic production will continue to rise; the output of industrial products however may expand at a somewhat slower rate as a result of slower growth in this component of demand.

In view of the likelihood that productivity will go on rising relatively strongly and that the labour force will also increase, the labour market may again tend to be slightly less tight, though the shortage of manpower, especially of skilled workers, is unlikely to improve to the point where there could be a genuinely moderating influence on the movement of wages.

Imports of raw materials and semi-manufactures are likely to ease somewhat, and purchases of capital goods will probably increase at a rather slower overall rate than hitherto. As a result of the good harvests, imports of agricultural products are likely to be on a more moderate scale, though the overall trend of visible imports should be clearly upwards.

The outlook for visible exports and imports implies that the deficits on visible trade will continue to decline, with a consequent improvement in the current balance of payments—though perhaps not so marked as between the first and second quarters.



A number of factors are combining to exercise a restraining influence on the level of prices. One of these is the "relative price freeze" decreed in May, which will remain in force until at least the end of the year. The quieter trend of import prices will also have some effect and, as already noted, overall demand in money terms is rising at a somewhat slower rate than hitherto. Furthermore, supplies of some agricultural crop products which affect the cost-of-living index have improved again. All this, however, should not conceal the fact that in the present economic situation prices and costs are still tending to rise far too steeply, even though the pressure of costs will probably not be so strong as in the corresponding period of last year.

Thus neither the outlook nor the analysis of the changes which have taken place since the beginning of the year suggests that the quantitative forecasts on the supply of goods and services and their use for the full year 1966 published in the last Quarterly Survey need substantial revision. Only for total exports and total imports are slight corrections required; the "external contribution" is still negative, even though rather less so than was initially forecast. The growth of the gross national product is still provisionally estimated at 5.5 %.

*National product and expenditure*

	1963 <sup>(2)</sup>	1964 <sup>(2)</sup>		1965 <sup>(2)</sup>		1966 <sup>(3)</sup>	
	At current prices (in Fl. '000 million)	% change on preceding year					
		Volume	Value	Volume	Value	Volume	Value
Gross national product	52.86	+ 8.8	+ 17.0	+ 5.4	+ 11.0	+ 5.5	+ 11.5
Imports <sup>(1)</sup>	26.19	+ 14.8	+ 17.9	+ 7.4	+ 7.7	+ 9	+ 10
Private consumers' expenditure	31.52	+ 6.1	+ 12.9	+ 7.8	+ 11.9	+ 4.5	+ 10.5
Public current expenditure	8.19	+ 2.8	+ 19.4	+ 0.9	+ 11.2	+ 2	+ 11.5
Gross fixed asset formation	12.38	+ 16.9	+ 24.2	+ 5.1	+ 9.4	+ 7.5	+ 12.5
Exports <sup>(1)</sup>	26.48	+ 11.8	+ 14.4	+ 9.1	+ 10.6	+ 7.5	+ 9

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> Statistical Office of the European Communities, General Statistical Bulletin No. 7-8, 1966.

<sup>(3)</sup> Commission estimates.

Notes :

a) The difference between the figures for product and those for expenditure 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.

Nor does any alteration appear necessary so far in the forecasts made in the last Quarterly Survey of how the economy is likely to develop in 1967. It still seems certain that expenditure on investment, but only on investment, will slow down appreciably during the period—though not enough to bring about a significant easing of the labour market, and so to curb the rise in mass incomes and the expansion of consumer demand in money terms sufficiently to help in stabilizing prices; for public current and transfer expenditure will no doubt rise very appreciably once more, while exports will show a further considerable increase—even though, despite the slowdown in domestic expenditure on investment, this increase will probably not be much faster than that between 1965 and 1966. It is to be feared that the decisions concerning wages and the working week in 1967 will result in further considerable rises in unit prices, especially since gross national product is not expected to increase by more than 4 % if working hours are in fact shortened.

It is thus still perfectly reasonable to assume that in 1967 the growth of real gross national product will be accompanied by persistence of the inflationary tendencies at home. However, the current balance of payments may show a further improvement, largely because of the slowdown in imports, especially of capital goods, raw materials and semi-manufactures, and it may even swing back to moderate surpluses.

It must none the less be said that these forecasts are extremely tentative. The situation might still be changed by the short-term economic policy followed, particularly in connection with the budget, and by the decisions on wages. When this survey was prepared the most important decisions in these two areas were not known or had not yet been taken.

It is unofficially reported that in 1966 the rise in the so-called “relevant” government expenditures, which according to the current budget were to be about 11 % higher than the outturn for 1965, will in fact rise faster than planned, even though the rise may not be quite as rapid as between 1964 and 1965 (18.5 %). At the same time, current revenue will again fall short of original budget estimates, although the expansion of turnover and incomes will have been appreciably more inflationary than originally expected: revenue for 1966 has suffered from the impact on yields of pre-tax-increase buying towards the end of 1965. In addition the incidence on the yield from the wages tax in 1965 of reduced direct taxation seems to have been underestimated. The 1966 deficit should be roughly double the figure originally estimated (Fl. 1 100 million) and should thus beat the 1965 record of Fl. 1 800 million.

However, it now appears that a substantial reduction in the rate of growth of expenditure is after all being planned for 1967. This would in any case be essential, but is made more so by the determination to implement on 1 January 1967 the second cut in the income and wages tax, which will lead to a drop in revenue of approximately Fl. 800 million a year; in addition there appears to be no readiness to effect a corresponding increase in indirect taxes on the same date, apart from applying the increases for textiles and the footwear industry which had been decided upon earlier, and certain measures relating to taxation of petroleum products. It is also understood that direct taxes are to be collected more quickly. This would mainly affect company profits, since the direct tax is already deducted from wages at source. This incidentally would affect the trend of

government revenue in 1968 compared with 1967; it appears that there will then be a general rise in indirect taxation to offset this.

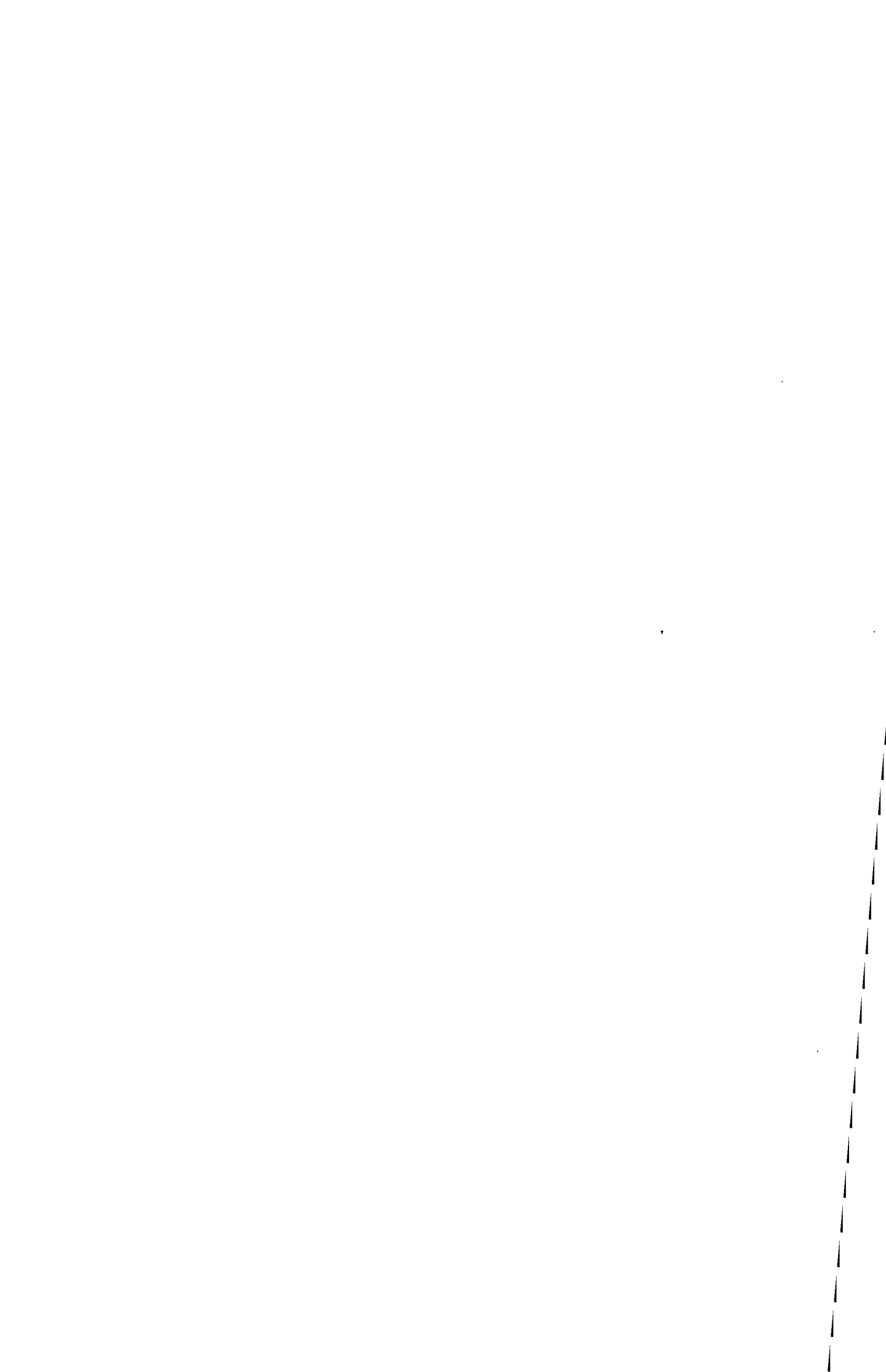
In what way the expansion of government expenditure is to be limited is not known—nor how heavily this will bear on expenditure going directly or indirectly to consumption and how heavily on investment outlays. Neither is it known to what the deficit, or “net impetus” is to be reduced. It is greatly to be hoped that some braking action is intended, and that it will bear mainly on consumption expenditure.

Even if the 1967 budget does show a reduced deficit, this would not of itself be enough; it would on the contrary also be necessary that the sums appropriated should not again be considerably exceeded in the course of the year, as has consistently happened up till now.

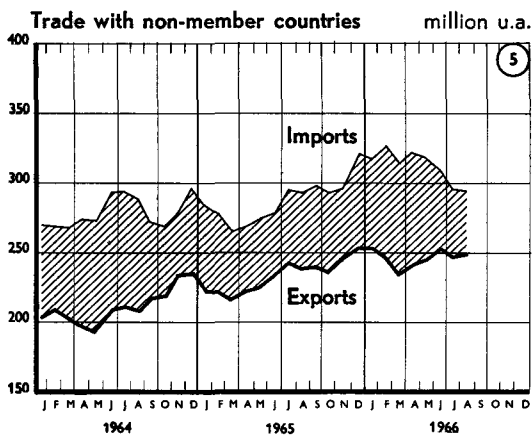
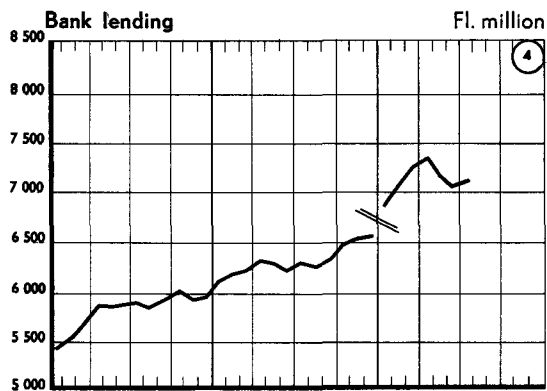
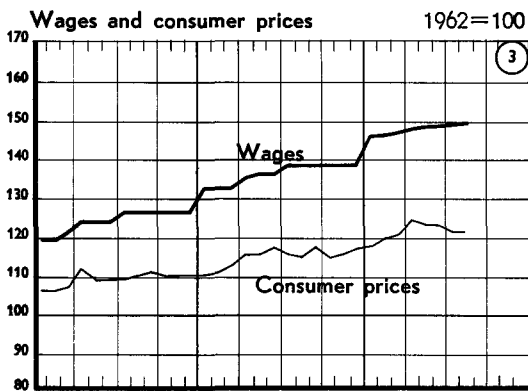
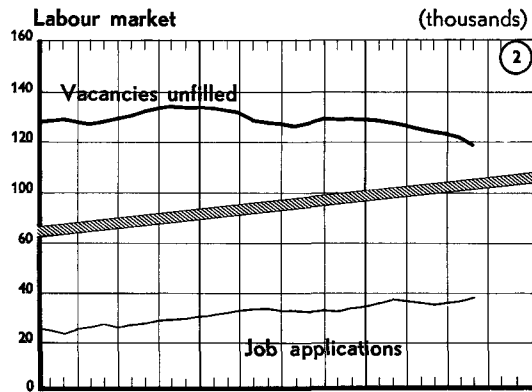
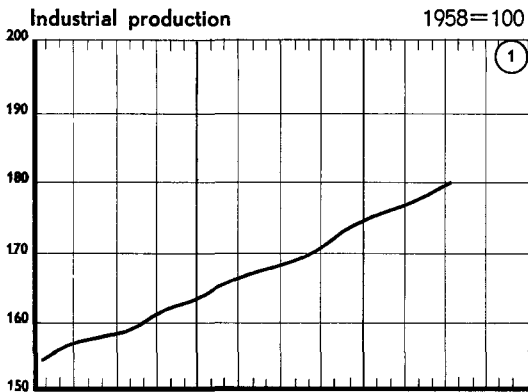
Unless the public authorities pursue a policy of genuine restraint, it is unlikely that the two sides of industry will reach agreements compatible with the need to stabilize unit costs and prices. Moreover, the disadvantageous effects of the new medium-term wage agreements, containing not only provision for high annual wage-rate increases (usually 5 %) but also sliding-scale clauses which may add up to 2 % more according to the rise of the price level, are already becoming apparent in these areas. The authorities should therefore do everything in their power to ensure greater moderation.

The need to exercise the greatest restraint in public finances and in wages was indeed confirmed recently in the “Eighth Half-Yearly Economic Report”, unanimously approved by the Economic and Social Council of the Netherlands at a meeting on 8 July 1966. Especially worthy of note is the conclusion in this report that suitable measures are urgently necessary to counteract the danger that the effects of a policy of restriction applied too late might act cumulatively with the results of a spontaneous decline in fixed investment.

This however does not warrant the conclusion that monetary and credit policy curbs should be relaxed again soon in anticipation of a possible slackening of investment expenditure. Monetary and credit policy should continue to impose restraints until such time as budget policy itself comes to exert a much more definitely moderating effect on the trend of domestic demand in money terms. As was shown by the mid-1966 measures on penalty deposits, the effectiveness of monetary and credit policy can be improved, especially since the balance of payments might move in such a way as to reduce the pressure on bank liquidity; this possibility of improvement will exist as long as unduly expansionary impulses continue to emanate from the deficits in public budgets and from the way in which these deficits are financed.



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. 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 1.1.1966.

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	8.5
— Industry	41.2
of which: Construction	(7)
— Services	50.3
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 1964 GNP
	1959	1960	1961	1962	1963	1964	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	+ 4.6	+ 9.5	+ 6.0	159	—
Total imports	+13.8	+17.3	+ 5.8	+ 7.5	+ 9.5	+14.8	+ 7.4	205	48
Private consumers' expenditure	+ 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	+ 7.4	+ 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	1965	1965	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	+15.8	+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	+26.9	+ 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	+ 5.8	+ 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	4 828	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	+18.8	+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	166	168	174	177	176	174						
Investment (Fl. million)	1964			3 333			4 030			3 913			4 100
	1965			3 744			4 283			4 224			4 581
	1966			4 131									
Building (Fl. million)	1964			1 362			1 682			1 783			1 613
	1965			1 545			1 814			1 993			1 854
	1966			1 587			2 079						
Private consumers' expenditure (1958 = 100)	1964	157	146	159	158	173	160	181	161	166	182	173	193
	1965	175	158	175	186	189	180	204	174	185	198	200	230
	1966	192	169	194	209	206	204						
Total visible im- ports (million u.a.)	1964	589	569	549	640	562	628	636	499	559	628	567	630
	1965	554	564	630	614	577	617	665	537	620	676	625	793
	1966	625	626	759	701	630	684	652	620				
Total visible ex- ports (million u.a.)	1964	452	446	440	479	455	491	484	405	561	552	505	538
	1965	477	489	532	506	501	554	543	438	596	594	557	611
	1966	500	470	572	570	544	612	549	515				
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	- 182
	1966	- 125	- 156	- 188	- 131	- 86	- 72	- 103	- 105				
Official gold and foreign exchange reserves (million u.a.)	1964	1 860	1 841	1 833	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	2 083	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	(2 003)	(2 003)				
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	15.67	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					

## 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

*The development of the economy over the last few months and the outlook to the end of 1966 indicates a slight slowing down in the expansion of overall demand.*

*These trends are by no means undesirable, for an easing in the pressure of demand, due principally to some weakening of foreign demand and also to some decline in the high rate at which consumer expenditure is expanding, should enable progress to be made towards stabilizing prices and costs. These have shown a further heavy increase and only recently, thanks to some special factors, has there been a tendency for the rate of increase to slow down.*

*General economic activity is unlikely to decline appreciably, sustained as it is by the continuing effects of investment by enterprises, public current expenditure and exports. On the contrary, economic growth in real terms is expected to be approximately the same in 1967 as it was in 1966.*

*The present temporary slowdown in economic growth is no reason for relaxing efforts to put the public finances on a sound footing. On the contrary a firm check should be placed on increases in public current expenditure in order to bring about a definite improvement in the ordinary budget and so to make more funds available for the non-inflationary financing of public investment.*

#### 1. Recent developments

The second quarter and, as far as can be seen from the statistics (some of which are appearing late), the summer months too were characterized by continued expansion of overall demand; in relation to the preceding months, (when it had already reached a high level), economic activity rose at a comparatively modest rate, despite the revival in foreign demand.

The growth of exports of goods and services again quickened noticeably. Customs statistics for the second quarter showed that the value of merchandise exports was 11.1 % higher than a year earlier, compared with a year-to-year growth rate of only 4.8 % in the first quarter of 1966 and 14.4 % in the last quarter of 1965. In particular, exports to non-member countries, which for fortuitous reasons had shown a considerable weakening in the first quarter, recovered appreciably, and deliveries to member countries also rose somewhat faster than during the early months of 1966.

The rise in expenditure on gross fixed asset formation appears to have continued at approximately the same rate as in the early months of the year. Indeed, the propensity to invest of enterprises appears to have strengthened somewhat, according to the latest surveys of business intentions, especially when the backlog of domestic orders in the capital goods industry is taken as an indicator. This however appears to be largely due to the vigorous expansion of investment outlay by foreign firms.

Investment by the public authorities also showed a further rise during the second quarter; here it seems that some decline in the rate at which expenditure by regional and local authorities was increasing may have been counterbalanced by slightly faster expansion in central government expenditure. On the other hand the growth-rate of investment in housing, which was still very high in the first quarter, appears to have lost some of its vigour.

Investment in stocks, at least at the manufacturers' stage, has certainly not increased very appreciably.

The pace at which consumer expenditure expanded had slowed down distinctly in the early months of the year, but in the second quarter it recovered somewhat. To judge by the partial information available, public current expenditure was again rising more rapidly, and private consumers' expenditure also rose more vigorously, though here the rise does not seem to have gone much beyond what was to be expected after the weakening that occurred in the first quarter owing to buyers' pre-budget and post-budget reactions.

The rising trend in the disposable incomes of households appears to have continued, since the quite rapid increase recorded in the total wages bill in the first quarter has continued almost unabated. The numbers employed and the hours worked per employee do not indeed appear to have risen, but a further sharp rise took place in hourly wage rates during the second quarter, largely under the influence of the sliding wage scales. Generally speaking, other incomes also tended to rise briskly, in the main because of an appreciable rise in transfer incomes resulting from the decision to raise old age and retirement pensions retroactively from 1 January 1966 (1 April for self-employed persons).

Domestic supply showed only moderate growth. The INS index of industrial production even fell back slightly between the first and second quarters, after adjustment for seasonal influences and fortuitous fluctuations. The unadjusted index showed an increase of only 2 % over the figures for the second quarter of the previous year. This weakening was due almost entirely to declines in consumer durables, raw materials and semi-manufactures. In the capital goods industries, on the other hand, expansion was maintained. When changes in the production index are being interpreted it should be borne in mind that it does not yet include many of the new enterprises whose production is naturally increasing very vigorously, and consequently gives too much weight to certain traditional branches of production such as coalmining, the iron and steel industry and textiles, some of whose difficulties are structural and not attributable to the current situation.

After seasonal adjustment, building showed a further increase, but the actual rate of growth was appreciably lower.

Aggregate agricultural production appears, on the available figures, to have exceeded last year's results, though it probably has not reached the very high level of 1964.

There has been a further tendency for strains in the labour market to ease, not only because of the limited growth of domestic production, but also as a result of the evident endeavours by enterprises to raise productivity in order to limit the increases in unit wage costs. Last but not least, the structural difficulties of some branches and regions had their effect on the manpower situation, with the result that there was a further slight increase in the seasonally adjusted number of unemployed.

The unemployment rate, defined as the ratio of the number of persons—fully or partly fit for work—seeking employment, as a proportion of the total labour force, was 2.1 % in July, compared with 1.8 % a year previously.

Largely because of slacker investment in stocks, imports of goods and services expanded rather more slowly in the second quarter than hitherto. Provisional customs returns show the value of merchandise imports to have been 9.9 % higher than in the second quarter of 1965, after a year-to-year growth rate of 15.4 % in the first quarter.

In the last few months the upward movement of both wholesale and retail prices has shown some signs of slowing down, partly because the passing on of higher indirect taxes was ceasing to have so marked an impact. Also, the Government decreed a general prices pause from May 6, and this no doubt had some influence (though it would be hard to say precisely how much) on the attitude and the expectations of transactors, dissuading them from applying or accepting price rises as readily as in the past.

Nevertheless prices still showed a very definite tendency to rise, though their effect on the retail price index was masked by seasonal movements and more particularly by the fact that the unusually high prices that had been paid for some important vegetable foodstuffs, particularly potatoes, came down as this year's harvest proved to be better than last year's. This led to stabilization, and even a slight dip, in the retail price index. Nevertheless in July-August the index was still 3.7 % higher than at the corresponding time of the last year and in the second quarter the year-to-year rate of increase was as high as 5.1 %.

Though the balance of trade as shown in the foreign trade statistics, remained in heavy deficit, there appears to have been some slight improvement. The deficit appears to have fallen from Bfrs 2 300 million in the first quarter to about Bfrs 1 500 million in the second, whereas a year before it had reached Bfrs 2 600 million. However, the current account showed a heavier deficit than in the first quarter (Bfrs 1 400 million compared with Bfrs 600 million) owing to a deterioration in the net surplus on services (on a transaction basis) and on income transfers. Owing to an increase in net imports of capital, the overall balance of payments was in equilibrium while in the period

January-March it was in deficit to the extent of Bfrs 500 million. As the net gold and foreign exchange reserves in the National Bank showed an increase of Bfrs 3 300 million between the first and the second quarters, the net foreign exchange position of the other monetary institutions must have deteriorated.

Transactions with abroad continued to curb the development of domestic non-banking liquidity. On the other hand, the financing of public current expenditure by short-term borrowing and the expansion of bank lending to business and private customers seem both to have been at a higher level than in the preceding quarter. Nevertheless the expansion of short-term lending by the commercial banks to business and private customers remained, at least until the end of June, below the ceiling fixed by the National Bank at the end of April 1966. On balance the money supply (including near money) rose by only some Bfrs 15 000 million from the end of the first quarter 1966 to the end of the second quarter, compared with Bfrs 17 500 million for the comparable period of the preceding year. The slowdown in the increase of liquidity was accompanied by a steady rise in interest rates on the money and capital markets.

## 2. Outlook

The expansion of overall demand is likely to continue during the remainder of 1966, but the pace is unlikely to be particularly brisk.

For one thing, foreign demand is hardly likely to supply any very strong additional impetus. Exports will probably continue to increase, though hardly faster than in the first six months of the year. This assumption is supported by both the backlog of orders from abroad, as currently estimated by managements, and by the economic outlook in those countries inside and outside the Community which take a significant proportion of Belgium's exports.

On the other hand the expansion of domestic demand looks like being no more than moderate during the next few months, though overall expenditure on gross fixed asset formation will probably continue to rise at the same rather brisker pace already observed in the first six months. Investment by industry may even rise somewhat more steeply than hitherto, owing primarily to the progress made with large projects undertaken by foreign firms, especially in the chemical and metalworking sectors. Of investment by the public authorities, expenditure by the central government may be expected to show a further appreciable rise until the end of the year, whereas the regional and local authorities will probably be unable to engage in any further considerable increases in expenditure because of difficulties in financing them. To judge from the incomplete information at present available, investment in housing is hardly likely to expand very markedly.

In view of the trend of world prices for raw materials and semi-manufactures, of the likelihood that final demand will remain relatively quiet, and of difficulties in obtaining finance, investment in stocks is not likely to add much impetus to overall demand.

Consumer expenditure will no doubt continue to expand. A further appreciable rise in public current expenditure on goods and services is to be expected, but only a moderate increase may take place in private consumers' expenditure. Private incomes, especially those of wage and salary earners, may rise less steeply than in the first six months. To judge by the results of the latest business surveys, the volume of employment can scarcely be expected to continue rising till the end of the year, and furthermore the rise in wage rates is again likely to lose some momentum, in part because the sliding scales will have little impact on wages during the period, in part because the basic trend of wage increases has been noticeably weaker for some months past. Lastly, other private incomes, particularly transfer incomes, are not expected to rise as quickly as hitherto.

Domestic supply may well show a fairly slow rate of growth during the next few months. The seasonally adjusted INS index of industrial production is unlikely to rise much above the average level of the first six months. Building and construction, on the other hand, may show a slight overall increase.

*National product and expenditure*

	1963 <sup>(2)</sup>	1964 <sup>(2)</sup>		1965 <sup>(2)</sup>		1966 <sup>(3)</sup>	
	At current prices (in Bfrs '000 million)	% change on preceding year					
		Volume	Value	Volume	Value	Volume	Value
Gross national product	695.6	+ 6.6	+ 11.2	+ 3.3	+ 8.2	+ 3.5	+ 8
Imports <sup>(1)</sup>	259.0	+ 11.1	+ 13.9	+ 7.8	+ 7.9	+ 10	+ 11
Private consumers' expenditure	472.4	+ 3.9	+ 7.3	+ 3.4	+ 8.1	+ 3	+ 7.5
Public current expenditure	90.9	+ 4.2	+ 7.8	+ 5.3	+ 9.6	+ 4	+ 10
Gross fixed asset formation	135.8	+ 12.8	+ 20.7	+ 1.4	+ 5.5	+ 3	+ 6.5
Exports <sup>(1)</sup>	254.2	+ 12.5	+ 16.1	+ 8.5	+ 10.4	+ 8	+ 9.5

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> Statistical Office of the European Communities. General Statistical Bulletin No. 7-8, 1966.

<sup>(3)</sup> Commission estimates.

*Note:*

a) The difference between the figures for product and those for expenditure 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.

Since domestic demand, particularly investment in stocks and private consumers' expenditure, is comparatively quiet, the expansion of imports is unlikely to regain much speed.

Prices may be expected to start creeping upwards again during the next few months, especially as relaxation of the controls on prices may lead to price rises that will be steeper because of the ground to be made up. But the rise may well be somewhat slower than in the early months of the year, first because the pressure of demand will be relatively limited, because the urge to pass on the effects of higher indirect taxes will largely have spent its force, and also, perhaps, because unit wage costs can be expected to rise at a slower rate. Of course the stabilization of world prices for raw materials naturally will have some effect too, while the fact that the prices of various foodstuffs, particularly potatoes, are lower than they were last year should help to moderate any upward trend in the retail price index during the next few months.

The development of the economy so far and the outlook for the rest of the year outlined above are broadly in line with the quantitative forecasts, published in the last Quarterly Survey, on the growth of the real gross national product and of the most important aggregates for the full year 1966. A somewhat slower expansion of exports of goods and services will be partly offset by a slightly stronger increase in fixed asset formation. Imports may also prove to have grown more slowly than was expected. The estimate for growth of real gross national product is unchanged at a bare 3.5 %.

Nor is any change required at present in the forecast regarding the expansion of overall demand and production in 1967 published in the last Quarterly Survey. It should however be noted that in consequence of the agreement recently signed between the two sides of industry to maintain the working week at its present length during 1967, it may be possible to expand domestic supply without much additional strain on the labour market. Gross national product at constant prices may rise by about 3.5 %, as in 1966, and the conditions for maintenance of the economic stability may become somewhat more favourable than in 1966.

Nevertheless there is no reason for departing from the aim of stabilization in short-term economic policy; it is still apparent that prices could rise excessively, and furthermore it does not yet seem certain that a satisfactory situation will be achieved in the balance of payments, especially in the current items.

A policy of restraint has been followed so far in monetary and credit matters, and in its budget policy the Government appears to be striving with success to limit the deficit on the regular budget to about Bfrs 3 000 million, though this will probably be attained mainly through the increase in tax revenue, for expenditure under the ordinary budget has already substantially exceeded the sums voted. In this connection it is noteworthy that the decrease in the Treasury's cash deficit for the first six months compared with the corresponding period for the previous year was due not only to a decline in the deficit on the ordinary budget but also to some reduction in cash expenditure under the extraordinary budget. And although this is partly counterbalanced by some extra-budgetary financing of the central government's capital projects (in particular the road fund) through

direct recourse to the capital and credit market, and by local government capital expenditure, the total increase in capital expenditure by the public authorities during 1966 will none the less be distinctly smaller than was originally forecast. This reduction of the overall deficit, leading as it will to a more moderating effect on the development of domestic demand than would otherwise have occurred, is naturally to be welcomed; but from the viewpoint of longer term economic growth a differently structured pattern of expenditure would be more appropriate. It must also be recorded that some use was again made of the practice of direct recourse to short-term foreign borrowing for financing the Treasury deficit.

As regards price policy, the price pause for goods and services, which was only partially effective, was recently ended, though all future price rises must be notified. The Government is prepared to agree to price rises in all cases where a careful examination shows that they are justified in terms of production costs and profit margins, though percentage trade mark-ups must not be increased.

Lastly, regional action was taken during the second quarter under the 1959 expansion legislation to promote directly productive investment, but the effects of these measures will of course be felt only gradually—and during the first six months of the year no very vigorous use was made by the Government of the various forms of action open to it under the 1959 legislation.

The way in which monetary and credit policy is at present being conducted is very well in line with what is required for stabilization and for the co-ordination of short-term economic policies in the Community. The Government appears to have succeeded in slowing down the expansion of liquidity and in bringing it nearer to limits at which development could take place without inflationary strains, and at the same time has held in check certain speculative features in the attitude of transactors. This was in fact facilitated by a spontaneous decline in the expansion of overall demand, due mainly to the slower growth of exports and the deterioration in the current balance of payments. Additional measures to restrain credit do not appear to be called for at present, though the monetary authorities should maintain a careful watch on the development of credit over the next few months and see to it that the proper limits are not overstepped once more. Any substantial easing of monetary and credit policies should be delayed until there are signs that the level of prices is really becoming sufficiently stable and the balance of payments is beginning to show a surplus on current account.

Continued action to limit the expansion of credit is of particular importance; the vigorous action taken by the Government to put the budget on a sound footing has not yet been entirely successful. It is encouraging to note that the recently introduced supervision of the transactions of semi-public institutions enables their financial transactions to be run along better lines; but when one comes to the budget proposals of the central authorities, it would seem that the ordinary expenditure of the Government will continue to rise almost unabated. For although the draft budget had not been published when this survey was written, provisional figures for the various main heads lead to the conclusion that ordinary expenditure is going to be more than 10% above the figure budgeted for

in 1966 and approximately 7 % over the estimated outturn for the year. Even on the assumption (which has never yet been realized) that actual expenditure will not rise at a noticeably higher rate than is provided for in the budget, this is a considerable increase. Furthermore the balance of the ordinary budget, as far as can be seen from the draft, appears to be far from secure. For one thing, since there is to be no increase in tax rates, the forecast of revenue appears to be very optimistic, and furthermore the dates laid down in an earlier law for booking the yield of certain taxes and contributions have been modified, so that their yield appears twice in the revenue for 1967. Clearly this will not make it any easier to balance the 1968 budget, in which receipts will be correspondingly lower than in 1967.

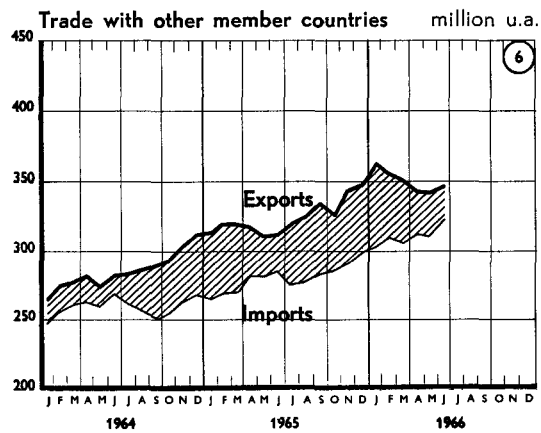
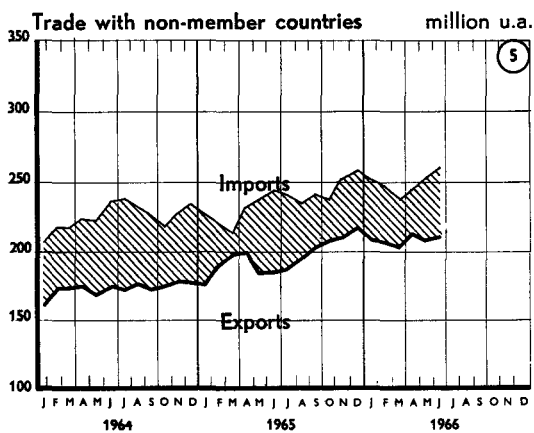
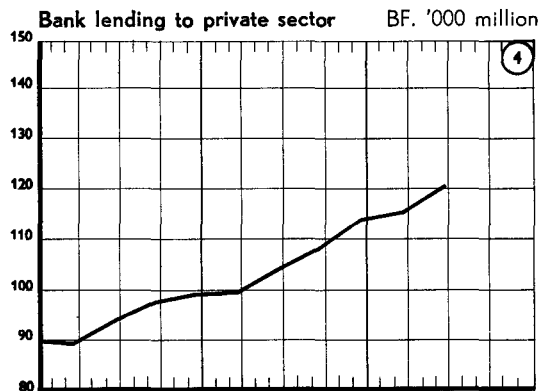
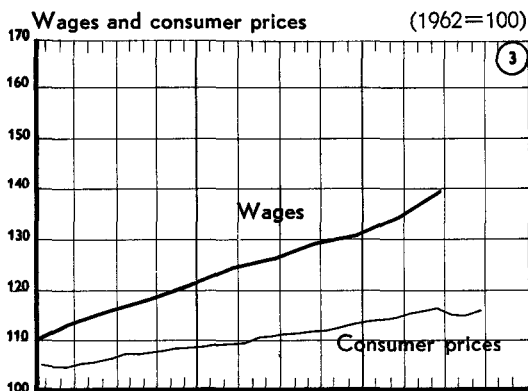
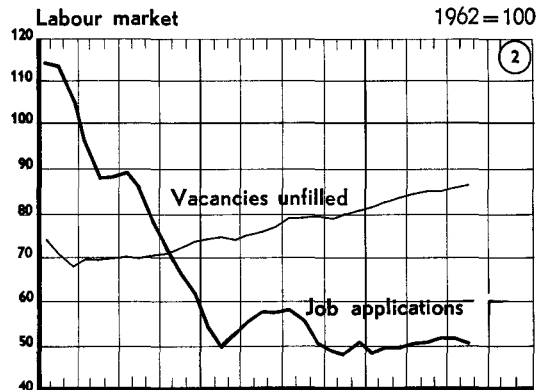
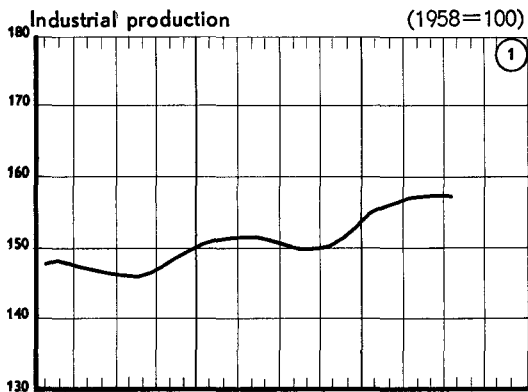
Consideration is now, it is true, being given to certain steps which would tighten up the collection of certain taxes, but these will not affect direct taxation (as could with advantage be done), being confined as before to indirect forms of taxation.

Lastly, it is understood that expenditure under the extraordinary budget is to be increased (approximately 10 % in real terms over the expected outturn for 1966). This in itself would be desirable, provided that the ordinary budget were not merely balanced but yielded an appropriate surplus, since otherwise it would be difficult to effect a reduction in the overall deficit for 1967 compared with 1966.

Experience shows that the maintenance of a large overall deficit always involves the risk of some recourse to short-term borrowing in order to finance it, and this could have unfortunate effects on prices and costs, preventing their stabilization. Alternatively it might lead to excessive demands on private savings, so that enterprises would find it still more difficult to obtain finance for their growing capital investment in productive facilities, and this would undoubtedly have an unfavourable effect on long-term economic growth. For similar reasons the "intermediate solution", of once more limiting the Government's overall deficit by cutting public investment expenditure, is not to be recommended. Therefore still further efforts should be made to achieve adequate surpluses in the ordinary budget, particularly by the imposition of sharper restraints on the expansion of public expenditure stimulating consumption directly or indirectly.



## 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. Adjusted for seasonal variations. Three-months moving average. 1962 = 100.

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 <sup>1</sup> (%)	
— Agriculture	5
— Industry	42
of which : Construction	8
— Services	53
Percentage share of gross domestic product :	
— Agriculture	6.2
— Industry	41.9
of which : Construction	6.9
— Services	51.9
Gross product per capita (Bfrs.)	88 400

TABLE 2 : Development of basic economic data

	% change by volume on preceding year							Volume indices (1958 = 100)	Contribution (in %) to 1964 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	+ 1.7	+ 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	+ 2.4	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			
<b>Visible exports</b>										
Total	+ 7.9	+14.7	+ 3.9	+10.2	+11.9	+15.5	+14.2	209	6 332	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
<b>Exports of food, beverages and tobacco</b>										
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
<b>Exports of raw materials and manufactures</b>										
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
<b>Visible imports</b>										
Total	+ 9.8	+15.0	+ 6.6	+ 8.0	+12.2	+15.9	+ 7.6	208	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
<b>Imports of food, beverages and tobacco</b>										
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
<b>Imports of raw materials and manufactures</b>										
Total	+10.4	+17.1	+ 7.6	+ 7.6	+12.7	+15.7	+ 6.6	208	5 548	87.0
Intra-EEC	+10.6	+18.4	+13.8	+ 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	155	160	153	157
	1966	143	142	159	151	145	158	118					
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	155.0	162.6							
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					
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	127.2	126.9	134.5	137.0	135.3	134.9	133.0	133.0	135.5	137.0	141.7
	1966	135.2	135.4	139.7	145.3	140.1	146.9						
Total visible imports (million u.a.)	1964	492	475	481	515	479	513	486	419	480	512	491	536
	1965	455	477	547	557	514	518	505	454	553	561	578	615
	1966	519	554	618	556	583	607						
Total visible exports (million u.a.)	1964	451	449	468	490	426	484	453	377	477	520	491	502
	1965	482	520	571	509	484	551	513	432	586	552	576	612
	1966	493	523	625	560	537	621	514					
Balance of trade (million u.a.)	1964	- 41	- 26	- 13	- 23	- 53	- 28	- 33	- 42	- 3	- 8	0	34
	1965	+ 27	+ 43	+ 24	- 48	- 30	+ 33	+ 8	- 22	+ 33	- 9	- 2	3
	1966	- 26	- 26	+ 7	+ 4	- 46	+ 14						
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	(1 980)	(1 974)				
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	308.5	321.0	325.2	331.2	330.7						

( ) 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

*No appreciable change appeared in the state of the economy during the second quarter and in the summer months. The contrast between the relatively unchanged demand for traditional products and the upsurge of exports from the new industries recently installed in Luxembourg was still very marked. Domestic consumer expenditure rose still further, while investment stagnated. There was little increase in domestic production.*

*The labour market is still tight and the upward movement of prices has continued to be fairly strong. Thus one of the main goals of economic policy should be to stabilize costs and prices, and budget policy ought to make a greater contribution to this objective than is at present planned.*

### 1. Recent developments

The slight increase in the value of exports of goods and services observed during the first quarter of this year continued during the following months. The various factors contributing to this result have remained virtually unchanged. A further decline in the volume of iron and steel exports was no doubt at least partially compensated by a small improvement in prices, especially within the Community. The exports of the newly-established industries have also increased still further.

The rate of growth of domestic demand has also remained virtually unchanged, though there is still a possibility that the decline that will probably have occurred in residential building despite the expansionary trend of public authority investment will have curbed the total increase of gross fixed asset formation, especially as fixed investment by enterprises is unlikely to have risen.

Private consumers' expenditure appears to have sustained the moderate rate of increase which was apparent in the early months of the year. The stabilization of activity in the traditional industries had a restraining effect on the development of incomes as well as upon the propensity to consume of households, and this doubtless counter-balanced in some degree the effects of the still considerable increases in transfer incomes and in the wages and salaries paid in other sectors.

Public current expenditure on goods and services, on the other hand, continued to expand fairly vigorously. Government expenditure at least must have increased faster than was provided for in the budget estimates.

Domestic supply continued to show only a small increase, the growth being mainly attributable to the growth of production in the new industries and in services. According

to the official index industrial production in the second quarter was 4 % below that for the corresponding period of the previous year, as it had been in the first quarter. However, this index does not yet cover the production of the most important of the new industries. Seasonally adjusted, building activity appears to have been at about the same level as in the January-March period.

The seasonally adjusted figures suggest that there has been a distinct slackening in the growth of imports.

Despite the slackening of demand for labour by the traditional industries, in which the level of employment has remained unaltered for several months, no real easing of the situation on the labour market is yet discernible.

Since March the cost of living index has been rising again, only partly in consequence of the movement of food prices. In the July-September period the official index was 2.4 % above its level for the corresponding period of the previous year. The slowdown in the annual rate at which prices were increasing—it had been 3.3 % during the first quarter—reflects the fact that very considerable increases had taken place between the first and second quarters of the previous year.

## 2. Outlook

The slow rise in exports of goods and services is likely to continue with little change until the end of 1966. There is even the possibility of some increase in the rate of growth thanks to the stabilization that can be expected in the volume of traditional goods delivered and to a small improvement in prices due mainly to a strengthening of international demand and the results of a more cautious production policy by steel producers in Europe.

On the other hand, expenditure on gross fixed asset formation is unlikely to rise appreciably during the next few months. For it looks as if the slight easing of the demand for residential building will detract from the expansionary effects of the revival in public investment expenditure. Moreover, investment by enterprises is likely to remain at a relatively low level.

The expansion of consumer expenditure may continue at about the same rate as in the preceding months. Public current expenditure in particular will show a further appreciable increase as a result of decisions already taken regarding the numbers to be employed and the wages and salaries to be paid in the public sector. Private consumers' expenditure will tend to increase because of the vigorous rise in transfer incomes resulting from changes in accident benefits, and also because of the wage increases impending in some sectors. Moreover, the sliding wage scale came into operation once again in September, and this will probably more than compensate for the slower rate at which incomes will rise in consequence of the virtual stabilization of employment.

Since this is the probable outlook for overall demand and its components, there is unlikely to be any considerable expansion of domestic supply. The industrial production index in particular may remain unchanged, while imports may continue to rise slowly, mainly because of the trend to be expected in private consumers' expenditure.

It is unlikely that the pronounced strains affecting the labour market will ease during the next few months, even though the overall level of employment will probably rise very slowly, as the traditional industries are reluctant to release workers, while the new industries and the services sector are still badly in need of labour. The tight labour situation tends in turn to perpetuate the rise in wage costs per unit of production, which is due not only to inadequate gains in productivity but also to the continued relatively vigorous upward movement of money wages. Largely because of this and because of the increase in the prices of imports, the price level is likely, apart from seasonal variations, to rise at about the same rate as hitherto this year.

*National product and expenditure*

	1963 <sup>(2)</sup>	1964 <sup>(3)</sup>		1965 <sup>(3)</sup>		1966 <sup>(4)</sup>	
	At current prices (in Lfrs million) #	% change on preceding year					
		Volume	Value	Volume	Value	Volume	Value
Gross national product	27 496	+ 6.5	+ 10.5	+ 1.5	+ 3	+ 2	+ 4.5
Imports <sup>(1)</sup>	23 753	+ 9.5	+ 12	— 0.5	+ 0.5	+ 3	+ 5
Private consumers' expenditure	16 641	+ 5.5	+ 9.5	+ 3	+ 7	+ 3.5	+ 7.5
Public current expenditure	3 484	+ 2.5	+ 6	0	+ 6	+ 3	+ 10.5
Gross fixed asset formation	8 826	+ 2	+ 7.5	— 18	— 16	— 6.5	— 3.5
Exports <sup>(1)</sup>	22 198	+ 13	+ 15.5	+ 4.5	+ 3	+ 4.5	+ 5

<sup>(1)</sup> Goods, services and factor income.

<sup>(2)</sup> Statistical Office of the European Communities. General Statistical Bulletin No. 11, 1965.

<sup>(3)</sup> Commission estimates.

<sup>(4)</sup> Commission forecasts.

*Notes :*

a) The difference between the figures for product and those for expenditure is accounted for by movements in stocks.

b) The estimates and preliminary estimates are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with experts from member countries, but they are established and published on the sole responsibility of the Commission.

The trend of the main aggregates since the beginning of the year and the outlook for the remaining months do not call for any great change in the quantitative forecasts

published in the last Quarterly Survey for the full year 1966. However, owing to the rather less vigorous growth of total exports it now seems necessary to adjust the predicted rate of growth of real gross national product slightly downwards from 2.5 % to 2 %. But it does not at present seem advisable to alter the probable growth figure for real gross national product in 1967, which was forecast at around 3 %, and so corresponds to the long-term trend. Meanwhile the latest information pointing to a considerable downturn in investment in the iron and steel industry offers no hope of any general revival of investment in industry.

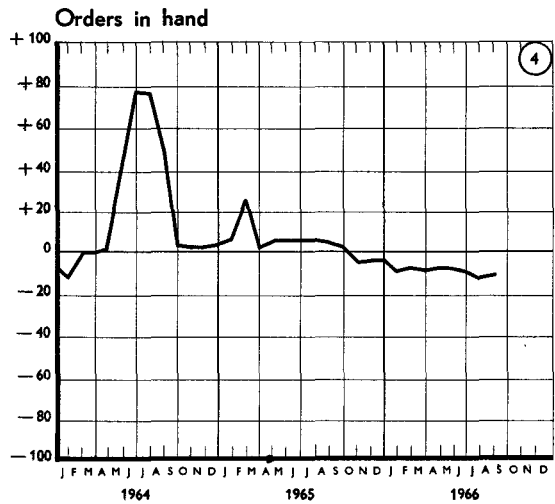
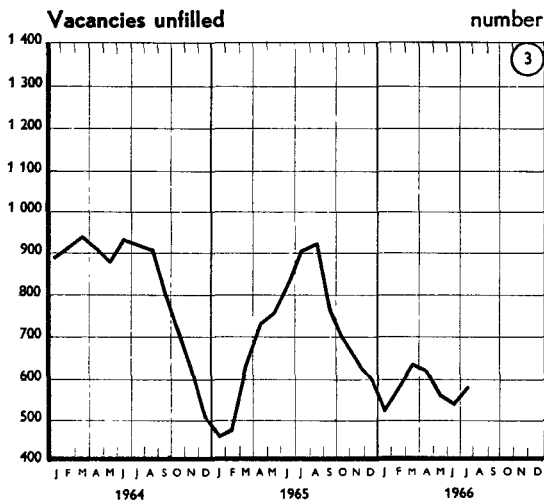
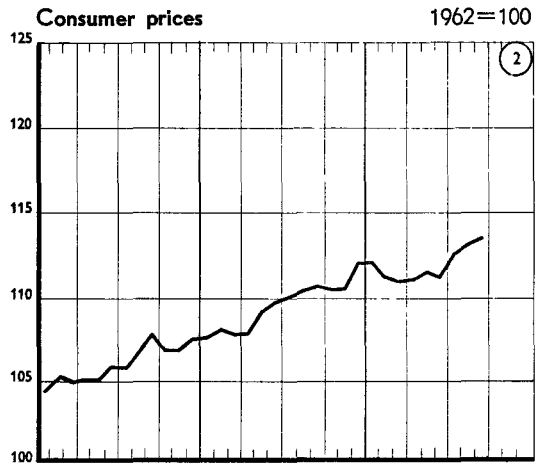
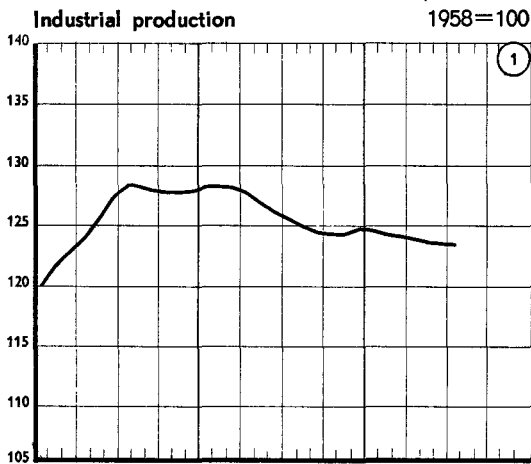
The considerations set out in the last Quarterly Survey No. 2/1966 regarding the short-term economic policy which should be followed call for little modification. It is however to be feared that the 1967 budget will do as little as its predecessors towards stabilizing prices and unit costs. It is understood that the draft budget estimates for 1967 provide not only for a rise of 13.6 % in government expenditure over the figures of the 1966 budget, but in addition a deficit of more than Bfrs 1 500 million, compared with 900 million in 1966.

It should however be pointed out that actual government expenditure in 1966 seems to be exceeding the budgetary provision, and there has been a considerable increase in borrowing. This would slow down the rate of growth for 1967 to about 7.5 %—always provided that in 1967 expenditure does not again exceed the sum approved in the budget. It is however strongly recommended that this should be avoided and indeed that the increase in non-investment expenditure should if possible be held down even further.

In addition, a number of recently adopted measures, especially those requiring longer annual holidays with pay and those affecting the length of the working week, represent a considerable further increase in wage costs. This could imperil the competitiveness of firms and their ability to finance an adequate proportion of their investment requirements themselves, and so prejudice the aim of a sufficiently rapid long-term growth of the economy. It is therefore highly desirable that for some time to come, at least, everything should be done to set strict limits on such further additions to 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	120					
Crude steel production ('000 m.t.)	1964	356	357	375	402	372	389	396	365	391	412	361	383
	1965	333	379	358	392	391	377	397	353	395	392	377	372
	1966	369	354	380	367	353	369	368	346				
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					
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				
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			

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.



**Council Recommendation of 28 July 1966**  
to the Member States  
in pursuance of Article 103 of the Treaty  
concerning arrangements to be made to improve  
trade cycle statistics

With the ever-growing interdependence of cyclical developments among the Member States, which has been particularly evident these last two years it has become necessary to strengthen the co-ordination of economic policies and this means an increased need for statistics on short-term trends. The statistical apparatus of Member States in its present form may no longer suffice to satisfy all the obligations flowing from Art. 103 of the Treaty.

The accelerated pace of implementation of the Treaty in essential fields of economic policy, such as the unification of industrial and agricultural markets, gives rise to certain common problems which call for urgent improvements in basic statistics. As the Community develops ever more rapidly in the direction of a unified economic area, it becomes necessary to consider certain questions from a comprehensive standpoint. New information is therefore needed at Community level.

As it is not possible to meet all requirements in a short space of time, a basic programme must be drawn up which will fill the principal gaps in figures on short-term economic trends, having regard first of all to their degree of importance for observing the course of the trade cycle and for short-term economic policy.

The Council, therefore, having regard to the Treaty setting up the European Economic Community and in particular Article 103 thereof, and acting on the proposal of the Commission, which has for this purpose consulted the Monetary Committee and the Short-term Economic Policy Committee, recommends that the Member States take the following steps to improve the compilation of statistics on short-term economic trends and their comparability.

**I. Programme for the near future**

It is recommended that the Member States :

1. Widen the basis of their industrial production indices so that they will reflect the whole range of industrial production apart from construction; that in weighting these indices they use the most recent data, that in particular they incorporate as soon as possible the results of the industrial survey relating to the year 1962, that they collate these results by the criterion of principal activity, so as to place in relief as far as possible industries producing capital goods, consumer goods and intermediate goods.

2. That they establish a separate index for production in terms of volume, in the first stage at quarterly intervals, adequately representative for building and public works as defined in the "Nomenclature of Industries in the European Communities (NICE)".

3. That they prepare, in the first place at quarterly intervals figures relating to inputs or order-books in industry.

That they compile quarterly statistics on turnover in industry, with a breakdown, using the nomenclature referred to in point 1 above, into goods for export and goods for the home market.

4. That they begin immediately preparatory studies for drawing up quarterly statistics on stocks of finished goods and raw materials in industry, agriculture, and the distributive trades.

5. That they establish, at intervals of no more than three months, indicators of movements in the number of wage-earners, showing the numbers employed in industry and in construction.

That they establish, at intervals of no more than three months, indicators of movements in hours worked in industry and construction.

6. That they draw up monthly unemployment figures, showing any changes with adequate precision.

7. That they establish, at intervals of no more than three months, indicators of changes in the actual earnings of workers in industry and construction.

8. That they establish monthly indices of all retail trade; and begin immediately the preparatory work for a quarterly index of all private consumption.

9. That they establish quarterly indices of retail prices, weighted, representative and covering all household consumption, these indices to be broken down into food products, industrial products other than foods, rents and other services.

10. That they establish in simplified form a balance of payments at intervals of no more than three months.

11. That they make available to the Commission the assistance of their appropriate government departments and national statistical institutes with a view to preparing coherent statistics of intra-Community trade.

12. That they make available to the Commission the assistance of their appropriate government departments and national statistical institutes so that a Community system of national accounting may be worked out and adopted as soon as possible.

13. That they begin preparatory work for the drawing up of Community statistics of the revenue and expenditure of the central government and if possible of all public authorities, together with the financing of deficits and the use of surpluses; that they supply a breakdown of expenditure under the headings of consumption, investment and transfer, together with a breakdown of revenues into the various types of tax.

## II. Programme for the longer term

It is further recommended that the Member States :

1. Prepare, after the necessary enquiries, figures on such factors as building permits, building starts and completions, reflecting as fully as possible cyclical movements in the building and construction industry, comprising housing, non-residential building and civil engineering works.

2. That they make the necessary enquiries to establish a breakdown of inputs or order-books in industry (other than construction), first according to the nomenclature referred to in Part I, 2 above, and secondly by origin, domestic or external.

3. That they make the necessary preliminary enquiries for the establishment of indicators for movements of production in the service industries.

4. That they study the possibility of establishing a general index of gross fixed asset formation, in the first stage every six months, either by direct observation or from the statistics for production and trade in capital goods.

5. That they draw up statistics on paid employment in sectors other than industry, together with indicators of movements between annual surveys.

6. That they establish a breakdown by categories of workers of statistics on unemployment or unsatisfied job applications.

7. That they study the possibility of obtaining quarterly statistics on total wages and salaries.

8. That they study the possibility of establishing indicators of transfer income.

9. That they study means of obtaining data on incomes other than from paid employment and of determining whether in certain cases the short-term analysis of such incomes would serve any practical purpose.

10. That they make enquiries in order to establish indices of building prices and of import and export prices.

That they collaborate with the Commission in defining the scope of production price indices and adopt common methods for their calculation, making a distinction between industrial and agricultural products.

11. That they improve where possible monetary and financial statistics as regards their details, exhaustive nature and comparability, particularly statistics on short-, medium- and long-term credit from the money and capital markets, issues of securities and the situation of banks.

12. That they classify by products their statistics on foreign trade in accordance with the nomenclature referred to in Part I, 2 above.

### III. General provisions

It is recommended that the Member States :

1. Authorize their national institutes of statistics and where appropriate other interested bodies to conclude among themselves and with the Statistical Office of the European Communities the necessary technical agreements; that they adapt as far as possible their methods, procedures and administrative practices so that these may not hinder the implementation of such agreements.

2. That they make available, so far as their general budgeting policy permits, the necessary funds to fulfil the purposes set out above.

3. That they reduce to a minimum the delay in supplying the statistics in question by drawing up, where necessary and so far as is possible, provisional tables; that they publish these tables or existing tables or transmit them confidentially to the Commission forthwith; that they issue, if possible within a month, figures for the following : industrial production, unemployment and employment, retail trade, foreign trade, retail prices, gold and foreign currency reserves, and balance of payments.

4. That they put in hand immediately the necessary work to improve certain statistics essential to trade-cycle policy, i.e. those referred to in Part I above, with a view to effecting such improvements within a period of three years.

### IV. Final clause

The Member States are requested to inform the Commission before the end of each calendar year of the steps they have taken to give effect to this recommendation.

Done at Brussels, 28 July 1966

By the Council

President

(signed) S.A. POSTHUMUS

Certified true copy

CALMES.

Secretary-General