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The Economic Situation in the Community

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In addition to the European economies' own problems, the rise in the price of oil and the recessionary tendencies developing in other industrialised countries allow only modest objectives for the Community as a whole to be looked for : real GDP growth decelerating from 3 % in 1979 to 2 % in 1980; price inflation rising to 9 % in 1980 on average, with deceleration in the course of the year; a swing in the balance of payments current account from the surplus in 1978 to deficits in both 1979 and 1980; and a renewed rise in unemployment in 1980, after the relative success in arresting its increase in 1979.

This prospect can hardly be considered satisfactory, even if better than the performance recorded by the Community economy following the 1973 oil price shock.

Further, the realising of this modest outcome requires that economic policies conform with certain fundamental principles :

- (i) in a first phase of policy incomes have to be constrained so that consumers absorb the increased cost of energy and secondary increases in inflation are avoided; meanwhile monetary policy should be kept strict, and budgetary policy should at this stage provide only very limited compensation for the effects of the oil price rise;
- (ii) as and when certain positive results are assured as regards inflation, then policy could eventually in the course of 1980 be adjusted into a more actively supportive posture, notably if investment and consumption were also found to be weakening significantly;
- (iii) energy policy must in any case be strengthened in all its aspects, since without achieving a sharp change in past relationships between oil imports and economic growth, there is little prospect for the latter to progress.

These guidelines aim at eliminating the risks of an inflationary skid and at finding, as quickly as possible, room for manoeuvre for higher growth and employment. Experience shows, in effect, that in an inflationary context

global measures intended to spark growth and thus improve employment are only palliatives, leading inevitably and quickly to the adoption of measures of contrary effect. Moreover, despite the prospect of a pause in 1980 in the process of improvement of employment levels, it remains opportune, so as to make that pause shorter and less painful, to agree on a vigorous effort to master inflation, an essential prior condition for an employment-support policy. In parallel, specific labour-market action should be developed.

In relation to these points of reference, the following recent trends, or policy developments, may be observed.

The risks are increasing that the growth rate for 1980 may be lower than 2 %. The production expectations of industrialists have begun to weaken in some countries where they have until recently been strong (Germany), and have deteriorated very substantially in some others (UK, Ireland). Further oil price rises are now threatened again, which may well go beyond the technical assumptions underlying the Commission's October forecasts.

Prices are continuing to rise at an average monthly rate close to 1 %, latest indices confirming the divergent development of consumer prices (+0.1 % in Germany, +2.6 % in Italy in September). Both for Italy and the United Kingdom the Commission expects that it will have to revise upwards its price forecasts for 1980.

Trends in income bargaining show a mixed performance in relation to the recommended policy of not making income increases to compensate for the oil price rise. In quite a number of countries the rise in the price of oil seems to have been effectively borne by consumers without a secondary spill-over into incomes. But this is not the case in some other countries : the indexation of public sector salaries has just been made more fast-acting in Italy, and settlements in the United Kingdom are being made across a very wide range of percentage increases.

In public finance policy most countries are pursuing the cautious line portrayed by the data in Table 1. In some countries, notably Denmark and Belgium whose currencies have been "divergent" in the European Monetary

System, measures are being prepared which should lower the deficits for 1980 by comparison with those indicated in the Table. In Italy, however, the budgetary policy foreseen for 1980 seems, despite inflationary pressures and the size of the public deficit as a share of GDP, to be expansionary rather than restrictive.

A general rise has since been seen in interest rates. This development is worrying. On the one hand, in a situation where the business climate has started to deteriorate, it is important to maintain, to the greatest possible degree, the confidence of economic agents; on the other hand, the rise in interest rates follows unavoidably from a reinforced control of the money supply, designed to choke off inflation. A satisfactory compromise between these two imperatives must be reached. Further progress in the co-ordination of monetary policies within the Community, particularly policies for the control of monetary aggregates and interest rates, could contribute to the achievement of this aim.

To ensure a convergence of economic performances within the Community, and to realise the adjustments of policy that are, or may become necessary to attain the objectives mentioned to maintain the stability of the European Monetary System, the Commission suggests the following policy attitude :

- . to strengthen coordination of member countries' economic and monetary policies; such strengthening, notably in the area of interest-rate policies, would in addition make it easier for the Member States to pursue a common attitude with regard to the dollar;
- . to consolidate the first successes which are being registered in policies to control money supply and unduly large public deficits;
- . to avoid the danger that some countries diverge substantially from the desirable trend. Given the damaging consequences for economic prospects for the whole Community and for the stability of the European Monetary System which could result from such a divergence, this risk must be taken into account by all the member countries together.

Table 1 Main economic aggregates 1978-80

	GDP volume (percentage increase)			GDP prices (percentage increase)		
	1978	1979	1980	1978	1979	1980
DK	0,9	1,8	3/4	9,7	8,0	9
D	3,2	4,3	3	3,9	3,9	4 1/4
F	3,3	2,9	2 1/4	9,9	9,6	8 3/4
IRL	6,1	2,8	3	11,3	12,1	13
I	2,6	4,3	2 1/4	13,3	14,3	14 3/4
NL	2,4	2,6	2 1/4	5,3	4,3	7
B	2,5	3,0	2 1/2	4,6	4,2	6 3/4
L	3,2	2,5	2	3,2	5,4	6 1/2
UK	3,7	0,3	-1	10,2	13,8	15 1/2
EC	3,1	3,1	2	7,8	8,3	9

	Balance of payments, current accounts (EUA 'COO mill)			Unemployment rate (percentage of civilian working population)		
	1978	1979	1980	1978	1979	1980
DK	-1,2	-1,8	-2,0	6,6	5,8	6,1
D	7,4	-0,9	-3,1	3,9	3,4	3,4
F	2,9	0,3	-0,8	5,0	5,9	6,8
IRL	-0,2	-0,9	-1,0	8,7	7,9	7,8
I	4,9	3,5	3,5	7,1	7,7	8,4
NL	-0,7	-0,3	0	4,2	4,3	4,3
B	-1,2	-1,4	-1,9	8,3	8,7	8,8
L	0,5	0,5	0,6	0,8	0,8	0,9
UK	1,6	-2,3	-0,4	5,7	5,6	6,6
EC	14,0	-3,3	-5,2	5,5	5,6	6,2

	Public finance, general government net borrowing (1) (percentages of GDP)			Money supply (3) (percentage change)		
	1978	1979	1980	1978	1979	1980
DK	-0,5	-1,0	-2,0	6,7	9,0	8 1/2
D	-2,7	-3,1	-2,8	11,0	7,0	6 1/2
F	-2,3	-1,7	-1,7	12,3	12,5	11
IRL (2)	-10,8	-15,8	-7,3	28,7	21,0	16
I	-10,6	-11,5	-11,4	22,8	17,8	16 1/2
NL	-2,0	-2,3	-2,0	4,2	8,1	8 3/4
B	-6,3	-7,2	-7,4	9,5	9,1	10 3/4
L	+2,8	+1,8	+1,0	13,7	12,5	11 1/2
UK	-3,9	-3,1	-2,4	13,7	12,5	11 1/2
EC	-4,0	-4,0	-3,9	12,7	10,9	10 1/2

Source : Commission, Annual Economic Review 1979/80 (COM(79)568 final),
18th October 1979

- (1) national accounts definitions, excluding loans and participations
(2) 1979 and 1980 figures reflect distortions in government financial transactions
due to the 1979 postal strike
(3) M2 for DK, F, I, NL, B/L; M3 for D, IRL, UK