

COMMISSION OF THE EUROPEAN COMMUNITIES

COM(80) 300 final

Brussels, 29 May 1980

THE ECONOMIC AND SOCIAL SITUATION IN THE COMMUNITY

(Communication from the Commission to the European Council)

COM(80) 300 final

1. Results for 1979 and recent trends. Following a fairly buoyant expansion throughout 1979 the economic activity of the Community showed a more hesitant development in the first half of 1980. Industrial production stagnated between the fourth quarter of 1979 and the first quarter of 1980 and the rate of unemployment rose by three decimal points from January to April, after quasi-stability since the middle of 1978. The rate of increase of consumer prices has been very high in recent months in response to the direct and indirect effect of the oil price adjustments and rise of indirect taxes in some Member States. The inflation momentum is now of the same order of magnitude as in 1974/75. The upward movement of hourly earnings has on the other hand been more modest and the profit situation and cash flows of the enterprises have deteriorated less than after the previous oil price increase.

2. As a result mainly, but not only, of the deterioration of the terms of trade following the oil price increase, the trade balance of the Community has deteriorated considerably since 1978. The deficit on the current account of the balance of payments reached approximately 7 mrd. ECU (10 mrd. dollars) in the first quarter of 1980 against a small surplus in the first quarter of 1979. The current deficit was to some extent financed through a reduction of official reserves, related to interventions in favour of European currencies against the dollar in the period up to the beginning of April. As a consequence of the fall in exchange reserves and a restrictive stance of monetary policy in some Member States the growth in money supply (measured over 12 months) has slowed down from more than 12 % in early 1979 to around 11 % in recent months.

3. Due not least to a forceful monetary policy in the framework of the European Monetary System, exchange rate movements have shown a high degree of convergence over the past year. But underlying rates of inflation and real economic performances have not yet shown signs of yielding to the policy constraints and are showing divergent movements which may become sources of balance of payments disequilibria and exchange rate tensions in later phases.

4. Outlook for 1980 and 1981. Based on the main assumption of no major changes in the stance of budgetary and monetary policies, of a stabilization of the savings ratio of households after a fall in the second half of 1979 and early 1980 and of a sustained growth of export markets (imports to non-EC markets, weighted with their share in Community exports are forecast to increase by 5% in 1980 and expand well also in 1981) real gross domestic product of the Community is expected to rise by 1.5% in 1980 (or slightly more than the 1.2% forecast in February). This would be consistent with a slight decline in the second and third quarters of 1980 followed by a gradual pick-up in the following year. By the end of 1981 the rate of expansion could (at annual rate) be around 2.5%. Inventory adjustments are expected to exert a negative influence on activity, notably in the second half of 1980, and other domestic components may show only little buoyancy. Net exports of the Community may, on the other hand, increase strongly in volume terms and should therefore help to sustain activity somewhat in face of weak domestic demand in most of 1980. However, domestic consumption is forecast to strengthen again in 1981, on the assumption that inflation moderates.

5. With economic activity in the first quarter of 1980 more buoyant than expected, unemployment is now forecast to reach 6% on average for the year (against 6.4% in the February forecast); but a strong increase is likely in 1981. The rise in consumer prices in recent months has been faster than foreseen and may on average for 1980 reach 12.3%. The month-to-month increase would be decelerating as from mid-1980 and should - if the rise in wage costs is checked - get back into single figures in the course of 1981. The deficit on the current account of the balance of payments may, for 1980 on average, reach 24 000 million ECU (33 000 million dollars) but should decline somewhat in 1981.

6. The outlook as presented here may be said to constitute the most probable outcome on the assumptions stated above. The growth of activity and employment could however prove to be slower or even negative if households, enterprises or the government sector - in order to avoid a deterioration of their financial position - increase expenditure less than foreseen. There is also a risk that more divergent movements of prices and wages, and in policy reactions by governments to the strains of the economic situation, could lead to graver instability in both the real economy and monetary relations; and thence also to a lower overall level of activity.

7. Policy issues for the period ahead. Against this background, there is, in the view of the Commission no alternative to maintaining broadly restrictive budgetary and monetary policies. Only through a marked and sustained deceleration of inflation will it be possible to strengthen confidence of households and enterprises and increase the propensity to invest. Without relaxing the overall policy stance, governments should contribute to this process through measures to facilitate necessary changes following the energy price rise, to economise energy and stimulate investment in general and assist the adaptation of the labour force to the changing pattern of supply and demand. Efforts to limit the growth of other public expenditure categories must be pursued. A reduction of the budget deficit in proportion to GDP must indeed be a key medium-term objective for the Community as a whole - and the restoration of better financial balance should remain an immediate pre-occupation in Member States where budget and/or balance of payments deficits are creating particular problems: Belgium, Denmark, Ireland and Italy.

8. While pursuing policies geared to medium-term objectives, governments should, however, over the next 12-18 months, be careful to avoid creating conditions conducive to a cumulative collapse of demand due to excessive expenditure cuts aimed at keeping budget deficits on predetermined levels. As a consequence of a slow growth of tax receipts some increase in budget deficits is likely in the period up to mid-1981 and, on average in the Community, governments should accept this in some moderate degree.

9. With appropriate recycling of OPEC surpluses, including active efforts, on the part of governments to step up long-term borrowing from the OPEC countries directly or via the international capital market, the present orientation of monetary policy could be maintained and domestic monetary financing kept under control. While it would not be practicable to seek to negotiate among oil-importing countries a scheme for distribution of the current account deficits it is highly desirable to arrive at a certain consensus on the approach to the financial problems involved so as to avoid disruptively competitive or divergent policy responses.

10. Given that on one hand total employment is likely to decline in 1981 and that the labour force may see a further increase, the Community will over the coming year be faced with increasing employment problems, notably for young people entering into the labour force; also the employment opportunities for the steadily rising part of the female population which is aiming at an active participation in economic and social life will be severely limited. Moreover, in a context of slow overall growth the difficulties encountered by some low-growth branches of the Community's industry may be seriously aggravated. In this context Member States should prepare themselves to step up efforts to improve employment opportunities in particular for young people.

Table : The Community economy 1978-80

	1978	1979	1980		1978	1979	1980
	GDP volume, % change				private consumption deflator, % change		
DK	1,0	3,5	- 0,8		9,4	9,6	11,5
D	3,2	4,4	2,5		2,5	4,1	5,5
F	3,8	3,2	2,2		8,1	10,5	13,2
IRL	6,0	3,2	0,9		7,9	13,2	19,5
I	2,6	5,0	3,5		12,7	14,9	19,6
NL	2,4	2,2	0,7		4,2	4,7	6,5
B	2,4	2,5	1,4		4,4	4,5	7,0
L	4,3	2,7	1,9		3,5	4,5	6,7
UK	3,1	0,6	- 2,6		8,6	12,0	20,3
EC	3,1	3,3	1,5		7,1	9,0	12,3
	unemployment rate, % civilian working population				balance of payments current account, mrd ECU		
DK	6,6	5,3	5,7	-	1,2	- 2,2	- 2,1
D	3,9	3,4	3,3	-	7,4	- 3,5	- 10,5
F	5,3	5,9	6,3	-	1,5	1,1	- 3,4
IRL	8,8	7,9	8,2	-	0,2	- 1,1	- 1,2
I	7,1	7,6	8,2	-	4,9	3,8	- 1,4
NL	4,1	4,3	4,5	-	0,7	- 1,5	- 0,6
B	8,4	8,6	9,0	-	1,1	- 2,6	- 4,0
L	0,8	0,7	0,8	-	0,3	0,6	0,6
UK	5,7	5,4	6,5	-	0,6	- 3,8	- 1,0
EC	5,5	5,6	6,0		11,7	- 9,1	- 23,7
	public finance : general government deficit, % of GDP				money supply, % change		
DK	- 0,9	- 1,0	- 1,5	(M2)	6,7	9,9	6,0
D	- 2,8	- 2,9	- 2,8	(M3)	11,0	6,0	6,0
F	- 2,3	- 0,8	- 1,5	(M2)	12,2	14,3	12,5
IRL	- 10,5	- 12,5	- 11,4	(M3)	28,7	19,0	12,6
I	- 10,6	- 9,4	- 10,2	(M2)	22,8	20,4	19,2
NL	- 2,2	- 3,3	- 2,8	(M2)	4,2	6,9	8,4
B	- 6,0	- 6,8	- 7,9	(M2M)	9,5	6,0	7,0
L	3,3	1,3	0,4	:	:	:	:
UK	- 4,2	- 2,9	- 2,4	M3	13,3	11,7	9,6 (1)
EC	- 4,0	- 3,5	- 3,8		12,7	11,0	10,1

(1) Financial year, mid-April to mid-April.

Source : Commission services, based on information available up to 27th May 1980.