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Annual Economic Report 1983-84

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No 18 November 1983

'EUROPEAN ECONOMY' appears four times a year, in March, July, September and November. The November issue contains the Commission's proposal for the annual report on the economic situation in the Community. This report, which the Council adopts in the fourth quarter of each year, establishes the economic policy guidelines to be followed by the Member States in the year that follows. The November issue also contains the Commission's annual economic review, the background analysis to the proposed annual report. In March and July of each year, 'European Economy' gives a review of the current economic situation in the Community, together with reports and studies on problems of current interest for economic policy. The September issue presents a report on the Community's borrowing and lending activities in the preceding year.

Three series of supplements accompany the main periodical:

— Series A — 'Economic trends' appears monthly except in August and describes with the aid of tables and graphs the most recent trends of industrial production, consumer prices, unemployment, the balance of trade, exchange rates, and other indicators. This Supplement also presents the Commission staff's macroeconomic forecasts and Commission communications to the Council on economic policy.

— Series B — 'Business survey results' gives the main results (orders, stocks, production outlook, etc.) of opinion surveys of industrial chief executives in the Community, and other business cycle indicators. It also appears monthly, with the exception of August.

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Commission of the European Communities

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Abbreviations and symbols used

Countries

B	Belgium
DK	Denmark
D	Federal Republic of Germany
GR	Greece
F	France
IRL	Ireland
I	Italy
L	Luxembourg
NL	The Netherlands
UK	United Kingdom
EC	Total of the Member States of the European Community
EC 4	Federal Republic of Germany, France, Italy, United Kingdom
EC 9	Community without Greece
BLEU	Belgo-Luxembourg Economic Union

Currencies

BFR	Belgian franc
DKR	Danish krone
DM	German mark
DR	Greek drachma
FF	French franc
IRL	Irish pound (punt)
LIT	Italian lira
LFR	Luxembourg franc
HFL	Dutch guilder
UKL	Pound sterling
ECU	European currency unit
USD	US dollar
SFR	Swiss franc
SDR	Special drawing right

Other abbreviations, etc.

cif	Carriage, insurance and freight
EAGGF	European Agricultural Guidance and Guarantee Fund
EIB	European Investment Bank
EMCF	European Monetary Cooperation Fund
EMF	European Monetary Fund
EMS	European Monetary System
ESA	European System of Integrated Economic Accounts
Euratom	European Atomic Energy Community
Eurostat	Statistical Office of the European Communities
fob	Free on board (valuation basis for exports or imports of goods)
GDP (GNP)	Gross domestic (national) product
GFCF	Gross fixed capital formation
IMF	International Monetary Fund
LDC	Less-developed country
MTFA	Medium-term financial assistance
OECD	Organization for Economic Cooperation and Development
OPEC	Organization of Petroleum Exporting Countries
SOEC	Statistical Office of the European Communities
STMS	Short-term monetary support
VSTF	Very short-term financing mechanism

( )	Estimate
:	Data not available
s.a.	Seasonally adjusted
,	Decimal point
—	Not applicable

Annual Economic Report 1983-84

(Communication from the Commission to the Council)

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Part I — The Community economy

1. Introduction: the central issue

The present *Annual Economic Report* for 1983-84 is submitted to the Community institutions in accordance with established procedures. [1]

The present short-term forecasts indicate only a hesitant and patchy recovery. The recession of three years, 1980 to 1982, was exceptionally long and damaging to the employment situation. These developments follow a whole decade of failure to achieve any substantial growth in employment alongside the rapid growth of population of working age. This report is therefore addressed to the central issue of economic policy now facing the Community: how to devise policies that will foster a stronger and durable recovery in the growth of production and employment in the European economy.

These questions have been highlighted by requests made in the conclusions of the European Council at Stuttgart on 17-19 June 1983. The European Council requested the Commission:

(i) 'to prepare a detailed analysis of the nature and extent of the recovery and what the authorities are already doing to support, consolidate and accelerate it';

(ii) 'to make full use of Community financial instruments in a coordinated manner to sustain and consolidate the economic recovery';

(iii) 'on this basis, to indicate what new factors the Member States and the Community can bring forward to underpin the recovery, as and when necessary'.

The European Parliament for its part decided at the end of 1982 to engage work on the conditions for recovery of the European economy. It has subsequently decided to conduct a debate on this early in 1984, preceded by a phase of consultations.

These various initiatives in effect concern the same central complex of economic problems. In responding to the mandate of the European Council, the present report sets out the conclusions that the Commission draws regarding the lines of action that seem appropriate for the period ahead.

[1] The Commission's proposed *Annual Economic Report* is submitted to the Community institutions in accordance with the Council's 1974 Decision for attainment of a high degree of convergence of economic policies of Member States (Article 4 of Decision 74/120/EEC of 18 February 1974, amended by Decision 75/787/EEC of 18 December 1975). The Council is required in the fourth quarter of each year—on proposal of the Commission and after consulting Parliament and the Economic and Social Committee—to adopt an annual report on the economic situation in the Community and to set economic policy guidelines to be followed by each Member State.
As in previous years the Commission is preparing, as a separate background document, an *Annual Economic Review* which contains a more detailed factual analysis of economic trends and the outlook for the year ahead. This second document is for the information of the Council, Parliament and Economic and Social Committee.

Table 1

The European Community economy, main economic aggregates 1961-84

	GDP nominal increase	GDP volume growth	GDP price increase	Consumer price increase	Compensation per employee	Current account of balance of payments	General government net lending or borrowing	Money supply growth	Unemployment rate
	% [4]	% [4]	% [4]	% [4]	% [4]	% GDP	% GDP	% [4, 5]	%
1961-70	9,1	4,7	4,3	3,8	8,9	0,4	−0,4	10,4	2,1
1971-80	13,0	2,9	9,8	9,7	13,3	−0,1	−2,8	13,8	4,2
1981	8,7	−0,4	9,1	10,1	12,1	−0,6	−5,2	10,8	7,8
1982	9,5	0,4	9,1	8;7	9,6	−0,6	−5,2	10,7	9,5
1983 Last report [1]	(7,5)	1,1	(7,0)	(6,6)	(7,4)	−0,4	−4,9	10,0	10,3
1983 This report [2]	6,9	0,5	6,3	6,3	7,2	−0,2	−5,4	10,1	10,4
1984 [3]	6,6	1,5	4,9	5,6	6,0	0,0	−4,7	7,8	10,9

1 Of October 1982. Figures in brackets from the last annual report are revised as a result of change in statistical weighting methods.
2 Estimates of the Commission services, October 1983.
3 Forecast of the Commission services, October 1983, on the basis of present or anticipated policies.
4 EC averages calculated with current GDP weights at purchasing power parities.
5 End of period (annual growth rates).

2. The nature and extent of the recovery in progress

The following sections set out an assessment of the extent of the recovery now taking place, and the risks surrounding the outlook; on the extent to which the problems of unemployment, inflation and the balance of payments are being corrected; and finally, on the extent to which the underlying performance of the European economy seems to be changing.

2.1 A hesitant European recovery in a turbulent international setting

The recession, for the Community as a whole, probably ended around the end of 1982. The recovery which is taking shape (Graph 1) offers the possibility of a progressive improvement in the economic situation. However, interpretation of the movement in progress, which in any case differs among the Member States, should not be exaggeratedly optimistic. It remains slow, and fragile in all respects, particularly because of a series of risks relating, as described in the report, to the international environment. In the EC the total volume of output (GDP) remained stable in the second quarter of 1983 after rising at an annual rate of around 2% in the previous two quarters, but the level of industrial production in the second quarter of 1983 was still lower than in the third quarter of 1982; in the United States, by contrast, industrial production has grown strongly (Graph 2). At all events, it is a characteristic of the present economic cycle that neither the recession nor the recovery phase has been particularly pronounced in Europe.

(% increase at seasonally adjusted annual rates)

	1982 whole year	1982 Q. 4	1983 Q. 1	1983 Q. 2
Gross domestic product				
EC	0,4	2,3	2,1	−0,2[1]
US	−2,2	−1,3	2,6	9,2
Industrial production				
EC	−1,4	−6,6	2,8	2,8
US	−8,5	−9,3	12,1	20,2

[1] Figures for individual quarters are often erratic, and the early results are subject to revision. In the second quarter of 1983 there was a strong rise of output in Germany, offset by drops in Italy and the UK. However in the UK case alternative official estimates indicate stability in this quarter.

In its composition, the recent growth in Europe has been essentially due to a pick-up in private consumption, stockbuilding and house-building. This has been helped by the decline in inflation directly, as well as indirectly through lower nominal interest rates. It will be recalled that around the beginning of 1982 there were also signs of a modest recovery. But these were sharply reversed by a collapse in world export demand, whose proximate cause lay in international debt and monetary problems.

Table 2

Forecast evolution of gross domestic product in 1983 and 1984

(% change)

	1983	1983			1984		
	Nominal GDP (previous report)	Nominal GDP	GDP outut volume	GDP price deflator	Nominal GDP	GDP output volume	GDP price deflator
B	7,9	6,2	−0,9	7,1	7,0	0,6	6,3
DK	8,6	9,8	2,2	7,4	6,5	1,2	5,2
D	4,7	3,8	0,7	3,1	5,1	2,1	3,0
GR	23,0	19,5	−0,2	19,7	19,7	1,5	17,9
F	10,8	9,5	−0,3	9,8	7,7	0,4	7,3
IRL	15,5	11,2	0,5	10,6	10,1	1,8	8,2
I	16,9	14,1	−0,8	15,1	12,0	1,5	10,4
L	8,8	5,6	−2,4	8,2	6,3	−1,0	7,4
NL	3,3	1,9	0,3	1,6	2,4	0,0	2,4
UK	8,2	7,9	2,8	4,9	7,2	2,2	4,8
EC	(7.5)	6,9	0,5	6,3	6,6	1,5	5,1

Source: Commission services.

The experience of previous cycles suggests that in a second phase investment and exports should become the engines of the recovery process. For this to happen it is important that there should be a decline in interest rates—which would help not only the growth of private investment within Europe but also a steady recovery in world trade through an easing of debt service burdens.

The distribution of the European recovery by country is quite uneven. The main growth is forecast in the UK and Germany. In some countries the recovery will be retarded for reasons of necessary policy adjustment.

Looking ahead, there is a range of indicators which supports the forecast of gradual recovery (Graph 9). Surveys of opinion among consumers, industrialists, and construction enterprises all show widespread improvements. The share price index has in most countries showed striking gains, and this is usually a leading indicator of business prospects.

Revised forecasts by the Commission now suggest that the year-on-year GDP growth rates for the EC as a whole will be 0,5% for 1983 and 1,5% for 1984. Among demand components, in 1984 exports are expected to grow by 3,4%, investment by 2,0%, private consumption by 0,5% and public consumption by −0,1%, whereas stockbuilding is expected to contribute a little to growth. While aggregate growth will be modest, its structural composition should thus be broadly in line with policy objectives.

This slow European recovery contrasts with that of the US. However, while not denying that a major stabilization effort has been made in the US and that its economy possesses genuine advantages of size and flexibility, it should be stressed that the US recovery springs to a considerable extent from a disequilibrium between a budgetary policy with expansionary effects and a monetary policy whose overriding aim, even though it has recently been more accommodating, is to reinforce the slowdown of inflation. The consequences of such a policy in terms of interest rates, the exchange rate and the trade deficit can, in the short term—and so long as their international impact is not taken into account—be more easily borne by a powerful, homogeneous economy benefiting from the advantages conferred by the status of its currency. In the Community, the economic policies of the Member States are subject to narrow margins of manoeuvre which reflect more burdensome constraints, notably constraints emanating from abroad. This situation has two consequences. First, an economic policy analogous to that in the US cannot be adopted in the Community. Second, the effectiveness of European policies is very largely determined by their degree of coordination.

As to the effects of the US recovery on Europe, there are simultaneous and partly offsetting influences through several channels: the stronger direct US demand for imports, but also a more complex set of interest rate, exchange rate and business confidence effects. To give a simple first perspective, total European exports of goods and services to the US amounted in 1982 to around USD 50 000 million or 2% of the EC's GDP. Every 5% increase in these exports would amount to a direct demand impulse of 0,1% of GDP. Taking into account further possible European export gains in third country markets as well as the US, in part as a result of the appreciation of the dollar's exchange rate, the total boost for European exports could—*ceteris paribus*—be twice or three times as great. However there are important factors reducing this expansionary impact. The Japanese yen has remained relatively weak, which means that European competitivity gains overall have been much more limited than the dollar-ECU comparison might suggest. In addition, high world interest rates dampen the capacity of the indebted Third World countries to import, *inter alia* from Europe among others. Finally, financial conditions within Europe are less favourable than they might otherwise have been, as a result of US interest rate conditions and of a larger dollar appreciation *vis-à-vis* the EC. Overall it is hard to say where these offsetting influences net out; it should not be easily presumed that the balance for Europe is positive.

The world trade environment has evidently been depressed over the past three years (with nil or negative growth in 1981 to 1983) as a direct or indirect result of the second oil shock to begin with, and then the large and unpredictable swings in world interest rates and exchange rate conditions. An acceleration of world trade is expected for 1984 (growth could be 3,5%, according to Commission forecasts). The EC may be expected to make some small gains in market share.

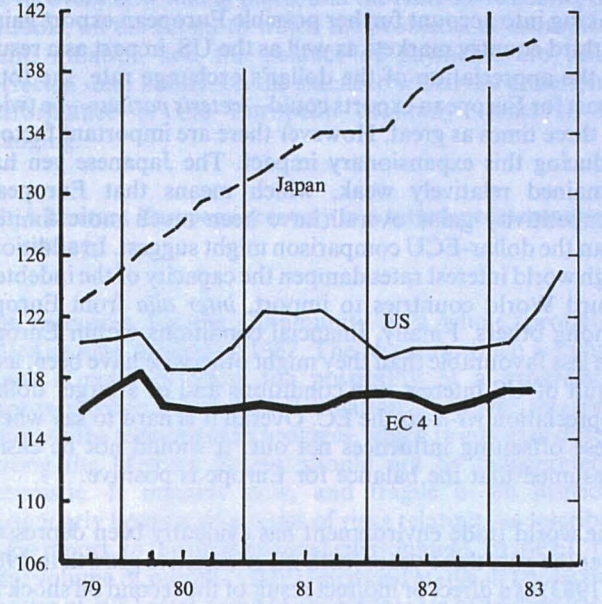
2.2 Stabilization of the unemployment rate?

While a complete analysis cannot yet be made, and caution is therefore called for, it seems that the recovery in activity was accompanied at the beginning of 1983 by a slowdown in the growth of unemployment and even a degree of stabilization. It should not be forgotten in interpreting this development that the forecasts for 1984 show a further slight increase in unemployment. In any case the level of unemployment remains excessive: total unemployment at the end of August stood at 11,7 millions, compared with 10,6 millions at the same time last year.

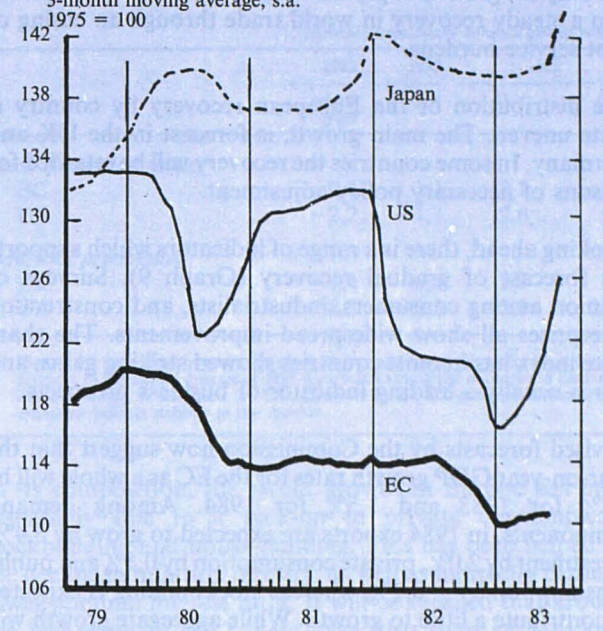
From March to June 1983, the seasonally-adjusted average rate of unemployment in the EC remained stable at the peak level of 10,7%, and the observation for July showed a slight fall to 10,6%, making it the first month to record a fall since July 1979. This level remained unchanged in August. The pattern of a stabilization or slight fall in unemployment since the spring of this year was common to all of the four large Member States, although continuing rises are still evident in most of the other countries and unemployment growth rates over the last 12 months are still positive for all Community

GRAPHS 1 to 4: **Comparative evolution of the EC, US and Japanese economies, 1979-83**

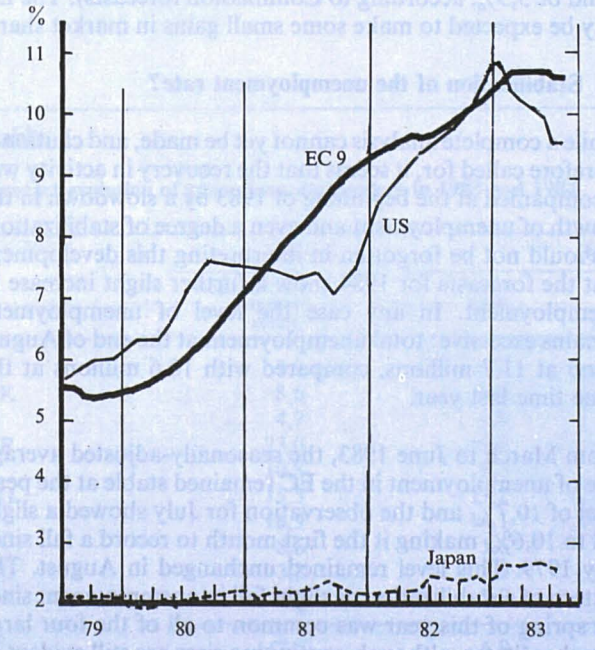
1. **Gross domestic product,** s.a.
1975 = 100



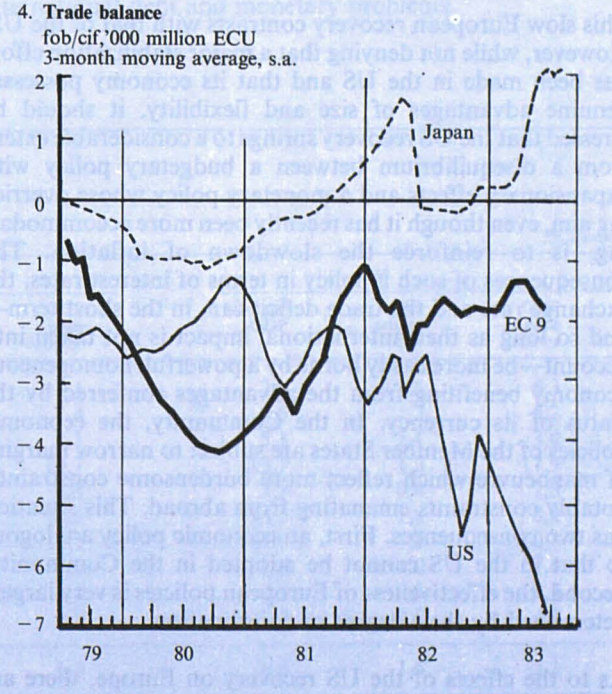
2. **Industrial production**
3-month moving average, s.a.
1975 = 100



3. **Unemployment rate**



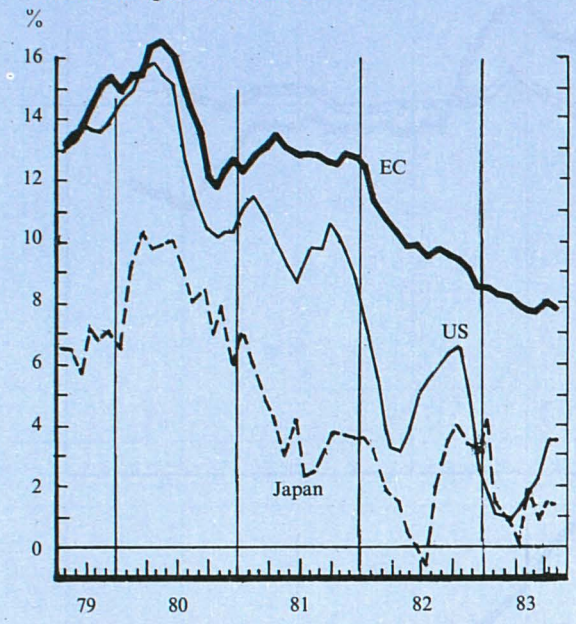
4. **Trade balance**
fob/cif,'000 million ECU
3-month moving average, s.a.



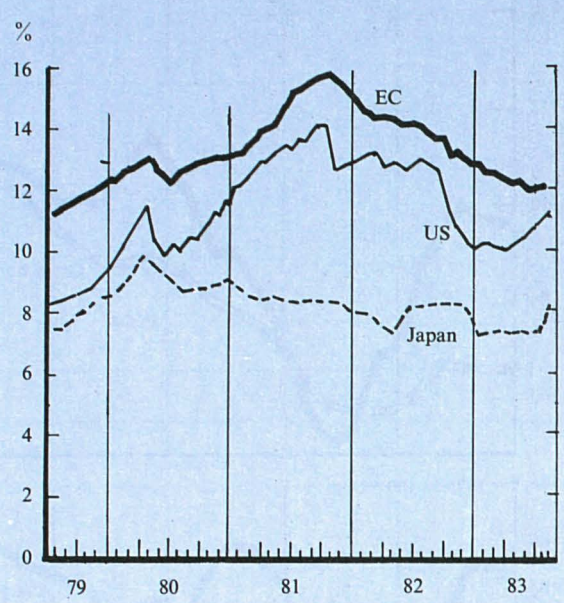
[1] D, F, I, UK.

GRAPHS 5 to 8: **Comparative evolution of the EC, US and Japanese economies, 1979-83**

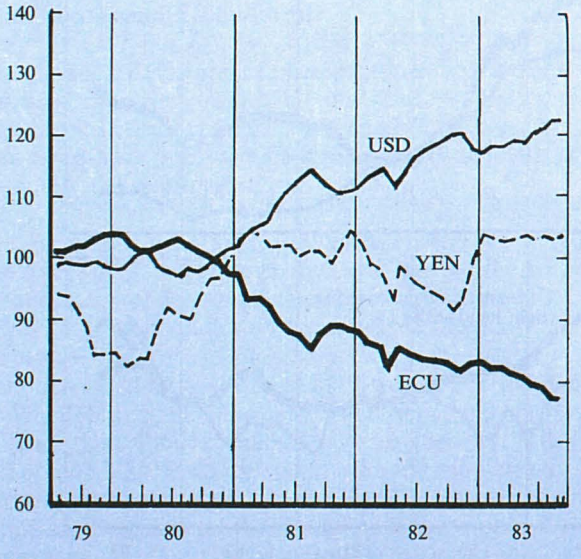
5. **Consumer prices**
6-month change, s.a., annual rates



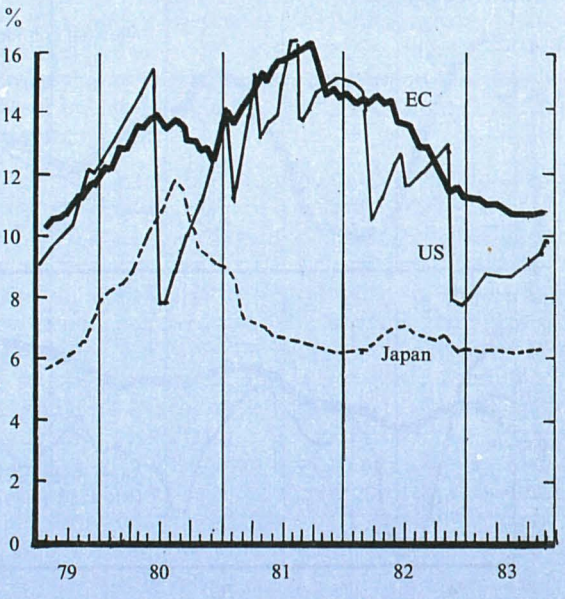
7. **Long-term interest rates**



6. **Exchange rates**
Index of SDRs per currency unit
March 1979 = 100



8. **Short-term interest rates**



GRAPH 9: **Indicators of output and economic sentiment — EC**

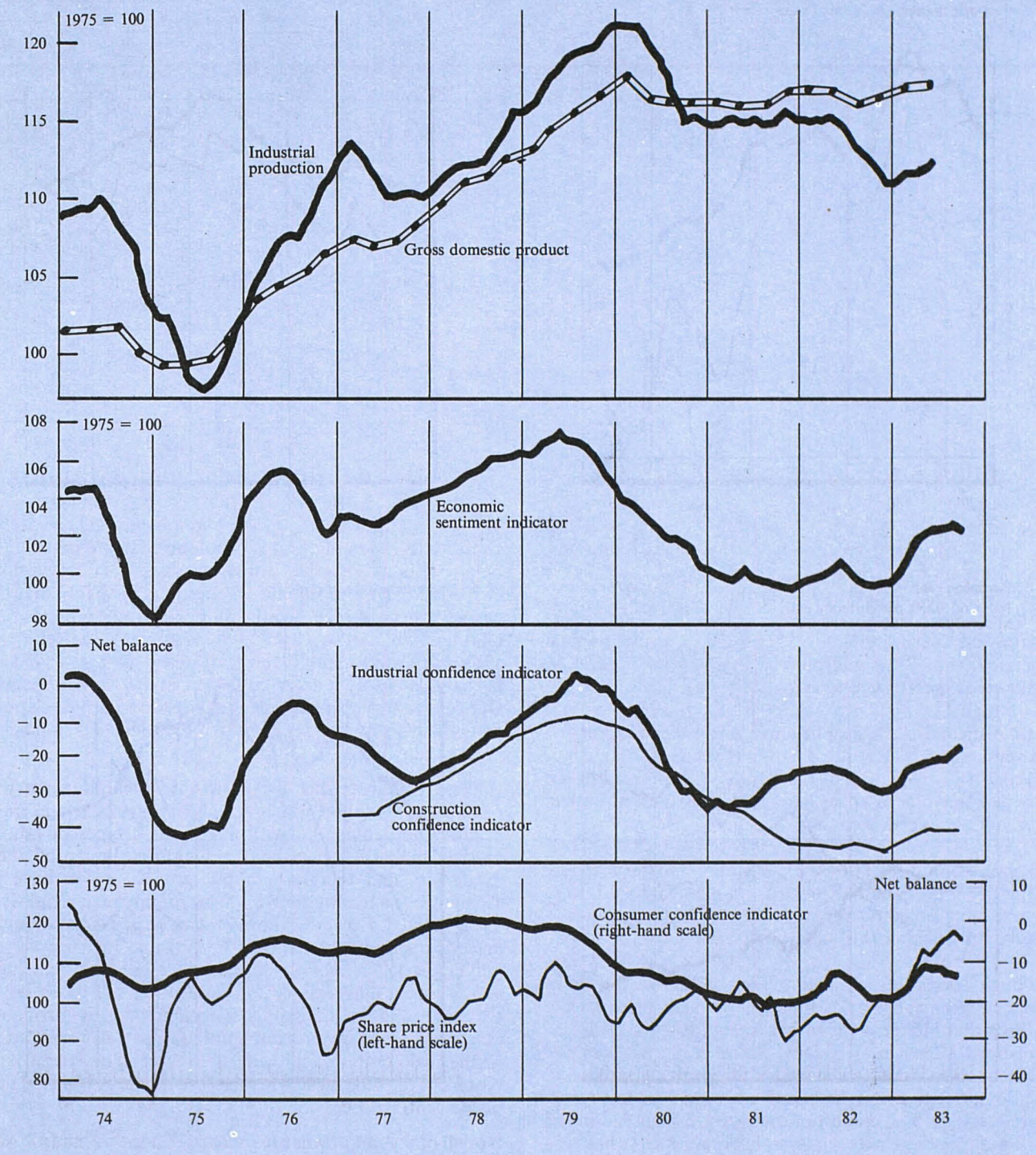


Table 3

Indicators of macroeconomic disequilibria and constraints in 1983

	Unemployment rate	Private consumption deflator % change	Balance of payments current account % of GDP	Real rate of interest, [1] long-term	Public finance		Public debt % of GDP 1982 [2]
					Budget balance % of GDP	Budget balance less interest payments	
B	14,4	7,8	−2,4	3,6	−12,2	−2,9	(97,8)
DK	10,7	6,6	−2,2	7,8	−8,8	−3,9	25,8
D	8,6	3,0	0,9	5,5	−3,3	−0,7	38,3
GR	7,8	20,5	−5,0	−0,6	−6,3	:	:
F	8,9	9,0	−1,8	4,1	−3,1	−1,4	(16,8)
IRL	14,6	11,0	−2,6	3,5	−13,4	−3,3	102,5
I	9,0	15,0	−0,4	2,3	−11,9	−3,5	70,3
L	1,8	8,4	:	:	−2,9	−4,8	:
NL	15,6	2,8	3,3	6,5	−6,7	−3,4	(54,0)
UK	11,7	5,7	0,2	6,7	−2,2	+0,9	54,7
EC	10,4	6,3	−0,2	3,6	−5,4	−1,6	(43,4)

[1] Government bond yield in July 1983 adjusted by consumer price inflation over the preceeding 12 months.
[2] Central government debt for DK, GR, F, IRL, L, NL: general government debt for D, 'settore statale' for I, public sector for B and UK.

countries except France. By comparison, in the United States the rapid cyclical recovery has already reduced the rate of unemployment quite substantially from a peak of 10,7% at the end of 1982 to 9,5% in July of this year.

Coming after three years of continuous sharp rises in unemployment, the significance of these recent developments needs careful assessment.

The statistical definition of unemployment has been revised in several countries (raising the total in the Netherlands but reducing it in Belgium and the United Kingdom), but the time-series have been corrected and so this does not affect materially the recent trend.

The principal questions are whether the very recent stabilization of unemployment is to be attributed to a strengthening of labour demand or a reduction in labour supply, and whether this will now be sustained.

Although a definite assessment of the recent development of labour supply and demand cannot yet be made, there is some evidence that labour demand has strengthened a little: the number of vacancies registered showed increases in the second quarter of this year in the FR of Germany, the United Kingdom, Belgium and the Netherlands, but not in France, where they fell. The modest output growth recorded in the last three quarters may at least have arrested what was previously a slightly declining trend in total employment.

The intensification of special labour market measures concerning, especially, young people and early retirement for older people (see further below) has had an effect on both labour demand and supply. One result is probably that the labour force is now nearly static in size, whereas the population of working age (15-64) is growing by over 1% in 1983. Some direct employment-creation measures have also been taken in a number of countries (again see below). Overall, it seems probable that changes on both the labour demand and supply sides lie behind the recent developments in unemployment.

Forecasts indicate that the growth in unemployment will resume and that there will be a slightly higher yearly-average rate in 1984 compared with 1983. Some types of labour market measures may be reaching the limits of their expansion, and therefore output growth would have to strengthen if a renewed rise in the unemployment trend were to be avoided. However, the evolution of participation rates and productivity trends and the possible reaction of the labour market to real wage adjustments is also a matter of considerable uncertainty. In addition, the process of reducing and reorganizing working time is probably accelerating, and given certain prerequisites (also referred to further below) this could help ease the unemployment rate. Not all of the unknowns are therefore on the pessimistic side of the central forecast.

Not all of the unknowns are therefore on the pessimistic side of the central forecast.

2.3 A gradual convergence on slower inflation

Considerable, but far from complete, progress has been made in reducing inflation in the period since the second oil-price shock in 1979-80. In 1980 the EC average consumer price rise was similar to that of the US, being in the region of 14%. By August 1983 the 12-month rate of increase had declined to 8,2% in the EC but to 2,6% in the US. In recent months there have been signs that in both the US and the EC the deceleration in inflation may have progressively been tending to ease off.

Consumer price increases, %

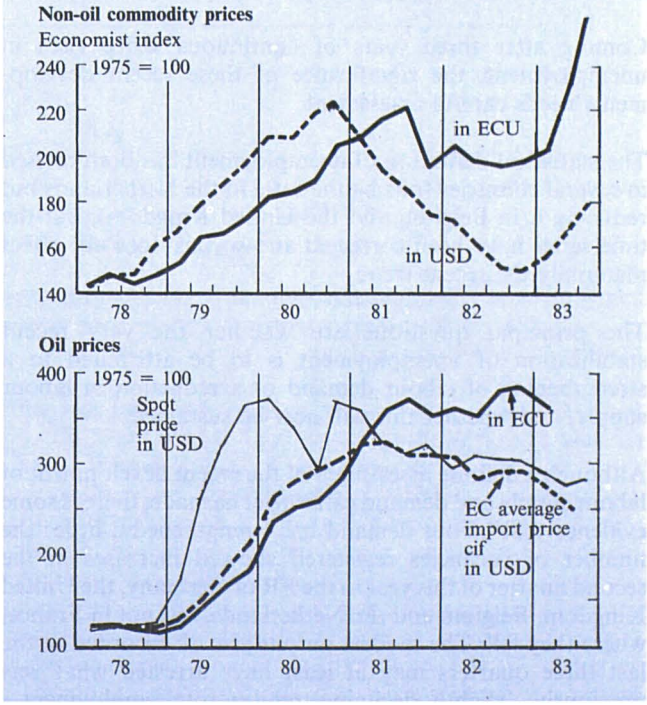
	1980	1981	1982	12 months to August 1983
B	6,6	7,6	8,7	7,9
DK	12,3	11,7	10,1	6,1
D	5,5	5,9	5,3	3,0
GR	24,9	24,5	21,0	20,0
F	13,6	13,4	12,0	9,6
IRL	18,2	20,4	17,2	10,
I	21,2	19,5	16,4	13,6
L	6,3	8,1	9,4	8,3
NL	7,0	6,8	6,0	2,7
UK	18,0	11,9	8,6	4,5
EC (10)	14,3	12,8	10,9	8,2
US	13,5	10,3	6,2	2,6

Decomposing the total 7 percentage points deceleration of inflation (measured by the total expenditure deflator) within the EC from 1980 to 1983, slower import price rises accounted for 2,5 points, unit labour costs 4 points and indirect taxes 0,5 points. While slower unit labour cost increases thus helped on average to reduce the inflation rate substantially, there were notable differences as between countries in the extent of the real wage adjustment in response to the second oil shock. Taking 1981 and 1982 together some real wage cuts occurred in several countries: Belgium, Denmark, Germany, Ireland, Luxembourg and the Netherlands. However, in France, Italy, Greece and the United Kingdom real wages continued to grow.

As regards the problem of divergent inflation rates, the figures above for the four larger countries show some progress in that the deceleration has (in percentage points) been greater in the countries which had double-digit rates of inflation in 1980. By mid-1983 the reduction in inflation had been 3 points in Germany, 4 points in France, 6 points in Italy, and 14 points in the United Kingdom. Indeed, by mid-1983 no EC countries except Italy and Greece any longer had double-digit inflation. In 1982 Denmark, France and Ireland were in double digits and in 1981 this was also true of the United Kingdom.

With the cycles of world inflation at times strongly influenced by world commodity prices, it is to be noted that the low-point in the weakening of commodity prices in 1981 and 1982 has now passed. For non-oil commodities there was a clear break in trend around the end of 1982 as world prices for agricultural and mineral commodities turned sharply up (18% in dollar terms, 34% in ECU terms in the first nine months of 1983). However this upward movement has been halted in recent weeks. The impact on costs and prices within the EC is reduced for agricultural commodities covered by the CAP, but is immediately felt for such commodities as rubber or aluminium. For the time being the positive aspects of these price adjustments must be recognized: they improve the terms of trade of many heavily indebted developing countries and are a condition for expansion of capacity in a number of cases.

GRAPH 10: **Commodity prices**



The average price for oil imported into the EC did decline in dollars from USD 33,7 per barrel in the fourth quarter of 1982 to USD 29,4 in the second quarter of 1983, following the cut in OPEC's marker price to USD 29 on 14 March 1983. Spare production capacity in OPEC countries should ensure a period of approximate dollar price stability through to 1984. However the price of oil in ECU has hardly declined at all from its mid-1981 peak level, and with the further recent appreciation of the dollar the ECU price probably rose again in the third quarter of 1983.

As noted in the table above, the deceleration of inflation has on average in Europe been considerably slower than in the United States. A large part of this difference may be identified in the 40% appreciation of the dollar against the ECU in the three years from mid-1981 to mid-1983. To the extent that at least the more recent rises of the dollar are deemed to be 'overshooting', then world inflation has been temporarily redistributed to the disadvantage of Europe and other countries with depreciating currencies. It is hazardous to quantify by how much there would have been a relatively better European price stabilization performance with less exchange rate movement. However, if for example the ECU had depreciated by 15% less against the dollar, certain estimates suggest that the difference between the deceleration in inflation noted above from 1980 to mid-1983 as between the EC and US might have been more than halved. At some stage in the future when the dollar/ECU exchange rate reverses somewhat, it is likely that the current European stabilization effort will be more amply rewarded, if it continues to be pursued with determination.

2.4 Rapid balance of payments adjustments within Europe, but problems internationally

Within the European Community the pattern of balance of payments evolutions in the recent past has been a mix of several processes: the general adjustment to the second oil shock, correction in some cases of large, twin deficits in the budget as well as the balance of payments current account (e.g. Denmark, Ireland, and Belgium), and correction in some cases of problems due to the marked desynchronization of business cycles (e.g. in France).

Overall, this complex adjustment process is proceeding reasonably well, both as regards the situation of the EC in the world, which is in moderate and declining deficit on current account, and as regards the situation of individual Member States. Several EC countries which have been in serious current account deficit have in recent months been reporting much better trading results. In January of this year Denmark and Belgium reported their first month of visible trading surplus for many years. For Ireland and France, also, a much improved foreign trade performance is emerging, whereas the results for Germany and the United Kingdom have recently weakened. In the deficit countries the trade accounts have responded quite promptly to corrective measures including restraints on internal demand. Visible trade balances of course give only an incomplete picture, and rising debt service burdens in deficit countries require an improving trade account before the current begins to improve. However, current account deficits are also being reduced, and Commission forecasts for 1984 suggest that in Belgium, Denmark and France their size as a share of GDP will be cut by two-thirds or more compared to 1982. For Ireland and Italy the reduction is even more marked, but for Greece an improving trend is not yet evident.

Major changes in the distribution of current account balances at the world level are taking place:

Balance of payments current accounts

(USD '000 million) [1]

	1980	1982	1983
EC	−37	−14	−4
US	0	−11	−30
Japan	−11	+7	+18
OPEC	+111	−4	−22
Other developing countries	−76	−65	−47

[1] The world balance, in theory equal to zero, differs from zero because of statistical discrepancies (non-recording of certain credits).

Compared to the extreme 1980 situation, by 1982 the industrialized and oil-exporting countries had, on the whole, completed the adjustment to the second oil-price shock. However the developing countries had delayed their adjustment, and were also caught heavily exposed to the rise in world interest rates. By 1982 their current account position was still as unfavourable as in 1980. A rapid adjustment is now taking place; for example, Mexico reduced its imports by 60% over the last 12 months.

Among the industrialized countries there remain the problems of the worsening current account deficit of the United States and surplus of Japan.

For the Community a particular concern is that the US-Japanese disequilibria are not yet being met by plausible exchange rate movements (a weaker dollar and stronger yen), Such movements would reduce protectionist pressures world-wide, and greatly ease problems of macroeconomic policy in Europe. The EC's average competitiveness index improved by about a fifth from 1980 to 1982, whereas that of the United States deteriorated more than a quarter; however that of Japan changed much less.

Trade-weighted competitiveness index

(1970-75 average = 100)

	1980	1982	1983 (estimated)
EC	124	100	100
US	80	104	104
Japan	92	89	97

It is to be noted that these figures are significant for their evolution over time, rather than the relative levels of the index in a particular year, and the yen in particular is generally considered to be undervalued.

2.5 Insufficient signs of structural improvement

With cyclical trends gradually turning in more favourable directions, there remains the important question of whether the European economy is now on a course of more fundamental structural improvement. This notably concerns the problems of increasing the medium-run propensity to invest and employ, as well as performance in certain crucial branches of the economy such as energy and advanced technology industries, and services.

As long as both employment and investment are stagnant, as they are on average in the EC, the assessment must at best be cautious. Surveys of industrial investment intentions for the present year support this view. Between 1975 and 1982, the low-points of the two major recent recessions, industrial output grew only by 1% per year in the EC as a whole. Yet capacity utilization was reported by industrialists to be at the same level in both these years (76%), which illustrates how little net addition there has been to the usable capital stock in industry and even hints at a possible reduction when capital productivity increases are taken into account.

Total investment has continued to slide down as a share of GDP, probably reaching 18,6% in 1983, compared to 21,1% in 1980 and also in the 1975 recession year. Investment has become increasingly concentrated in market service sectors, but employment growth in this branch, while positive, has still been much slower than in the United States (1,5% per year in the EC, compared to 3% in the US in the years 1973 to 1981).

In the energy sector there has been considerable progress. Energy demand has fallen sharply, and this is estimated to reflect a sharp responsiveness to price (with an average negative long-term eleasticity in the EC of 0,45) and a lower positive elasticity with respect to output growth than previously thought (0,65 rather than around unity). [1]

[1] For a detailed analysis see 'Energy and the economy: a study of the main economic relationships in the countries of the European Community', *European Economy*, No 16, July 1983.

These economic adjustments can be illustrated by the reductions in *final consumption of oil per unit of GDP* over the period 1973 to 1981 as follows:

(percentages)

B/L	DK	D	F	I	NL	UK	EC 10
−34	−34	−30	−30	−24	−36	−26	−29

This shows a strong adjustment in all countries. However the cost of imported energy, at first in dollars, and then through the dollar's appreciation, has continued to rise, or only just stabilized for European countries. This may be seen in the *net import bill* of Member States in energy products:

('000 million ECU) *(% of GDP)*

	B/L	DK	D	F	I	NL	UK	EC 10	EC 10
1978	3	3	12	11	8	1	4	40	2,5
1980	5	3	25	22	16	2	1	76	3,8
1982	8	3	31	28	24	2	−7	91	3,8

As regards the major industrial technologies the evidence continues to show a lagging performance in Europe. Recent studies by the Commission show the Community's traditionally very strong position in the equipment goods sector to have been deteriorating. The EC's export/import ratio in this sector declined from 3,4 in 1963 to 2,5 in 1973 and to below 2 in 1981. While Japan gained strongly (its ratio rose from 2,2 in 1963 to 9,7 in 1981), the United States appears to have arrested its declining performance (the US ratio fell from 3,9 in 1963 to 1,3 in 1973, but was still at that level in 1981). Germany, the EC's principal producer, has been worst affected. [2]

There have been some examples of striking increases in average labour productivity performance, notably in the United Kingdom, Belgium and Denmark. However this has so far more reflected cuts in employment levels in sectors or enterprises which used to be overmanned, rather than growth in high productivity enterprises. Elsewhere productivity growth has slowed down substantially:

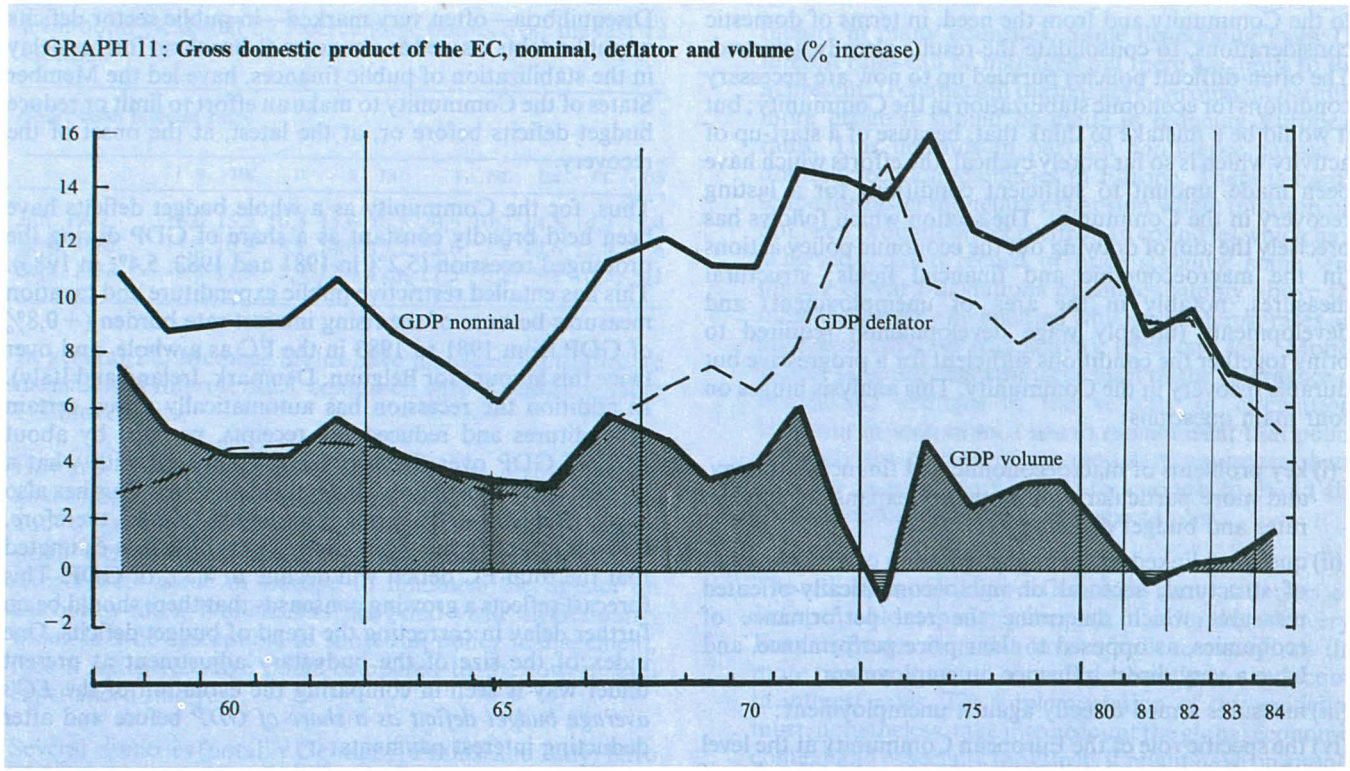
Annual average growth of manufacturing productivity per employee

	B	DK	D	F	I	NL	UK	EC
1960-80	5,3	4,5	4,2	4,7	4,6	5,3	2,4	4,0
1980-82	3,8	4,4	1,0	1,5	0,6	2,7	4,7	2,2

As regards the adaptability of real labour costs and labour income shares and their impact on investment and employ-

[2] For a detailed analysis see 'Community foreign trade; the equipment goods industry under threat', *European Economy*, No 16, July 1983.

GRAPH 11: **Gross domestic product of the EC, nominal, deflator and volume** (% increase)



ment growth in the enterprise sector, there are difficulties of measurement and interpretation. However it seems, as reported below, that there has been some relative improvement in Europe in the period following the second oil shock compared with the first one: real wages seem to have been less rigid and there has been some recovery in profits, although not in all countries, and overall the change would not yet seem to be decisive in relation to the more positive environment for enterprise in the United States and Japan.

In summary, the European economy has set in train a series of important economic adjustments and is progressively managing to face up to serious external constraints. Thus one should not underestimate the results which have already been achieved, notably on inflation. These results demonstrate both a collective recognition of the changes to be made and a capacity to implement the necessary policies. Similarly, the energy crisis has shown that the Community is capable of adapting to sudden upheavals in prices and supplies. But a return to lasting growth requires the continued pursuit of the adjustment effort already undertaken. It is on this effort that will ultimately depend the Community's capacity to achieve a lasting solution to the problem of unemployment. The results already achieved and the conditions which must still be fulfilled show that it is both indispensable and possible for the Community economy to follow through its structural adjustment effort and to assure a progressive increase in its trend rate of growth. It would, at all events, be a mistake to underestimate either the size of the task to be performed or the capacity which the Community has recently shown for committing itself to such action and for reacting to the developments bearing on it. Moreover, the timescale for the realization of this task underlines the need to continue to pursue an active employment policy for the more immediate alleviation of unemployment, which at its present high levels imposes major economic and budgetary costs as well as social ones.

3. Policy to strengthen the recovery: recent initiatives and the scope for further action

The stabilization policies followed in 1982-83 in the Community are now giving rise, as has been shown above, to a number of encouraging results: inflation is slowing down; external imbalances are being rectified; the stabilization of public finances is, at least in several Member States, proceeding favourably. The beginning of a recovery is becoming apparent and an acceleration in growth in 1984 can reasonably be expected. The situation and prospects with regard to unemployment, however, remain a major source of anxiety. Moreover, the positive results on the stabilization front, and similarly the economic outlook for 1984, are highly fragile: this fragility stems both from factors external

to the Community and from the need, in terms of domestic considerations, to consolidate the results already achieved. The often-difficult policies pursued up to now are necessary conditions for economic stabilization in the Community; but it would be a mistake to think that, because of a start-up of activity which is so far purely cyclical, the efforts which have been made amount to sufficient conditions for a lasting recovery in the Community. The section which follows has precisely the aim of drawing out the economic policy actions (in the macroeconomic and financial fields; structural measures, notably in the area of unemployment) and developments (notably wage developments) required to bring together the conditions sufficient for a progressive but durable recovery in the Community. This analysis hinges on four main questions:

(i) key problems of macroeconomic and financial strategy, and more particularly of monetary expansion, interest rates and budget deficits;

(ii) questions linked to the implementation of a whole series of structural, sectoral or microeconomically-oriented measures which determine the real performance of economies, as opposed to their price performance, and have a very direct influence on employment;

(iii) measures aimed directly against unemployment;

(iv) the specific role of the European Community at the level of its share of responsibilities in an important number of economic policy fields.

3.1 The macroeconomic and financial policy assessment

The principal characteristic of the macroeconomic and financial policies pursued in the Community in the recent past has been one of increased convergence. Certainly, this has not yet been sufficiently evident in all the key economic indicators—even though very substantial progress has already been achieved on inflation. But going beyond the realized outturn, there is now a broadly common approach both to very short-term questions and to the more fundamental adjustments to be made. In this respect it is particularly indicative that the present balance of monetary and budgetary policies—indeed narrowly determined by the international monetary environment—is the object of a rather widespread identity of view about the main medium-term objectives. Thus the Community's Member States are in general seeking to redirect the economy towards stronger growth of the private sector and a more satisfactory investment performance as well as a lasting consolidation of the reduction in inflation.

It has recently been very difficult to reconcile short-term monetary developments with the pursuit of medium-term objectives. World interest rates have remained high. This has retarded the recovery of productive activity in the Community—for which the widespread reduction or containment of budget deficits has been intended to make room. Disequilibria—often very marked—in public sector deficits or public debts, as well as a concern to brook no further delay in the stabilization of public finances, have led the Member States of the Community to make an effort to limit or reduce budget deficits before or, at the latest, at the onset of the recovery.

Thus, for the Community as a whole budget deficits have been held broadly constant as a share of GDP during the prolonged recession (5,2% in 1981 and 1982, 5,4% in 1983). This has entailed restrictive public expenditure and taxation measures because of the rising interest rate burden (+0,8% of GDP from 1981 to 1983 in the EC as a whole, and over twice this amount for Belgium, Denmark, Ireland and Italy). In addition the recession has automatically raised certain expenditures and reduced tax receipts, perhaps by about 1,5% of GDP over the two years, compared with what a modest trend rate of growth would have given. This has also been offset by restrictive policy measures. Overall, therefore, budgetary policy has been severe. For 1984 it is estimated that the total EC deficit will decline to 4,7% of GDP. This forecast reflects a growing consensus that there should be no further delay in correcting the trend of budget deficits. One index of the size of the budgetary adjustment at present under way is seen in comparing the evolution of the *EC's average budget deficit as a share of GDP* before and after deducting interest payments:

	1981	1982	1983	1984
Before deducting interest	−5,2	−5,2	−5,4	−4,7
After deducting interest	−2,2	−1,9	−1,6	−0,6

Thus, merely to offset the rising interest rate burden and keep the total budget deficit roughly stable, it was necessary to make significant tax increases or cuts in other public expenditures.

In the EC as a whole, money supply is expanding at present at an annual rate of 10%, whereas nominal GDP is probably expanding at a rate of 7%. Monetary policy is thus on average allowing for economic expansion in spite of international interest rate constraints.

Some substantial reductions in nominal interest rates in the EC have been made. From the beginning of 1982 to September 1983 average short-term interest rates in the EC fell from 14,3% to 10,5%, and in Germany they fell from 10,3% to 5,9%. Over the same period bond rates fell by about 2,5 percentage points in the EC on average, and by 1,5% in Germany. There have been some important successes registered in some other EC countries, such as Denmark, Ireland and Belgium, where stricter public finance and incomes policies appear to have changed expectations to the point of permitting large interest rate reductions. The most striking case has been Denmark, where government long-

term bond yields fell by 7 percentage points over the last 12 months.

Short-term interest rates

	B	DK	D	F	IRL	I	NL	UK	EC	US
Jan. 1982	16,0	15,3	10,3	15,0	18,5	20,5	10,2	14,5	14,3	13,4
Sept. 1982	13,0	16,3	8,1	14,0	15,2	18,6	7,9	10,6	12,0	7,6
Sept. 1983	9,3	11,9	5,9	12,6	12,8	17,5	6,3	9,8	10,5	9,1

In general EC Member States have managed a progressive reduction of interest rates, compared with the more volatile US movements.

However the real rate of interest remains high. The real government bond yield stands at present at 5,5% in Germany and 6,5% in the UK.[1] During the months of July and August, when United States rates were hardening again, distinct efforts were made in Europe to minimize the impact on European rates. Nonetheless the bond yield in Germany, which is little susceptible to short-run policy management, rose a full percentage point compared to the lowest level experienced this year.

Several countries (notably Germany, France and Italy) have maintained and expanded selective interest rate subsidies in favour of productive investments and specific sectors and regions, in part so as to give further protection against international interest rate conditions.

A result of the broad European preference for a budget-monetary policy mix different from that of the United States has been the tendency for the ECU's exchange rate to decline against the dollar. In the past year, European monetary authorities have at times intervened in exchange markets to moderate these exchange rate movements, and in August 1983 there was some concerted intervention involving the US, Japanese and some European central banks. While the Community would have preferred to see a greater convergence of financial policies internationally, the ECU's depreciation against the dollar has in the circumstances provided some extra opportunities for European enterprises in the US and world markets. However, as already pointed out, this is mitigated by other factors, including a low exchange rate for the yen.

Considering how monetary and budget deficit policies should best be adapted to the priority of consolidating the recovery in 1984, the broad assessment may be as follows:

(i) Monetary policy remains constrained by the international monetary environment as well as domestic factors in many countries. Some decoupling from US interest rates can be managed but there are limits to this at present. If changes in the market environment permits, more progress should be made in reducing European rates. This depends in part on confidence earned in domestic economic policies in Europe. There is hardly scope for faster monetary expansion where inflation has not been brought under control. In countries which have achieved a good record of price stability, some temporary upward deviations of money supply above the target range may be justified while real interest rates are high and inflation and activity levels are low. Money supply targeting has also to be alert to the emergence of unexpected changes in the velocity of circulation. However in such cases it has to remain clear that policy will steer the growth of the monetary aggregates back into the targeted path promptly enough to avoid the recrudescence of inflationary expectations.

(ii) The reduction of budget deficits is, in many countries, an indispensable step along the path of a durable recovery. Further progress in this area is still necessary, all the more because it would contribute directly to a reduction in interest rates. The implementation of this guideline must, nonetheless, take into account the global economic context and especially the effects it might have on supply and demand. Thus countries which have already achieved major progress in their adjustment (slowdown of inflation, bringing the external account back into balance) and record modest budget deficits should avoid too precipitate a reduction of those deficits. At all events, if activity showed further signs of weakness, it would be appropriate to allow the automatic stabilizers to operate. Just as it is indispensable for the policy of reducing public deficits to be presented in a convincing way, it should also be possible to follow this policy without adhering too rigidly to pre-established targets but rather taking account of its possible destabilizing effects on short-term developments. Progress achieved in reducing deficits should, in any event, increasingly leave room for a reduction in tax pressure.

3.2 Policies to strengthen productive potential and improve resource allocation in the public and private sectors

Three broad domains of action will be discussed:

(i) The restructuring of public expenditure and taxation, with priority for improving productive potential;

(ii) The role of the social partners in improving competitivity and stimulating the recovery process;

(iii) Re-examination of regulatory functions of government with a view to stimulating the economy.

[1] The deflator used is the rise in the consumer price index over the last 12 months.

3.2.1 *Restructuring public expenditure and taxation* [1]

Efforts to achieve better control of total public expenditure have been widespread. However, given both the continued weakness of the labour market, and hence a rising cost of unemployment compensation and programmes to create jobs and to reduce the labour supply, and a continuing increase in the nominal cost of debt-service, these efforts were still not able to prevent its share of GDP from rising. The share rose from 49% in 1981 to an estimated 51% in 1983 for the EC as a whole. Over the two year period only Germany succeeded in stabilizing this ratio; in the UK the increase was quite small. In other countries the increases ranged from 2% to 4,5% of GDP.

On the whole public consumption's share of GDP has been stabilized at about 19,5% of GDP in the EC as a whole. The compression of entitlements or benefits levels for current transfer payments was often significant, but in many countries it did not prevent further increases in their share of GDP, notably from 22,5% of GDP in 1981 to 23,5% in 1983. Measures to limit current transfers often included, for example, reductions in some social and family benefits, a tightening of eligibility criteria for unemployments benefits (and in some cases reductions in the levels of such benefits), and various techniques for increasing user charges for health services. Announcements recently made in Member States for 1984 budgets indicate further efforts, often of exceptional severity, to bring the trend of current transfer payments under control (Germany, Italy, France, Belgium, Netherlands, Denmark).

As regards public investment, some countries, notably France and Greece, have made very large absolute increases in the level of their public investment expenditures. Several other countries have been introducing a positive discrimination in favour of investment expenditure in roughly maintaining their level in real terms alongside a severe curtailment of many programmes of current public expenditure (Germany, Italy). This policy thrust comes after a number of years in which public investment appears to have been more squeezed than current expenditures.

For the promotion of private investment, a number of fiscal initiatives are being implemented. [2] Indeed this category of action is receiving probably a stronger priority than public investment, notably in the UK. Here two broad types of action may be recognized: fiscal provisions to induce physical investment by enterprises, and fiscal provisions to strengthen the flow of savings into risk capital.

In the former category, depreciation allowances have been notably improved in France, and this is envisaged in Germany in 1984. The UK has introduced a large number of fiscal provisions to help the enterprise sector, some targeted on selected sectors such as oil exploration and new small firms, some easing corporate taxes more generally. Italy has improved the VAT treatment of investment, while the Netherlands has eased taxation on the self-financing of enterprises out of profits.

To aid the risk capital market France and Belgium have extended or introduced fiscal advantages for personal investment in shares as has the UK for investment in smaller companies; in Italy a law has been passed to permit and encourage the establishment of investment funds; Germany and the United Kingdom have improved the fiscal provision for employees to take up shares in their enterprises. [3] Germany and other countries are examining how to improve the supply of venture capital.

A general policy objective has been to reduce subsidies to uneconomic sectors and the financing of the operating losses of State enterprises. A particular aim has been to couple this with the reduction of excess capacity and with restructuring measures in the sectors and regions concerned. Remaining subsidies need to be subject to better control of their economic justification, that they lead towards the competitiveness of recipient enterprises and are in any case compatible with EEC competition law. In terms of aggregate expenditures, although the statistics are often incomplete or difficult to interpret, it is certainly not yet evident that the trend of these expenditures has on the whole been mastered. There remains a strong concentration of subsidies in contracting industries (steel, ships, textiles, coal, railways) compared to the financial effort in favour of innovation and advanced technology industry. In the UK there are major examples of reduced subsidies or losses of State enterprises (automobiles, railways, air transport) and individual examples in other countries. In Italy, the losses of the State enterprise sector remain of considerable macroeconomic proportions. In Germany the recent *Subventionsbericht* reported still slightly increasing federal subsidies, with a DM 29 000 million total expected for 1984. Other countries would do well to publish equally systematic information on their subsidies.

A reduction of the tax burden, or at least putting a stop to its rise, is recognized as a major aspect of improving the European economy's performance and competitivity. The combination of cyclical influences and the priority given to containing deficits resulted in fact in further increases in the GDP share of tax and social security contributions taken

[1] See also the Commission's communication to the Council on 'Fiscal policy in the Member States in 1984' (COM(83) 423), 1 July 1983, and a related report on 'Budget discipline and economic convergence' and 'Restructuring public expenditure in favour of productive potential' (SEC(83) 1147), 6 July 1983.

[2] See 'Business investment and the tax and financial environment', *European Economy*, No 16, July 1983. Also the Commission's communication to the Council on 'Tax and fiscal measures in favour of investment' (COM(83)218) of 18 April 1983 (also reprinted in *European Economy*, No 16, July 1983.

[3] Through increasing the amounts of share capital participations subject to tax advantages and, in the German case, benefiting from subsidies.

together (46,6% in 1983, after 44,7% in 1981 and 38% 10 years earlier for the EC as a whole). Germany held the aggregate unchanged from 1981 to 1983. In the UK it broadly stabilized between 1981-82 and 1982-83 but in all other countries the tax burden grew, in some cases very substantially (France, Italy, Greece, Luxembourg).

Broad changes in tax structure have been pursued in Germany, as in the UK in recent years, aimed at improving incentives and private investment. As regards France, major changes in 1981 and 1982 in the tax structure have been guided by the objectives of fiscal equity, with the result of moving the income-equalizing effect of the tax system closer to the European average.

Social security costs are conspicously high as an addition to labour costs in Europe compared with other industrialized countries. All countries have been attempting to limit these costs. However, no country was able to reduce the average rates of social security contributions in the past year, although in the UK the additional labour cost imposed in the form of a surcharge on firms has been reduced. Several countries were faced with rising social security expenditure (especially unemployment benefits) and deficits, and were obliged to raise total contributions (France, Luxembourg, Netherlands). Such action to reduce deficits is helpful *vis-à-vis* interest rates, but from the point of view of the future of the enterprise sector and employment, and even if part of the problem is linked with the level of activity, the correction should be made less by increasing contributions than by curtailing expenditure. Heavier contributions still appear to be the predominant remedy.

As regards further action on the restructuring of public expenditure and taxation:

(i) While recent policy initiatives have often been important, the effort will have to be sustained or even in some cases intensified if past trends in the structural growth of public expenditure and taxation are to be adequately corrected;

(ii) There is still a tendency in several countries to curb budget deficits more by further increases in the tax burden than by economizing on expenditure, and this needs to be halted or reversed;

(iii) Improvements in the tax and financial environment of firms should be made in order to induce a greater flow of resources into investment and a larger supply of risk capital. In its communication of April 1983, [1] the Commission concluded that there was a need to avoid increasing, and even to reduce, the tax burden on firms; to strengthen and adapt investment incentives; to encourage risk taking by adjusting certain tax arrangements; to improve the channelling of savings, especially the savings of wage- and salary-earners, into risk capital. A number of measures along these lines has recently been adopted or is proposed in the Member States. It is important for this effort to be maintained and adapted, along the lines proposed by the Commission and as a function of the specific situation in each member country. In this way, firms should be enabled to respond better to the requirements of modernizing productive structures.

[1] 'Tax and fiscal measures in favour of investment', 18 April 1983, (COM(83) 218 final).

3.2.2 *The development of wages*

In many EC countries there have been strong efforts to reduce wage cost increases in order to improve international competitiveness and reduce inflation. The form of this action has been quite varied according to institutional and other aspects of national situations. Examples include action focused on indexation practices (Belgium, Italy, Denmark, the Netherlands and Luxembourg), on the important role of public sector contracts (Germany, Netherlands, United Kingdom), or on broader incomes policy concepts (France). Overall, considerably stricter nominal and real wage-cost disciplines are being observed in EC countries. In nominal terms the average increase in compensation of employees per head in the EC is estimated to have declined to 7,2% in 1983, compared with a peak of 13% in 1980.

Cyclical recession usually causes an adverse development in labour productivity, but on this occasion the effort to improve productivity performance has outweighed the cyclical influence. Thus unit labour cost increases in the EC have on average declined to an estimated 5,5% in 1983, compared with the peak of 11,5% in 1980. However this is still above the 3% increases estimated for 1983 for both the United States and Japan. The real product wage (unit labour costs deflated by the GDP deflator) fell by about 1% in 1982 and is expected to do so too in 1983. This indicates some redistribution of income in favour of enterprise profits, a pattern common to almost all EC countries.

For the period ahead there is still much to be done to adapt costs and income shares in a manner that will support a long-run economic recovery.

(i) the development of nominal pay must continue, in certain EC countries in particular, to contribute to the slowdown in inflation, thus also creating increasing room for real economic growth. The 'real' degree of restrictiveness of financial policy, which is fixed in nominal terms, depends in large measure on the behaviour of trade unions and enterprises with regard to pay.

(ii) While it is difficult to prescribe normative evolutions for real pay for a wide range of country situations, a plausible yardstick is that there should be little or no expectation of real pay increases, at the level of the macroeconomic aggregate, until the economic recovery has well advanced into a phase of strong investment and employment creation. In some cases negative real wage adjustments are still necessary. Income growth needs to be channelled as a priority into capital accumulation and capacity expansion for a period of some years. The relatively low profitability of the European enterprise sector remains a fundamental problem inhibiting the recovery process.

(iii) As regards the negotiation of pay at the enterprise level, two objectives are of widespread relevance. First, increased flexibility in pay differentials as between skills or branches is often needed to create more employment opportunities and better clear the labour market, even in countries where aggregate pay has evolved reasonably. Secondly, pay negotiations should be adapted far more directly to helping the individual enterprise invest and expand. Europe would probably benefit from a higher share of renumeration being related to enterprise profits and performance, a practice which is far more developed in Japan. Schemes for participation of employees in the capital wealth of the enterprise are on a modest scale. Imaginative schemes are called for to adapt pay to the overwhelming need in the years ahead for high investment financed by risk capital. While the main initiative must lie with the social partners, governments can, as already indicated, encourage the process with regulatory and fiscal provisions.

3.2.3 *Re-examination of regulatory functions of government*

It is increasingly recognized that many regulatory activities and mechanisms do not properly achieve their desired goals, or do so at very high costs—both in terms of administration and disincentives to innovation and to the legally-imposed efficiency of resource allocation; thus they may have in effect a depressing impact on the potential rate of growth. Recent actions to reduce the economic costs of (broadly defined) regulation are extremely disparate in nature, and no doubt leave large further scope for reform. Such examples include: the easing of rent regulations in Germany, of the conditions of labour recruitment in Italy, of working time regulations in Belgium; the introduction of lightly regulated enterprise zones in Belgium and the United Kingdom; and the privatization of some State enterprises, and in the Netherlands a wide-ranging programme of action to streamline regulations that impede economic activity.

There is typically a very wide range of restrictive arrangements affecting service branches and the professions as well as industry and labour markets. Competition policy in its traditional sense is usually quite limited in scope by comparison with what needs to be done. Many service branches, which are sometimes self-regulated or locally regulated, are good candidates for review—for example restrictions on opening hours of shops. Many financial services and professional activities are needlessly compartmentalized and sheltered from competition, imposing higher costs on the economy—or, directly, a higher cost of living. Monopolistic arrangements in various branches of industry may have lost their *raison d'être,* for example for reasons of technological change. While not calling into question basic standards or some recent well-founded regulatory legislation, there are nevertheless labour laws, often introduced at times of full employment and of a smaller income-redistributive role of the State, which need to be re-examined for conformity with present economic and social priorities.

In conclusion, for the period ahead:

There is much more to be done in Member States to remove unnecessary market rigidities. The objective must be to devise a continuing stream of regulatory reforms pushing in the direction of higher productivity and less inflated prices.

3.3 Direct labour market actions to ease the unemployment problem

Major training programmes have been further developed, for instance in Germany, France, Ireland, Netherlands, United Kingdom and the Commission has prepared a resolution on vocational training. There is an efficient large consensus on the usefulness of these types of measures. They constitute an means of combating that part of unemployment which is structural. Technological progress is such that training needs constant adaptation if mismatch on the labour market between skills and vacancies is to be avoided. Direct aids to employment creation, either through a reduction in employers' social welfare contributions, or employment subsidies to the public sector, have also been introduced or expanded (particularily in Belgium, Denmark, Germany, Greece, France and the UK). In Germany, for example, 56 000 people are now concerned in the programme of employment subsidies, while 130 000 jobs are to be created in UK for the long term unemployed. In both cases the additional financial burden is expected to be limited, since planned expenditure is partly offset to the unemployment benefit payments saved.

On the other hand, early retirement schemes (such as those which have been introduced in Belgium, the Netherlands and France) are representing a growing financial burden on social security budgets. In addition, some doubts exist as to how much further these measures can be expanded. Depending on activity rates, a progressive reduction of the average retirement age may lead to a reduced ratio of employed to retired population, especially in a few years'

time (1986) when the demographic growth of the population of the age bracket 15-64 stops, whereas the older population will be growing fast.

Programmes of local initiatives are receiving increasing attention, for instance in France and United Kingdom, in order to encourage self-employment creation both in the service and in the industry sectors. Such developments need help, for example as regards skills and guidance over organizational, fiscal and regulatory matters. If such support can be given at the time the initiatives are established, this will additionally help stem the growth of the black economy.

The Commission is preparing a communication to the Council on this subject. The potential employment capacity in very small-scale enterprises appears to be very considerable—depending upon diverse legal forms: self-employment, company with individual ownership, cooperative enterprises and non-profit making companies and voluntary organizations. Such initiatives may exploit local skills in craft and engineering sectors, local natural resources; they may also, for example, take over valuable parts of failed enterprises.

The reduction and reorganization of working time has become an important element in debate and action on the very high rate of unemployment.

In several Member States, negotiations have been engaged or concluded with a view to using shorter working hours as an instrument of employment policy. In France, following official measures decided to reduce the average working week from 40 to 39 hours in 1981-82, the initiative has been passed on for decentralized negotiation.

In Belgium and the Netherlands, collective agreements have, as proposed by the government, in many cases linked the reduction of annual working time to increases in employment, together with measures of pay restraint. In Italy, specific working hours reductions are envisaged in new collective agreements. In some cases an increased flexibility in working time in service sectors has been negotiated alongside a lengthening of opening hours and increase in employment (e.g. in the Belgian bank sector).

For such measures to have a durable positive impact on total employment, strict conditions have to be assured to prevent increases in the costs of enteprises. Experience is in fact showing both favourable and unfavourable examples. Among the positive examples, the combination of more flexible and shorter individual working hours with longer opening hours for service branches, more shift-work in industry, and more part-time jobs can all contribute positively to the economic recovery and to the reduction of unemployment. Many more detailed and often decentralized initiatives are emerging, such as the job splitting schemes in the United Kingdom. The French Ninth Plan, too, is intended to encourage the development of 'new formulae' for part-time jobs. They will be integrated into the negotiation on reduction of working time.

In response to the Commission's memorandum [1] of 1982 on the reduction and reorganization of working time the European Parliament adopted a Resolution on 28 April 1983 recommending in the short run a significant reduction in working time, taking account of national circumstances and the circumstances of individual sectors and firms, and implemented in a way that avoids cost increases.

The social partners in the Economic and Social Committee adopted in July 1983 an opinion which concluded that the reduction and reorganization of working time could help to mitigate the unemployment problem, if conditions similar to those outlined in the Commission's memorandum were met. [2]

In September 1983 the Commission proposed a Recommendation [3] to the Council on the reduction and reorganization of working time aiming:

(a) to bring about a reduction in individual working time, combined with its reorganization, sufficiently substantial to support the positive development of employment, under conditions which safeguard competitivity as well as basic social rights; and

(b) to limit systematic paid overtime more strictly and to increase the extent to which necessary overtime is compensated by time off in lieu of additional payments.

In conclusion, for the years ahead active policies must be pursued which aim at reducing unemployment and its social and economic cost. While it takes time to change macroeconomic environment in the desired directions, many immediate initiatives have to be vigorously pursued. In particular the Commission is advocating that the following domains of labour market policy be given priority:

(i) training and retraining schemes, especially for young people; [4]

(ii) job creation initiatives, also with priority for young people; [4]

(iii) increased emphasis on the stimulation of local initiatives for small-scale employment creation;

1 COM(82) 809 final.
2 ESC 663/83 and 664/83 of 6 July 1983.
3 COM(83) 543 final.
4 In April 1983 the Commission addressed to the Council a proposed 'Resolution on the promotion of employment for young people', (COM(83) 211); this is currently under discussion.

(iv) initiatives to increase employment through the reduction and reorganization of working time, while respecting the necessity of avoiding increases in unit costs of production.

3.4 Actions by the European Community to strengthen the recovery

The European Community's own policy responsibilities are substantial in its management of policies for trade, the internal market and competition. Moreover its role is tending to develop in the macroeconomic field and in the field of improving competitivity, notably industrial competitivity, and more generally of strengthening the economic structure in liaison with the development of its financial instruments. The present report gives an overview of recent developments and initiatives following, notably, the conclusions of the European Council held in Stuttgart in June 1983.

3.4.1 *Macroeconomic and monetary policy*

The European Monetary System fulfills several functions in the present economic situation, all tending ultimately to ensure stable economic growth. First, it ensures exchange-rate coordination for most of the European continent and protects participating countries against the pronounced exchange-rate instability prevalent in the industrialized world as a whole. It thus ensures a certain homogeneity and cohesion for the economic entity formed by the Community. It thence contributes to consolidating the advantages afforded by the possibility of exploiting, notably in the industrial field, a large, integrated market. Further, the EMS is a strong instrument for monetary policy coordination and, beyond that, serves as framework for discipline and for experience in the better common practice of coordinating economic policies. Finally, the EMS, by requiring a common assessment of the external monetary constraints, provides the Community with an organized base for its contribution to work on improving the international monetary system.

In the past year there was one realignment of parities in the EMS, on 21 March 1983. This realignment was notable for two reasons. It was a realignment involving finely-judged changes for most of the central rates. It was accompanied by important domestic policy adjustments, in particular in France, so strengthening the future stability of the System.

The use of the ECU in private markets also grew markedly in the past year, and this should contribute in time to a more balanced international financial system.

The world economic recovery is almost certainly being hindered by slowly increasing protectionism. An important aggravating factor at present lies in misaligned exchange rates and widening current account imbalances on the part of the United States and Japan. More stable and cooperative solutions to these problems are strongly desired by the EC.

3.4.2 *Structural and microeconomic policy*

The dimensions of the *internal market* in Europe represent an enormous underexploited potential for making the economic environment propitious to growth, efficiency and low inflation (taking a broad view of this domain to include non-tariff barriers and the potential for more active competition and industrial policy). The extension of the internal market, which should provide enterprises with guaranteed access to a market of continental size, could constitute an element of dynamism as powerful as that which the achievement of the customs union represented for the Community during the first 10 years of its existence. The time has come to recognize the fundamental interdependence between this complex of microeconomic topics and the macroeconomic prospects for the economic recovery of the European Community in the mediumrun. The links between EC actions, or potential actions, are widely and deeply connected with national policies. The two—national and Community—sets of actions have to move powerfully together in mutually supporting directions. Whole branches and sectors of the economy are at present blocked in their potential for higher productivity growth and for lower costs and prices by a combination of national restrictions and resistance to the efficient use of Community powers. Almost all trade in manufactured goods is severely impeded by multiple non-tariff barriers, including failure to agree on common technical standards, restricted public procurement and frontier delays and costs. Fast growing, and potentially even faster growing, branches of the service sector—such as civil aviation, road transport, insurance and financial services—are the subject of very serious regulatory restrictions across the EC, and negotiations on Commission proposals have been extremely slow-moving in this field, and the conclusions of the European Council of Copenhagen should be implemented more rapidly. The capital markets of the Community are also badly fragmented: the Commission has proposed a new attack on these problems, with a view to assuring a free flow of Europe's large capacity for savings into the effective restructuring of the Community economy. [1]

As regards several of the technologically-advanced growth industries—such as information technology, biotechnology, aerospace and alternative energy sources—there is in the view of the Commission a vast potential for more effective European collaboration. There are several different types of organization of the European effort which have shown

[1] See communication of the Commission to the Council 'Financial integration', 20 April 1983 (COM(83) 207 final).

themselves to be successful, of which the Community's Esprit programme is a new example, and should stimulate a much larger strategic push for a reversal of Europe's industrial-technological weaknesses. [1]

Regarding the Community budget, the Commission has, in its recent communications, recommended increasing the share of spending devoted to action to right the economy and to improve the employment situation: it has therefore proposed a doubling in real terms, over a five-year period, of the resources devoted to industrial, regional and energy objectives and to research and development.

The Community's borrowing and lending activities have also been developed and adapted to the need for an improvement in investment performance. Lending operations amounted to 5 300 million ECU in 1982 and will probably show a significant increase in 1983, apart from the 4 000 million ECU balance of payments loan to France. The higher priority given to the financing of investment in the productive sector is illustrated by the fact that loans in this area have more than doubled from 1981 to 1982—particular attention having been paid to small and medium-sized enterprises. The continuing development of these activities has been secured in 1983 by the extension and renewal of the New Community Instrument (NIC), under which the Commission has been empowered to borrow a further 3 000 million ECU, with subsequent authorization of a first tranche for an amount of 1 500 million ECU. In addition, the Commission has made in June 1983 a proposal for a Community financing of innovation in small and medium-sized enterprises (COM(83)241). In the Commission's view, a determined Community action, with the main objective of encouraging the private financial sector in the Member States to become more active in favour of innovative investment in small and medium-sized enterprises, will open up a substantial growth potential and lead to the creation of additional future-oriented jobs.

In conclusion, the following further action by the Community is called for the period ahead:

(i) Reinforcement of the European Monetary System is feasible as an aid to economic recovery, and a most important next step could be extension of its membership to the whole Community. Strengthening of the European monetary mechanisms should help give economic policy in Europe a greater margin of manoeuvre in relation to the international monetary environment. Development of the private and official uses of the ECU, and a revision of the capacity of its lending mechanisms, are among the possibilities of action.

(ii) Better international cooperation could certainly help strengthen the recovery, and the Community must increasingly organize a collective position in order to influence events as effectively as possible. Concretely, the Community's interest is that the major industrialized countries should correct, or avoid creating, large distortions and external shock impulses in their financial policies. In the present situation, action in the United States to reduce future budget deficits is important to European policy management aimed at sustaining the recovery. The Community should also encourage work towards an international monetary regime that is less unstable in its exchange rate behaviour, and whose adequacy in terms of the supply of reserve assets is assured. The Community urges that the expansion of IMF financial resources is quickly ratified by the United States. The industrialized world must give strong support to efforts to strike the right balance between adjustment and financing in the heavily-indebted developing countries.

(iii) A quantum step in progress in opening up the Community's internal market and in the stimulation of its advanced industrial capacity is now required as a contribution to medium-term economic recovery. If such progress is realized, the productive sector will have new opportunities to develop trade and industrial production.

(iv) The Community budget should progressively be directed towards giving more active support to the achievement of industrial, regional and energy objectives as well as research and development objectives. Finally, the exploitation of the credit of the Community, through the development of its borrowing and lending activities, should contribute directly to the priority objective of strengthening investment in the Community.

4. Summary and conclusions: for consolidating a European recovery

1. The European Council has requested the Commission's assessment of the extent of the economic recovery, and what further measures could be taken to strengthen it.

2. Some cyclical recovery in Europe is apparent. But it is patchy and on the whole weak and potentially vulnerable to any new adverse shocks from the international economy. The increase in unemployment may have tailed off, but even if the level does stabilize it remains very high. Some of the major prerequisites for a stronger recovery—monetary and financial stabilization—have been largely assured in several

[1] For further detail see note of the Commission (COM(83) 547 final) on '*L'amélioration de la Competitivité internationale des entreprises européennes*', and many convergent ideas also presented in memoranda of the French Government '*Une Nouvelle Étape pour l'Europe: un Espace Commun de l'Industrie et de la Recherche*', and of the United Kingdom Government 'The Development of the Community: other policies', and of the German Government 'Reconsideration of policies and the development of new actions (excluding agriculture)', all of September 1983.

countries, and progress is being made elsewere. There is increasing evidence that there is now a Community-wide effort to bring trends in public finance and wage costs under control.

3. But the transformation of the adjustment process into a next dynamic phase of recovery is not yet evident on a wide or deep scale. This may emerge automatically in some degree. However, in the Commission's judgement, the risks of relapse into continued quasi-stagnation are too great to let policies stand on the status quo.

Because of the risks, mainly of external origin, to which the recovery is still subject, the Community should make it its first priority, alongside the national or related internal actions described in this report, to participate in every way in action to stabilize the international environment. whether such action concerns contributions to finding a lasting and balanced solution to the problem of indebtedness, or the improvement of the international monetary system.

Internally, a further impetus, as outlined below, is needed if the European economy is to be regain the desired course— one of significant growth, of high levels of employment and competitivity, and low or declining inflation rates.

4. The Commission is of the view that the further development of policy to strengthen the prospects for a durable and profound European economic recovery should be in the following directions:

(i) Use of room for manoeuvre to reduce interest rates further as and when international and domestic conditions allow;

(ii) Reduction of structural budget deficits and then their stabilization at a low level to facilitate a renewed growth of private investment, without, however, excluding recourse to the automatic stabilizing properties of the budget, where its basic financial condition is sound,

(iii) Restructuring of public expenditure and taxation, notably to:

— give priority to expenditure, particularly infrastructure expenditure, that helps expand productive potential,

— stop and even reverse the growth of the tax burden,

— further improve the fiscal environment for the enterprise sector;

(iv) Review of regulatory activities of government with a view to reducing inefficiencies and rigidities that depress productive potential;

(v) A sustained effort to reduce unemployment through direct measures such as:

— training and retraining schemes, especially for young people,

— job creation initiatives, especially through stimulating local and small-scale employment units,

— the reduction and reorganization of working time respecting the need to avoid cost increases;

(vi) Development of incomes in line with the conditions for economic recovery, in particular:

— in many countries, further nominal deceleration in pay, which will reduce inflation and help financial policies have a more expansionary real effect,

— real wage evolutions that allow for a major improvement of enterprise profitability to support an investment recovery, and growth in employment,

— greater flexibility in pay, through collective negotiations to help clear the labour market better, and an expansion of practices which relate pay to enterprise performance and boost employee participation in the financing of investment;

(vii) Strong support at the European Community level for this concerted direction of national policies, notably through action under three headings:

— reinforcement of the Community's monetary mechanisms and determined action of the Community in pursuing improvements in the international monetary system and the environment for world trade,

— building up Europe's potential in new growth sectors of advanced technology such as information technology, telecommunications and biotechnology, through complementary national and EC action,

— large steps in fully opening up the Community's internal market, in which the remaining plethora of restrictions is barring the way to a potential growth dynamic.

5. The European countries have little hope, if they act in a disorganised way, of transforming achievements in stabilization into a dynamic recovery process. Only a quantum step forward in a concerted national and European Community action, which could be much helped by better wider national cooperation also, can achieve a strong recovery.

6. With a number of internal and external factors now clearly working in favour of economic recovery, a rapid mobilization of all the means of action presented above could confirm the movement.

7. If a sufficient critical mass of consistent policy initiatives is built up within countries and the EC as a whole, the fundamental climate of economic expectations in Europe could be changed in favour of growth in investment and employment and in favour of competitive European enterprise.

8. The objective should be to make 1984 the pivotal year in confirming this fundamental change in the European economy's development. A straw-fire of unsustainable growth should not be the objective. What is required is the maximum positive growth consistent with progress in reducing fundamental structural problems that have been accumulating over a least a decade, if not two.

Labour market policy measures in 1982-83 [1]

Belgium: Early pension granted on proof of replacement workers taken on; temporary reduction in social security contributions for employees recruiting their first employee; financial aid to small and medium-sized firms taking on registered unemployed; raising of school-leaving age; possibility of reduction in working hours associated with taking-on of additional workers.

Denmark: Government aid to firms or local authorities taking on young unemployed people.

FR of Germany: Temporary aid to firms taking on unemployed people; programmes of training and retraining for young and adult unemployed people.

Greece: Financial aid to creating jobs for young people; reorganization of apprenticeship system; reduction of working-time to 40 hours a week.

France: 'Job training' contracts (financial aid to employers who guarantee training and a certain length of employment); help towards the reduction of working-time if this takes place without loss of output and with the number of workers maintained or increased.

Ireland: Training programmes for young people; setting-up of an investment body for direct job-creation.

Italy: Setting-up of a investment fund for employment; agreement among the two sides of industry and the government, among others, on the wage escalator (*scala mobile*) and on a reduction in working-time by 40 hours a year by mid-1985.

Luxembourg: Aid for employing long-term unemployed people; ban on overtime.

Netherlands: Periods of job training for unemployed young people; subsidies to employers offering apprenticeships; agreement between the two sides of industry on the possibility of a reduction in working-time.

United Kingdom: Job-training programme for young people involving 12 months training for all those leaving school at 16; community programme creating part-time community-service jobs; job-splitting scheme to encourage part-time work.

[1] This list is illustrative, not exhaustive.

Part II — The economies of the Member States

In *Belgium,* the economy made further progress towards restoring external balance by improving competitive capacity. However, economic activity was weak for the third consecutive year and this led to a further increase in unemployment. Gross domestic product for 1983 contracted by almost 1% in real terms.

It is expected that 1984 will see a slight expansion, mainly due to increased exports, since domestic demand will, on balance, probably remain stable. Private consumption is expected to contract somewhat as a result of the squeeze on households' disposable income, while business investment should gradually show more vigour. The balance of payments on current account will show a smaller deficit than in 1983; the deficit of 1,5% of GDP will be mainly attributable to the levels of official transfers and interest payments on public debt, denominated in foreign currency since, for the first time since 1975, a small surplus is expected on the balance of trade. Unemployment is likely to be up again on the previous year, affecting on average 15,3% of the civilian labour force in 1984. The agreements concluded since the end of 1982, at sector or individual firm level, which provide for shorter working hours and extra recruitment in the context of wage restraint, may help to curb the growth of unemployment.

Since the currency realignment of March 1983, the Banque Nationale has managed to reconstitute its foreign currency reserves and clear its debtor position in the European Monetary System, while reducing the discount rate from 14% to 9%. If monetary policy could be geared to a steady reduction in interest rates, this would make a major contribution to the recovery of investment; however, the distance still to cover in achieving external equilibrium and the sizeable borrowing requirement of the public sector, would appear to make the implementation of such a policy far from easy.

Incomes restraint must be maintained to safeguard the competitiveness of the economy and the development of productive investment in 1984, but the reduction of the budget deficit is now the keystone for economic improvement and for a return to conditions conducive to sustained growth. Against a background of weak growth, with adverse effects on tax revenue, the reduction of the central government deficit to 7% of gross domestic product—the target for 1985 set in the 1982 government agreements—will certainly not be easy, in spite of major savings in expenditure in the past two years. Even the slight reduction in net borrowing in relation to 1983 planned in the draft budget for 1984, which actually implies somewhat slower progress towards the 1985 objective, will be difficult to achieve in view of the weakness of activity in 1984. However, the cost of servicing the public debt and the burden of taxation have reached a stage where even tighter management of expenditure is absolutely essential. Also, the limit imposed on the central government deficit (11,3% of GDP in 1984, compared with a deficit of 12,7% of GDP in 1983) cannot in any circumstances be exceeded as it has been in previous years. If necessary, supplementary measures will have to be taken to keep the deficit within this limit during the budget year.

Table 4

Belgium: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	8,5	4,8	3,5	3,2	7,8	0,2	−1,3	8,6	2,2
1971-80	10,4	3,2	7,0	7,0	11,9	0,4	−4,6	10,3	5,8
1981	4,0	−1,1	5,2	8,8	7,4	−4,2	−12,6	6,6	10,7
1982	8,1	1,0	7,0	7,4	8,0	−3,6	−11,9	5,7	12,6
1983 [1]	6,2	−0,9	7,1	7,8	6,0	−2,4	−12,2	5,0	14,4
1984 [1]	7,0	0,6	6,3	6,5	7,7	−1,5	−11,1	6,7	15,3

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies
2 % change over previous period, annual rate.
3 End of year.

Restoring the budget to a sound footing is an essential condition for more satisfactory development of economic activity and employment, but basically, it will be determined in the medium term, by in-depth restructuring of the economy which in turn depends on a substantial increase in productive investment. The tax measures adopted in 1982 will help here, but a policy of restraint for both direct and indirect wage costs is equally important, if not more so. The results obtained so far confirm, subject to the above-remarks, that the policies pursued are producing results and that a return to growth in production and employment, in the years to come, can be expected.

In *Denmark*, economic growth slowed down from 3,4% in 1982 to some 2,2% in 1983, and the inflation rate came down from about 9,8% to 6,6%, partly as a consequence of the restrictive stance of fiscal and incomes policy since the end of 1982. Following the sharp deterioration in 1982, the deficit on the current balance of payments improved considerably as a result of a favourable shift in the terms of trade. Although the public finance situation worsened between 1982 and 1983, there was some improvement during 1983 as social transfer payments and public sector pay increased at a slower rate, and the cost of servicing public sector debt increased less rapidly. Thus the net central government borrowing requirement was limited to 12,4% of GDP, slightly below the corresponding guideline adopted by the Council last year. Although lower inflation helped to increase the room for manoeuvre with regard to economic policy, the employment situation did not improve. The slow increase in economic activity inhibited the demand for labour from the private sector and consequently the reallocation of resources envisaged as between the public and the private sector.

The outlook for 1984 points to rather slow growth, accompanied by a moderate increase in nominal wages and prices. Real domestic demand is likely to level off, reflecting a stagnation of private consumption, a fall in public consumption, and a moderate pick up in private investment. Despite growing net interest payments abroad, the current balance of payments should improve, particularly since domestic substitution of imported energy becomes more and more important.

The economic policy pursued during 1983 and envisaged for 1984 aims primarily at reinforcing the competitive parts of the economy and at improving resource allocation, and thus the overall performance in the longer term, even though there will be some dampening effects on economic activity in the short run.

The government plans to cut expenditure and to raise public revenue in 1984 with a view to reducing the net central government borrowing requirement to some 11% of GDP. Apart from slowing down increases in various obligatory and non-obligatory expenditure, the government envisages higher social contributions and public service charges. The planned reduction of the budget deficit is fully in accordance with a strategy designed to achieve better economic convergence within the Community. The cost of servicing the growing public sector debt represents a major constraint, so that it is unavoidable, if the central government net borrowing requirement is to be reduced, to cut other public expenditure, although this should not lead to a reduction of items needed to develop productive activities. A substantially lower government deficit will no doubt have a favourable effect on inflationary expectations and on interest rates and thus become a major incentive for enterprises to invest and accelerate the necessary structural change in the economy.

The biennial wage settlements agreed in the spring of 1983 conform to the government guideline of a 4% nominal increase in 1983 and 1984 and imply a rise in unit labour costs below the EC average. The aplication of this guideline should allow for sufficient flexibility in the labour market to promote a better allocation of resources. This should help to avoid bottlenecks in parts of the labour market and, together with the implementation of various training schemes, facilitate the redeployment of the labour force.

The government's structural policy, incorporated in its overall strategy, is mainly embodied in the investment programme launched in the autumn of 1982, which aimed at coordinating private and public activities in such major areas as education and research, technological innovation, infrastructure and communications. As investment in energy will be falling in 1984, more room will be available for capital formation in advanced technology with the aim of reinforcing the competitiveness of the economy. Under the 1984 budget, the government proposes to change tax legislation so as to encourage risk capital investment.

The *Federal Republic of Germany* experienced a distinct upturn in economic activity in the first half of 1983 but, because of the low level from which the recovery started, the year-on-year increase in GDP is expected to be only modest (0,75%). Whilst exports remained sluggish, reflecting both their country and commodity composition, domestic private demand expanded at a fairly strong rate. Consumers' expenditure, which had been falling steadily since the end of 1980, picked up as a result of the slowdown in inflation, combined with a fall in the savings ratio, whilst wage settlements remained modest. Capital formation also recovered, following government measures taken in 1982 and the beginning of a revival of business confidence. Inflation decelerated to about 3% and the rise in unemployment virtually ceased in the autumn.

Prospects for 1984 point to a continuation of the recovery mainly led by domestic demand. Some slowdown through the year however cannot be excluded. The direct effects of government incentives to invest weaken; in addition, other factors determining investment such as capacity utilization

Table 5

Denmark: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2H [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	11,2	4,9	6,0	5,2	10,5	−2,2	0,7	10,2	1,1
1971-80	12,2	2,3	9,7	10,2	11,1	−2,9	0,0	11,3	3,8
1981	10,9	0,1	10,8	11,8	10,2	−3,1	−7,0	9,6	8,3
1982	13,6	3,4	9,9	9,8	11,0	−4,2	−9,1	11,7	9,7
1983 [1]	9,8	2,2	7,4	6,6	7,5	−2,2	−8,8	12,5	10,7
1984 [1]	6,5	1,2	5,2	5,4	5,5	−1,3	−7,8	7,5	11,8

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year. Until 1979: M2.

and interest rates are not expected to become favourable in comparison with earlier periods of recovery. The current moderate pace of wage settlements, admittedly, is helping to improve the depressed level of corporate profitability but is not providing direct short-term support to the level of demand in the economy. The continued modest rise in consumer spending expected for 1984 implies a further fall in the savings ratio. The balance of current account is projected to stay in surplus (0,75% of GDP) and inflation to remain at around 3%. Overall, GDP is expected to rise by 2% in 1984.

With regard to budgetary policy in 1984 and beyond, the authorities have announced their firm intentions to reduce both the share of public expenditure in GDP and the structural deficit. This is reflected in the decision to limit with regard to 1984 the growth of expenditure of the federation to 2% and the net borrowing of the federation to DM 37 340 million, slightly below the projected outturn for 1983 (taking account of lower Bundesbank profits to be transferred to the federation). At the level of general government net borrowing could well fall from DM 54 000 million (3,3% of GDP) in 1983 to about DM 37 000 million in 1984 (2,1%).

This deliberate strategy of consolidation of the general government account at a time of only modest growth prospects is designed to bring about a larger absorption of economic resources by the private sector. However, should there be clear indications that activity is weakening again, a temporary deviation from the projected path of consolidation could be contemplated, allowing the automatic stabilizers to support demand. If, however, satisfactory progress in reducing the budget deficit can be achieved notably as a result of favourable economic circumstances, it should be possible to lighten the tax burden somewhat as well as to pursue a more active investment policy. In any event a firm grip on subsidies and transfer payments should be maintained. Policies with regard to subsidies should pave the way for a more positive supply side policy shifting resources towards encouraging new technologies rather than to supporting declining industries. An expansion of public sector investment could also contribute to the sustained growth of private investment and the process of structural adjustment.

The tight stance of budgetary policy voted for 1983 may have helped the Bundesbank to announce its intention to steer the growth of the central bank money stock (CBM) within the upper half of the target range, set at 4-7% for the year to the fourth quarter of 1983. From the beginning of the year however CBM growth has been outside the target. As these developments were considered to be largely due to special factors (such as the effects of the transfer of Bundesbank profits to the federation, speculative movements related to the March EMS realignment and unusually high maturity payments from savings contracts), the Bundesbank refrained from taking measures which would have had adverse effects at an early stage of the recovery. Only in September, when it became very unlikely that the growth path of CBM would return within the target range, did the Bundesbank react by raising the Lombard rate in line with money market rates,

which had already increased in part in response to external developments.

Of great importance for the behaviour of fixed capital formation, in addition to interest rates, are developments in the labour market. Some progress has recently been made towards a better balance of relative factor incomes but it is important that the relation between wage settlements (in real terms) and the rate of growth of productiviy is such that returns on capital investment can be restored to satisfactory levels. In this respect, it is important that more consideration is now being given to the role that participation by company employees in future profit earnings could play in the process of wealth creation. On the other hand, at a time when the external and public sectors are not contributing to overall demand, the evolution of real wages should help to improve the propensity to invest.

While appropriate wage settlements are fundamental in re-establishing a growth oriented economy, they cannot solve in the short term the large imbalances in the labour market that have built up over the years. Specific labour market measures remain therefore of great importance, in particular those which improve training, incentives and mobility. Reductions in working time are now also being widely considered in the Federal Republic. There is as yet no consensus, however, of the effects of such measures, nor about the conditions under which they would be beneficial for the long run performance of the economy. If any generalized implementation of shorter working time would appear to be inappropriate, individual schemes could be negotiated at the level of sector or company, to take account of particular circumstances, such as the structural problems of the sector concerned, the cost and profit situation and the age structure of the workforce.

In *Greece* where economic policy is geared to reconciling the requirements of external adjustment with those of a recovery of investment, the improvement aimed for on these two fronts is not yet clearly apparent. Weak private consumption has been offset by stronger demand from general government, especially public investment but business investment has continued to be slack. Moreover, the real balance on goods and services has slightly deteriorated once again. Overall, the contradictory effects of these trends have resulted in a slight fall in activity in the first half of 1983, but some recovery is expected in the second half. As agricultural output fell sharply, gross domestic product for the year is unlikely to show any growth. The rate of consumer price rises has remained high at around 20% through the year.

Table 6

Federal Republic of Germany: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	8,4	4,7	3,5	2,9	8,6	0,7	0,5	10,4	0,8
1971-80	8,2	2,9	5,2	5,2	8,6	0,6	−2,2	9,8	2,8
1981	4,2	0,2	4,0	5,6	5,3	−1,0	−3,9	5,0	4,7
1982	3,7	−1,0	4,8	5,3	4,4	0,5	−3,5	7,1	6,8
1983 [1]	3,8	0,7	3,1	3,0	3,8	0,9	−3,3	7,5	8,6
1984 [1]	5,1	2,1	3,0	3,2	3,5	0,9	−2,1	5,5	8,7

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year.

For some time to come, economic policy must continue to give priority to improving the real balance of trade and, consequently, to developing competitive production capacity. In spite of some improvement in the terms of trade, the balance of payments on current account is still heavily in deficit, and the burden of foreign debt is still growing rapidly. The recovery of business investment, on which prospects for restoration of external balance heavily depend, looks uncertain. The efforts which must be made in this regard imply that there will be no significant recovery in private consumption in 1984, and that public consumption should be kept in check. They should also be geared more forcefully to containing inflationary pressures so as to reduce as quickly as possible the factors making for instability, which distorts behaviour, and, in particular, produce a cautious attitude on the part of private investors. In 1984, growth could amount to about 1,5% and inflation to an annual average of about 18% while the balance of payments on current account could once more show a large deficit, amounting to over 5% of gross domestic product.

Even such limited achievements imply a strict policy on the incomes side as well as in budget management. Wages policy in particular must be aimed at a reduction in real unit costs, by an appropriate limitation on the effects of indexation while avoiding as far as possible a further squeeze on wage differentials.

This policy should restrain both incomes and transfers, and the ultimate aim should be appropriate limits on the growth of households' real disposable incomes, without any reinforcement of tax pressure other than that resulting from more energetic measures to combat evasion. While the provisions adopted should make for better balanced public finance, they will not be sufficient to reduce the public deficit to a level commensurate with growth and price targets: less than 6% of gross domestic product in 1984 for the general government borrowing requirement, and less than 9% and 12% of GDP respectively for the gross financing requirements of the central government budget and the public sector. Although these figures are only about half a percentage point below the expected outturn for 1983, they will still be diffficult to achieve against a background of hesitant economic recovery. In particular, they imply a substantially slower rate of growth of real operating expenditure and an increase in public service charges large enough to lighten the real burden of subsidies to public sector firms.

The main reason why the public deficit must be reduced is that it is financed by highly inflationary means. Although liquidity is showing a growing tendency to settle spontaneously in savings deposits, disinflation in the economy will be all the more certain as the rate of monetary creation and the liquidity ratio in the broad sense decline. A smaller deficit would thus enable monetary policy to achieve its objective without imposing excessively strict limits on lending to firms. But disinflation also requires a firmer trend towards the stabilization of savings, and this can hardly be achieved without a gradual rise in real interest rates, which are still negative at present, in contrast to the general run of rates internationally. Some increase in real rates must now be encouraged, although cautiously, so as to avoid compromising the recovery of business investment, which is essential.

External monetary policy must be geared to helping the disinflation effort by keeping exchange rate depreciation in check as closely as possible.

In *France,* the measures adopted following the currency realignment of 21 March 1983 [1] reinforced the firm stance of economic policy. They reinforced the incipient decline in consumption followed after some delay by a halt of stockbuilding. Together with successive reductions in the exchange value of the franc, this produced an improvement in the trade balance, which shows a substantially lower deficit than in 1982. The rate of price inflation has also slowed down, and could average under 9% for 1983. However, with slightly recovering exports providing the only support, activity is loosing momentum and employment is contracting at a higher rate.

In view of the growing debt burden, the complete restoration of external balance is still some distance away. The present stance of economic policy will have to be maintained in 1984 therefore, pointing to only a weak recovery in activity during the year, and a positive but very low annual rate of growth. Nevertheless, substantial progress should be made towards establishing economic balance. The rate of increase of prices through the year should fall to well below the figure for 1983, and the trade balance should move out of deficit towards the end of the year.

The extent of such progress, which implies a further deceleration in costs and strict limitation of consumer demand, depends crucially on wage restraint. It depends particularly on maintaining the present wages policy which is directed towards separating the growth of incomes from previous price increases and rather to relate it to future developments, that is to say, leaving open the possibility of some catching-up at the end of the period, to the price increase eventually foreseen for the year. If this principle is applied, and if with virtually zero growth, a pause takes place in the indexation for the minimum wage, the growth of wages is likely to be strongly reduced compared with 1983.

Maintaining the restrictive stance of economic policy also means keeping the general government borrowing requirement to about 3% of gross domestic product, an aim which should be achieved by the draft budget for 1984 adopted by

[1] Followed by the granting of a Community loan of 4 000 million ECU to France.

Table 7

Greece: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	11,0	7,6	3,1	2,5	9,8	−3,1	:	17,6	:
1971-80	19,1	4,7	13,8	13,6	18,3	−2,7	:	23,8	:
1981	18,9	−0,7	19,7	24,4	27,1	−0,2	−10,1	34,3	4,1
1982	25,4	0,0	25,4	21,1	26,2	−3,8	−6,4	29,1	6,1
1983 [1]	19,5	−0,2	19,7	20,5	17,3	−5,0	−6,3	22,6	7,8
1984 [1]	19,7	1,5	17,9	18,5	18,5	−5,5	−6,3	20,2	8,7

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year.

the government on 27 September. Bearing in mind the lower revenue buoyancy, the continuing expansion of the burden of interest payments and the numerous factors contributing to an increase in the volume of social expenditure, this target implies a determined squeeze on expenditure and a further reinforcement of compulsory levies. Central government expenditure will at best remain constant in real terms—actually declining under a number of headings—except for expenditure on priorities such as employment, training, research and support for productive investment. Public investment and aid will suffer from restrictions but constraints will be especially tight on operating expenditure, limiting its rate of expansion to well below the average rate of price increases. The growth of social security benefits will also be strictly limited, in particular through the continued pursuit of efforts to curb expansion of expenditure on health and by making no real improvement in cash benefits that are not linked to the trend of wages. Even so, the additional effort required to increase revenue to the desired level—especially the revenue of social security schemes—will be very great, representing over 1% of GDP approximately equally distributed between taxation and social security contributions.

This strict discipline is indispensable to ensure that the economy as a whole is financed in a manner consistent with the aims of disinflation and restored external equilibrium. It must be accompanied by measures to achieve monetary growth commensurate with the outlook for nominal gross domestic product. Moreover, strict quantitative controls on credit and fairly high real interest rates will need to be maintained both to stimulate stable savings and to contribute to restoring the balance of payments position.

The present restrictive phase of economic policy should lay the foundations for the gradual improvement in business investment required for the restoration of durable external equilibrium and sustained growth. The positive effects of currency depreciation and cost reductions on firms' operating accounts will be the best guarantee of such improvement. The financial markets seem capable of responding satisfactorily to the need of business for a stable flow of capital. Finally, budgetary austerity deliberately does not affect such policies which, apart from general and sectoral tax incentives, involve large financial assistance, in particular capital grants for newly nationalized undertakings. It is thus reasonable to expect the first signs of a business investment recovery in 1984, particularly in the investment of industrial undertakings in the competitive sector, which have been lagging further and further behind over the years and consequently contributing to recent external trade difficulties. This recovery must be consolidated without compromising the emerging trend towards improved profitability. In particular, decisions on the financing of social security schemes and the adjustment of working hours must take this point into account.

The emerging signs of recovery in investment and growth trends are not such as to provide much hope of a spontaneous reduction in the disequilibrium between labour supply and demand in the near future. There is still scope, however, for an eventual reduction in the longer term. In particular, a labour force with training and qualifications that corresponded better to employers' needs could more easily take up the potential supply of jobs. More flexibility in working hours could be introduced, providing that the adjustment neither increases costs nor adversely affects capital productivity.

Overall, 1984 should be a year of transition marked by important progress towards restoring the overall balance in the economy and paving the way for sustained growth.

Economic activity in *Ireland* showed almost no growth in 1983 reflecting the unfavourable international conditions. There were however, definite encouraging features. The rate of price inflation, although still high, at around 11%, moderated significantly from the figure of 17,2% recorded in 1982. A marked improvement took place in the deficit on the current balance of payments which fell to less than 3% of GDP. The trend towards increasing budget deficits, particularly for current purposes, has been decisively arrested and Exchequer borrowing has been reduced by about 3% of GDP in 1983. On the debit side however, it must be remembered that the unemployment rate has continued to rise and at year-end may well approach 16%.

The outlook for 1984 points to a modest revival in economic growth. Foreign demand will be more buoyant but this is expected to be largely offset by the effects of the domestic deflationary forces, as there is little alternative to pursuing the current policy stance firmly over the medium term with a consequent lower level of consumption.

A number of factors are at the root of the present difficulties. Demographic changes are adding large numbers of young people to the labour force each year and, in the medium term, are putting increasing pressure on demand for basic social services. The long established policy of achieving growth and employment through the encouragement of export-based industry entails the need for considerable public expenditure, funded by borrowing, and the provision of essential infrastructure, both economic and social. The recession in international trade, and, until recently, in the UK market in particular, has meant that a full return could not be realized from the substantial investment made. Moreover, after the two oil shocks, fiscal policy remained expansionary, promoting short-term income generation to the detriment of the country's productive capacity. Attempts to maintain and increase real earnings despite adverse movements in the terms of trade, reduced the ability of many sectors in the economy to compete, and pushed the current balance into deficit in spite of a continued strong export performance.

Corrective action, taken vigorously in hand, has concentrated largely on reducing the Exchequer Borrowing Requirement and the authorities have committed themselves to phase out deficit spending for current purposes by 1987. In pursuing this objective, however, it is important to maintain an appropriate balance between tax increasing and expenditure cutting measures given their respective economic costs.

Table 8

France: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	10,2	5,6	4,4	4,3	9,4	0,2	0,4	12,7	0,9
1971-80	13,4	3,6	9,5	9,5	13,8	−0,4	−0,1	14,8	3,8
1981	12,1	0,2	11,9	12,9	14,5	−1,4	−1,8	11,4	7,8
1982	14,8	1,8	12,8	10,9	14,5	−2,9	−2,7	10,8	8,7
1983 [1]	9,5	−0,3	9,8	9,0	9,7	−1,8	−3,1	8,8	8,9
1984 [1]	7,7	0,4	7,3	7,2	8,2	−1,2	−3,3	6,5	9,7

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year.

Recent budgets have stressed large increases in the level and scope of taxation, while the current low level of activity reduces tax buoyancy; this suggests that a new general increase in taxation would not be appropriate in 1984 but that attention should now be directed at achieving significant real cuts in expenditure. Pressure on scarce Exchequer resources is likely to continue, principally because of the continuing high level of interest charges on the accumulated national debt and increasing demand for social expenditure. Great efforts are therefore necessary to reduce both current and capital spending programmes. It would seem appropriate to reduce the Exchequer Borrowing Requirement in 1984 by 1-1,5% of GDP by reference to the likely outturn for 1983 and on the basis of the current budgetary definitions.

It is of first importance that the authorities continue and intensify their efforts to achieve wage moderation. This is significant not only from the point of view of containing public expenditure, of which wages costs form a major part, but also from the point of view of protecting employment.

Monetary policy is designed to support the adjustment being pursued through fiscal policy, without itself imparting an independent and additional deflationary bias to macroeconomic policy. Give a favourable external environment, continued success in curbing domestic inflation and in reducing the current external deficit might facilitate some further lowering in interest rates. At the same time, an important continuing concern is to finance as large a proportion as possible of the Exchequer deficit from domestic sources.

Efforts to ease the labour market problems more directly in 1984 should concentrate on improving the flexibility of the labour market and encouraging the ending of overtime working while giving special attention to youth unemployment.

In *Italy,* new tax provisions and public service charges introduced at the beginning of the year and the difficulty in reaching new national labour agreements have tended to keep domestic demand and activity weak, the only dynamic factor being the marked improvement in exports. This helped to restore external balance which should be more or less realized for the current account by the end of 1983. It has also slowed inflation down considerably, and the average monthly rate is expected to be less than 1% in the second half of the year.

From now on, the various demand components should tend to expand, and activity should strengthen. The expected recovery of consumption, which should continue into 1984, might have been strong enough to interrupt the current but as yet insufficiently marked trend towards restored balance, particularly while the adverse inflation differential, in relation to the other industrialized countries, is still eroding competitiveness. To control the recovery and ensure that it is lasting, anti-inflationary policy has therefore to be actively pursued by an optimum combination of the three instruments available: concerted incomes and prices restraint, holding down the public deficit and monetary rigour. If all the available soope of these instruments is fully exploited, growth of about 1,5% can be expected in 1984, while payments on current account should remain more or less in

Table 9

Ireland: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	9,9	4,2	5,5	4,6	9,9	−2,3	−2,7	10,4	4,5
1971-80	18,3	4,1	13,6	13,8	18,0	−4,6	−8,1	18,5	7,4
1981	19,0	1,1	17,7	19,5	18,5	−13,1	−15,8	17,4	10,2
1982	18,3	1,2	16,8	17,1	14,9	−8,3	−16,2	12,9	11,7
1983 [1]	11,2	0,5	10,6	11,0	12,2	−2,6	−13,4	14,4	14,6
1984 [1]	10,1	1,8	8,2	8,8	8,9	−0,6	−11,8	14,4	16,6

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year.

balance and the rate of consumer price inflation in the 12 months to December should come down to under 10%.

Progress will depend firstly on whether incomes and prices policy can succeed in slowing down the wages and prices spiral as far as possible, along the lines of the tripartite agreement of 22 January 1983 on wages and working conditions. This means not only that the limits set for increases of wage rates for 1983 and 1984 must be rigorously observed (as, by and large, they have been till now), but also that deliberate measures to slow down the effects of indexation mechanisms must be taken as far as is feasible; for example by linking remunerations to planned rather than to observed inflation. The recent agreements between government and the professions to stabilize the prices of some essential goods and services should help to guide nominal trends in the desired direction.

However, the greatest effort will be required on the public finance front. Because of the automatic nature of increases in a large proportion of expenditure—notably social security expenditure and interest payments—and in view of the once-off nature of some of the tax provisions introduced to contain the deficit in 1983, the deficit for 1984 once again tended to show a large rate of increase, whereas a declining deficit would be necessary to foster disinflation. A further effort much more energetic than that made in 1983, has thus been agreed on to limit the deficit to an amount compatible with macroeconomic objectives, i.e. about 10% of gross domestic product for the general government borrowing requirement and less than 15% of GDP for net Treasury borrowing, which also includes financing operations. The reduction of the deficit again should be achieved partly through measures affecting revenue, both permanent measures, and, once more, temporary measures. But to keep the expansion of the tax burden within certain limits, it has been decided that this time a fair share of the effort would be borne by expenditure, involving major savings on government general services, expenditure on health and pensions.

The restrictive stance of monetary policy must be maintained, in a new effort to lower the liquidity ratio, which once again rose in 1983. Therefore, the financing norms for the economy should be defined from 1984 onwards in terms not only of total domestic credit, as heretofore, but also of money supply growth. A further substantial increase of public issuing of government securities will be essential to achieve these aims. This implies that real interest rates must remain definitely positive, in line with the international trend.

Demand management as outlined here should create appropriate conditions to help the economy to face its structural problems. The most serious of these is clearly the steady increase in unemployment which bears witness to an inadequate control of costs, the chronic weakness of productive investment, and the growing proportion of investments in labour saving capacity. It is therefore essential to make cost control and employment policy compatible on a lasting basis: this means long-term wage restraint, which can be achieved if the opportunities provided by the agreement of 22 January are used to improve profitability and not simply

Table 10

Italy: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	10,5	5,7	4,5	3,8	10,7	1,8	−2,3	13,3	5,2
1971-80	18,3	3,1	14,7	14,6	18,4	−0,2	−8,0	19,5	6,0
1981	17,4	−0,2	17,6	19,0	22,0	−2,3	−11,7	16,0	8,8
1982	17,1	−0,3	17,5	16,7	17,1	−1,6	−11,9	17,2	8,7
1983 [1]	14,1	−0,8	15,1	15,0	15,6	−0,4	−11,9	16,0	9,0
1984 [1]	12,0	1,5	10,4	11,5	12,4	−0,2	−10,0	11,0	9,4

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year.

to push ahead with disinflation. Special care will be required here to ensure that the benefits to be expected in the medium-term from limiting agreed increases are not compromised by wage drift or shortening of work time with adverse effects on unit labour costs.

In view of the need to restructure the system of production so as to improve competitiveness and employment trends, the gradual reduction of the public deficit is a priority. This reduction is necessary not only to avoid financial crowding out of private firms, but also, and especially, to impose a more efficient distribution of public expenditure and more generally to improve resource allocation. The effort should thus be concentrated on public expenditure by subjecting the management of departments of the social security system as well as public and semi-public enterprises to stricter efficiency criteria. In the medium term, measures to reduce the deficit should avoid as far as possible a further increase in the burden of taxation and contributions unless parallel steps are taken towards a more equitable tax system.

In *Luxembourg*, economic activity in 1983 has been affected by the steel crisis and the slackness of domestic demand. Gross domestic product in real terms fell by 2,4%. Despite wage restraint in the steel sector and the temporary suspension of wage indexation, prices have continued to rise fairly fast, not only because of the delayed effects of the devaluation, but also because of the increased rates of value-added tax.

Economic activity will probably remain slack in 1984. On the export side, the outlook for Luxembourg's main industries is not very bright; moreover, although the limitation of wage indexation in 1984 to a single adjustment will improve profitability in Luxembourg firms outside the steel sector and contribute to restructuring within the sector, it will also damp down private consumption.

The law of 1 July 1983 on restructuring the steel industry is intended to reduce production capacity in such a way as to avoid intolerable financial and social consequences in a country where steel is a major industry. The government's priority is to reconstitute a vigorous and internationally competitive economic structure. The strategy is based on wage restraint paralleling that in the competitor countries, but continued strict budget policy must also be given an important role. The net public sector borrowing requirement has again increased considerably in 1983 as a result of exceptional measures to aid the steel sector. The improvement in the central government borrowing requirement expected in 1983 (a reduction from 4,9% of GDP in 1983 to about 1% in 1984) due to increased revenue designed to offset extra expenditure on the steel sector, implies also a constant effort to hold expenditure down, and if necessary further compensatory measures should be taken.

In the *Netherlands*, budgetary restrictions and wage restraint in the private sector contributed to a further considerable reduction in domestic demand in 1983. On the other hand,

Table 11

Luxembourg: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	7,6	3,6	3,9	2,5	6,7	7,1	1,6	:	0,1
1971-80	9,5	3,0	6,3	6,7	10,5	18,5	2,0	:	0,3
1981	6,5	−0,3	6,8	7,7	8,3	31,1	−2,3	:	1,0
1982	6,7	−1,1	7,9	10,0	6,9	38,8	−2,0	:	1,2
1983 [1]	5,6	−2,4	8,2	8,4	7,1	37,2	−2,9	:	1,8
1984 [1]	6,3	−1,0	7,4	7,7	5,9	36,3	−1,5	:	2,4

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year.

the favourable trend of costs enabled Netherlands' exporters to take advantage of the slight improvement in world trade. Thus, after declining by a total of 2,9% in 1981 and 1982, economic activity remained stable in 1983. Nevertheless, unemployment expanded considerably, mainly because of a large increase in the labour force. In 1980, the unemployment rate at 4,7% was well below the Community average; by 1983, however it averaged 15,6%, compared with a Community rate of 10,4%. Nevertheless, the inflation rate fell to about 2,8% on average for 1983, and the balance of payments surplus on current account, which was already large in 1982, should amount to the equivalent of 3,3% of gross domestic product this year.

The world economic recovery will improve the Netherlands' exports in 1984, but domestic demand, especially private consumption, is liable to decline once more. Real gross domestic product will not grow in relation to 1983, and the rate of unemployment will rise further to about 17,6%. Inflation will remain fairly low. In view of the slackness of domestic demand, the current balance of payments surplus will increase once again.

The choice of economic policy guidelines is not easy against this background. The growing surplus on the balance of payments on current account, the firmness of the guilder on exchange markets, the large surplus of savings in the private sector, the slackness of investment, the stability of prices, the high rate of unemployment and the low rate of capacity utilization, all indicate that the economy could deal fairly smoothly with much more vigorous domestic demand. For example, while wage restraint—involving virtually no change in *per capita* remuneration in 1984—is regarded as necessary to maintain competitive capacity and to improve the profitability of firms and the climate for investment, it may, if taken too far, exercise an excessively restrictive effect on final demand. On the other hand, there would no doubt be major objections to the use of budgetary policy in promoting recovery.

The scope for action on the public finance front is particularly narrow because the borrowing requirement has ballooned over the past few years. Indeed, it has doubled in three years, and the expansion is likely to gain momentum if new suitable measures are not taken. The situation is the more alarming as the pressure of taxation, social security contributions and public service charges, the greatest in the Community, is increasingly eroding both real disposable private income and business profitability. There is no alternative to pursuing a policy of budgetary austerity, especially as tax revenue is expanding only very slowly because of slack economic activity and low inflation, revenue from natural gas is tending to stabilize, and some items of expenditure, notably on unemployment, are still growing rapidly. The draft budget for 1984 once again includes a programme to reduce expenditure by over HFL 10 000 million, mainly on public service remuneration, social security and public health. The draft budget also provides for a reduction of HFL 2 000 million in the burden on enterprises and new revenue amounting to about HFL 3,000 million, with very little change in the total burden of taxation. The net borrowing requirement of central government and local authorities, on national definitions, should be reduced to 12,4% of net national income in 1983 and to 12,1% in 1984. This should make it easier to lower interest rates—which in real terms are still among the highest in the Community—and stimulate productive investment.

In the medium term, the strategy adopted is expected to promote growth by improving competitiveness, thus boosting exports, and by improving profitability so promoting investment. It will not, however, prevent a further rise in unemployment in 1984. Special attention is thus called for to explore ways of reducing working hours and increasing labour mobility without increasing labour costs.

In the *United Kingdom* economic activity has expanded relatively quickly in 1983 (GDP growth 2,8%), faster than at any time since 1978, and at a rate significantly above the Community average. The principal reason for this has been the strength of private consumption, with consumers' propensity to save continuing to decline and consumer price inflation falling to 5-6%. In addition, the long period of destocking, lasting from 1980 to 1982, has come to an end. However, the impact of these developments on domestic output has been limited by substantial growth of imports, while there has been no increase in export volumes. The underlying trend of unemployment is still upward, although at a slower rate than in recent years. Fiscal developments have largely been in line with official plans, but some monetary aggregates have been growing at rates outside the target range despite high real interest rates.

It is likely that growth will continue in 1984, but perhaps at a slightly slower rate than in the current year, about 2-2,5%. The expansion of private consumption is expected to slow down, and this will not be fully compensated by faster growth of investment and exports. Manufacturing output should increase somewhat faster than in 1983, but there is some risk of a further increase in unemployment. Wage settlements and price inflation are likely to remain close to current levels.

In the last few years, the UK economy has gone through a period of considerable structural adjustment, partly as a result of the development of North Sea oil and partly through policies designed principally to bring about a rapid reduction in inflation. As these adjustments coincided with a period of international recession, their effects on domestic demand, output and employment were even greater than might otherwise have been expected. Despite the recovery now underway, the level of GDP has only just returned to

Table 12

The Netherlands: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	10,6	5,2	5,2	4,1	10,6	0,0	−0,9	9,1	0,9
1971-80	10,7	2,8	7,6	7,7	10,7	1,3	−1,4	10,8	3,4
1981	4,3	−1,2	5,6	6,2	3,3	2,2	−5,2	5,2	7,1
1982	4,0	−1,6	5,7	5,7	5,7	2,7	−6,9	7,6	12,7
1983 [1]	1,9	0,3	1,6	2,8	3,2	3,3	−6,7	5,5	15,6
1984 [1]	2,4	0,0	2,4	3,6	0,1	4,4	−7,1	6,0	17,6

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year.

that already achieved in 1979, and a period of lasting growth would be necessary to reduce significantly the level of unemployment. The achievement of such growth will be helped by improvements obtained in industrial structure and productivity, and by the low levels of price inflation and wage settlements. Nevertheless, the outlook is still uncertain, because of the unbalanced nature of the current recovery, at least during its early phase, depending predominantly on consumer demand. As the UK moved out of recession earlier than its major trading partners, and owing to the relative weakness of the international competitive position, there has been a substantial worsening of the balance of payments, the balance of trade in manufactured goods having moved into deficit. Capital goods investment has as yet shown little response to higher demand, a factor which may have adverse supply side effects at a later stage of the cycle.

Consolidation of the improvements achieved in labour market conditions will be essential to the achievement of more balanced growth. The very large productivity gains during the recession helped to compensate, in terms of international competitiveness, for some of the exchange rate appreciation, but future gains are likely to be smaller. In order to encourage investment, a further redistribution of relative factor incomes is necessary, allowing higher rates of return on real assets. It is therefore important that there should be no acceleration of wage settlements, even if consumer price inflation increases slightly in 1984. Prospects for higher industrial output and employment in the longer term appear to be dependent upon a stronger competitive position obtained through wage moderation and, if indicated by market forces, some exchange rate adjustment.

During the last few years, monetary conditions have improved considerably, as inflation, nominal interest rates and the growth rates of the monetary aggregates fell from very high levels. The strength of consumer spending in the last 18 months, however, has been accompanied by a sharp increase in lending to the personal sector and some acceleration of monetary growth. At the same time, the level of real interest rates has discouraged borrowing by enterprises despite the expansion of demand. Even though monetary growth has been exceeding the target range (7-11% annual rate) set for 1983-84 in the Medium Term Financial Strategy (MTFS) published in March 1983, the stance of policy as revealed by other indicators has remained cautious and the authorities should perhaps consider some reduction in interest rates in order to encourage borrowing for investment and stockbuilding purposes. For 1984-85, the March 1983 MTFS set out a target range of 6-10% for the growth of the monetary aggregates. This appears consistent with the financial outlook for that period, particularly given the planned level of public sector borrowing, and should allow for some further modest downward movement of interest rates.

The trends in public finance in the current financial year are such that the Public Sector Borrowing Requirement (PSBR)

Table 13

United Kingdom: main economic aggregates, 1961-84

	GDP value growth	GDP volume growth	GDP price deflator	Rise in consumer prices	Compensation per employee	Current account of balance of payments	General government balance	Money supply growth M2 [3]	Unemployed in labour force
	%	%	%	% [2]	% [2]	% GDP	% GDP	%	%
1961-70	7,2	2,8	4,2	4,0	7,1	0,0	−0,7	5,9	1,9
1971-80	16,0	1,9	13,9	13,3	16,2	−0,7	−3,2	14,5	4,4
1981	9,9	−2,0	12,1	11,0	14,7	2,4	−2,9	14,6	9,6
1982	9,4	1,5	7,8	8,0	8,8	1,5	−2,1	9,3	11,1
1983 [1]	7,9	2,8	4,9	5,7	7,9	0,2	−2,2	10,6	11,7
1984 [1]	7,2	2,2	4,8	5,8	6,3	−0,2	−2,1	8,6	11,9

1 Preliminary estimate of the Commission services on the basis of present or anticipated policies.
2 % change over previous period, annual rate.
3 End of year.

should be relatively close to the target indicated in the MTFS (UKL 8 200 million or 2,75% of GDP). Measures were announced in July to help keep public expenditure in line with plans, but it remains possible that the outturn for both expenditure and revenue will be a little above planned levels. For 1984-85, the MTFS target for the PSBR, of UKL 8 000 million or 2,5% of GDP, represents a broadly unchanged fiscal stance, given the increase in revenue resulting from moderate growth of the economy. In view of the modest level of the targets in both the current and the next financial years, slightly higher levels of the PSBR could be tolerated.

In the longer term, there may be scope for lowering the relative level of public spending and therefore also the tax burden. It would be desirable to improve the structure of expenditure in respect of its productive element. This depends partly on the overall level of expenditure and partly on the achievement of sufficient economic growth, so that the categories of expenditure determined by demand in the economy, such as unemployment and related benefits, can be reduced. Possibilities for cuts in other spending programmes appear more limited, in view of demographic factors (the increasing average age of the population) and the low level of public investment in recent years.

Annual Economic Review 1983-84

(Submitted for information to the Council, the Economic and Social Committee and to the European Parliament, together with the Annual Economic Report 1983-84)

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1. Economic problems and policy issues for the Community

A recovery in economic activity in the Community is now underway but it will be modest and vulnerable to increases in interest rates and will hardly be fast enough to induce a lowering of unemployment. The medium-term outlook for output and unemployment is discouraging. The 1981/82 recession proved to be more prolonged than expected, to a large extent due to the fact that monetary policy since 1981 has, in large degree and virtually unavoidably, replicated the interest rate conditions prevailing in the United States. Since mid-1982 real money supply growth in Europe has been more accommodating than in 1981/82. There are, however, narrow limits to the scope for using monetary policy actively to stimulate demand as long as government budget deficits are as high as at present and in many Member States inflation performance remains less favourable than that of United States and Japan. The present straitjacket on macroeconomic policy can only be lifted through supply policies, positive adjustment and, notably, new and substantial steps forward to strengthen the internal market and increase the monetary cohesion of the Community. A combined micro-macro approach is needed. A feasible framework for economic policy is one where financial policies (budgetary and monetary policy) are decided upon with reference to the need for greater convergence within the Community while the micro-policies (allocative and supply policies) address the problem of improving the split between the real component and the inflation component within a given rate of growth of nominal GDP.

1.1 Outlook and economic performance

After the failure of economic recovery in the Community to materialize in 1982, short-term forecasts (Chapter 2) suggest an upturn in output may now be getting under way. However, against a background of high real interest rates, tightening budgetary policies in most of the Community countries and a weakness of world trade partly attributable to the debt problems of developing countries, the recovery in the Community is likely to be slow and hesitant, certainly by comparison with the growth rates expected for the US and Japan in 1983 and 1984. Moreover, the potential recovery in the Community is likely to be very fragile and could easily be knocked off course by an adverse movement in, for example, interest rates.

Medium-term projections (section 2.3) are hardly more encouraging. The central projection, assuming an unchanged dollar/ECU exchange rate from 1984 onwards, budgetary policies unchanged from present announcements and broad stability of US long-term interest rates, suggests that real output in the Community might grow at an average annual rate of 1,9% between 1982 and 1987. Such a growth rate would allow unemployment to decline slightly from a peak reached in 1984 and 1985, but the unemployment rate would still be as high as 10,4% in 1987.

A particularly disturbing feature of the current recession has been the marked weakness of investment, one of the principal factors determining production potential (section 2.4). The danger that the present recession might lead the Community into a 'low-growth trap' is one which cannot be ignored.

The process of disinflation in the Community continues. The rate of increase of labour compensation per head in the Community, perhaps the soundest indicator of the underlying inflation rate, has decelerated smoothly in each of the three years since 1980. The deceleration is expected to continue in 1984.

The steadiness of the deceleration in labour compensation per head has been rather obscured by sharp movements in other price-determining factors: suppliers' export prices, exchange rates, profit margins and indirect taxes. The initial effect, most marked in 1981, of the sharp upward movement of the dollar was to increase the prices the Community had to pay for its imports from the rest of the world. Later, however, world prices in dollars fell sharply, so that in the latter half of 1982 import prices were having a considerable dampening effect on inflation in the Community. The interplay of these various factors is considered in some detail in Chapter 3.

Labour market developments, which have a crucial bearing on the interpretation of the current situation and of the

short-term and medium-term forecasts, are analysed in Chapter 4. This chapter shows that labour demand in the Community had been growing only slowly for a long period of time before the onset of the present recession (ever since 1963, in fact), a slower growth of output between 1973 and 1980 being matched by a slower growth of productivity. Labour supply, however, has been growing considerably more quickly since 1973 as a result of demographic factors. The almost uninterrupted rise in unemployment since 1973 was sharply aggravated from 1981 onwards by falls in employment as the recession developed. In 1983 the unemployment rate in the Community is likely to reach 10,4%, and is forecast to rise even further, to 10,9%, in 1984. No easing of the demographic pressure on the labour market can be expected before 1986, but thereafter the annual rate of growth of the working-age population will fall off sharply (to less than 0,1% a year between 1986 and 1990).

The effects of the continuing recession combined with those of heavy interest payments are clearly to be seen in the difficulties encountered in the Community in containing budget deficits (Chapter 5). The tax burden in the Community will probably have risen quite substantially in 1983. However, this will have been about offset by a rise in transfer payments (including unemployment compensation) and interest payments from general government as a proportion of GDP, with little change elsewhere in the accounts, leaving the budget deficit in the Community, as a proportion of GDP, much the same as in 1982. For 1984 a further substantial rise in the tax burden seems likely. Total expenditure, in contrast, may rise slightly slower than nominal GDP, and, as a consequence, the budget deficit is forecast to be reduced from 5,4% in 1983 to 4,7% in 1984.

During the period from 1980 onwards, the rate of growth of the broadly-defined money supply in the Community has been significantly lower than the rate during the 1970s and a further deceleration is forecast by the Commission for 1983 (Chapter 6). On the assumption that the realized deceleration has been matched by a similar downward revision of the expected trend rate of money supply growth on the part of economic agents, the desired liquidity ratio of the economy will have risen (velocity will have fallen). A rise in the actual liquidity ratio in the Community has in fact already taken place.

Trends in the Community's external competitiveness, together with the process of balance of payments adjustment are examined in Chapter 7. The Community as a whole suffered a very substantial loss of competitiveness during the period 1977-80. Since then, however, almost all the competitive loss has been recouped, largely as a result of movements in nominal exchange rates. By contrast, US competitiveness, after a strong improvement in the second half of the 1970s, deteriorated by one-third between 1980 and 1983. Japanese competitiveness has improved strikingly since the second oil-price shock. These trends perhaps indicate that, while a substantial movement of the real exchange rate of the ECU against the yen might be justified, a further substantial real appreciation of the dollar against the ECU would be uncalled for on competitiveness grounds (although it might have to be accepted for other reasons—see below).

While these changes in competitiveness among the industrialized countries have been taking place, the industrialized countries as a group have been seeing their share in total world trade decline, to the profit of the non-oil developing countries (section 7.3). In the absence of a decline in the industrialized countries' terms of trade or of a major effort of structural adjustment, this trend is likely to continue. In a sense, the decision has already been partly made: the industrialized countries reacted to the two oil-price shocks by reducing savings and investment, while the non-oil developing countries were able to maintain an expansion of investment by increasing their savings substantially and by allowing a rise in their external deficit with resulting financial exposure due to the rise in the servicing of external debt.

In general the operation of the EMS, (Chapter 6) has been such as to prevent the sharp swings in nominal exchange rates which have been so prevalent outside the system in the period since its inception. However, it is only fairly recently that there has been evidence of some convergence of underlying policies in the participating currencies such as might ensure that relative stability of nominal exchange rates could be combined with more convergent inflation performance. The absolute spread of inflation performance even among the members of the EMS remains very wide, and is wider still if Greece is brought into the comparison.

1.2 The causes of the Community's weak economic performance

Although an economic recovery now seems to be under way in the Community there is little comfort to be gained from the short and medium-term forecasts and there is every reason to explore all realistic options allowing an improvement of the economic performance and particularly a reduction in unemployment. But the remedy or the remedies—if available—clearly must be selected in accordance with the diagnosis of whether the current economic problems are due to:

(a) the stance of macroeconomic policy;

(b) international monetary and financial constraints;

(c) structural adjustment problems in Europe.

Each of these potential causes will be examined further below.

(i) *The stance of macroeconomic policy*

As shown in Chapter 5 the general government borrowing requirement as a percentage of GDP for the Community as a whole, despite the stagnation of economic activity, was stable in 1982 and rose hardly at all in 1983. This apparent overall stability of the budget balance, however, is the result of divergent movements of the main components: interest payments rose from 3,0% of GDP in 1981 to 3,8% in 1983 while the borrowing requirement excluding interest payments was reduced from 2,2% to 1,6%. Governments have indeed made considerable efforts to raise taxes and compress other expenditure categories to keep overall borrowing within acceptable limits. A measure of the effort accomplished in this respect is given in Table 5.6 in Chapter 5, showing that discretionary policy measures reduced the budget deficit by 1% of GDP in both 1982 and 1983.

The strict stance of budgetary policy was partly the result of policies to dampen the growth of public expenditure in the medium-term and partly a response to the very pronounced increase in the level of real interest rates in the last few years which made measures to dampen the growth of other expenditure even more urgent than before, notably in countries where the level of public debt had already reached sizeable proportions. This interest rate increase was instrumental in limiting the depreciation of the European currencies against the dollar in the face of high interest rates in the United States and the consequent increase in the flow of capital towards the latter country. Consequently real *ex post* long-term interest rates in the Community were by 1981 much higher than on average for the period 1973 to 1980 and this increase in market rates was reflected in a substantial increase in the average real rate of interest paid on public debt.

(ii) *International monetary and financial constraints*

The interest rate increases resulting from the rise in the US budget deficit, however, have also hit the Community indirectly due to the sharp reduction in imports by many of the LDCs which—in some cases as a result of internationally-negotiated adjustment programmes—have cut down severely on their imports of goods and services in order to make room for the rise in the burden of servicing foreign debt (Chapter 7). It is extremely difficult to produce exact quantitative estimates of the effects of this slower world trade growth. A Comet simulation suggests that if the growth of world trade is temporarily cut by about 2 points this causes a GDP loss of some 0,5 percentage points for the Community as a whole in the second year, rising towards 1% if the weaker trend is maintained. In addition to being affected by the interest rate increase, some LDCs were also hit in 1982 by falls in commodity prices. Although this resulted in some improvement in the terms of trade of the Community, it added to the financial difficulties of some of the most exposed countries in the Third World (see Chapter 2).

(iii) *Structural adjustment problems in Europe*

Apart from these international problems, it should be kept in mind that the trend rate of growth in the Community in the 1973-80 period had already fallen to close to 2% despite the fact that the real long-term rate of interest on average for this period was as low as 0,2%, or much less than the 1,9% seen on average from 1960 to 1973. [1] Indeed, many of the more fundamental adjustment problems and other structural and distributional issues which have often been discussed in the debate on economic performance after the first oil-price shock do not appear to have been brought closer to a solution in the last few years.

At a first glance the most serious adjustment problem of the 1970s, the need to reduce the dependence upon imported oil, has been handled much more successfully than imagined 10 years ago. The share of oil in domestic energy consumption in the Community was already down to some 47% in 1983, and the Council's objective, to reduce the degree of dependence to 40% by 1990, thus seems to be within reach. The reduction of dependence upon oil is to some extent attributable to the slowdown of economic growth rather than to a strong effort with respect to energy conservation and might in part be reversed if activity rose buoyantly. Nevertheless, for the time being energy supply seems to be much less of a constraint on economic growth than assumed some years ago, and even a somewhat higher rate of economic expansion in the Community could probably be accommodated without major tensions in the oil market.

On the other hand, there are signs that the Community is lagging seriously behind the United States and Japan with respect to the introduction of new technology and new methods of production. Moreover, a multitude of laws and regulations keeps firms from taking full advantage of the scope for increasing productivity. Inefficient production

[1] Conventionally, real rates of interest are often measured by deflating current levels of nominal interest rates by the rate of increase in consumer prices over a recent past, the assumption behind this estimation being that financial markets tend to project the most recent rate of inflation into the future. Available data on the real rate of interest on indexed bonds, for example in the United Kingdom, however, show that markets generally take a much more rational view of the future rate of inflation and that as a result the underlying anticipated real rate of interest is more stable than the apparent *ex post* rate measured as indicated above. The present level of nominal interest rates might thus be taken rather to indicate that financial markets expect the rate of inflation in the medium term to be higher than the one currently measured in the industrialized countries on average.

lines are kept in operation through subsidies and other aid programmes and in most Member States the weight of the public sector in the economy has grown to such proportions that thrift and investment are seriously hampered by excessive taxation on employment and income. During the 10 years from 1973 to 1983 public expenditure for the Community on average rose from 40 to 52% of GDP or by 1,2 percentage points by year. The relative decline of the productive sectors has clearly led to a slowdown in the overall growth of productivity and output in the economy and may also have exerted a negative influence upon business investment. Moreover, the rise in public expenditure in proportion to GDP has taken place in expenditure categories such as social transfers which are not conducive to employment and economic growth. Expenditure on R & D, development aid, public investment, etc. has been severely squeezed and has even in some cases fallen in absolute terms.

However, there also seem to have been specific constraints on economic growth in the Community attributable to the fact that the Community's enterprises are not able to exploit the potential economies of scale of the internal market fully, notably in the field of new technology and in the service industries.

While considerable progress towards economic integration took place in the first 15 years of existence of the European Economic Community the subsequent 10 years have seen very modest advances—even when account is taken of the creation of the European Monetary System. Public markets are still to a considerable extent reserved for national enterprises; firms with a European dimension are forced to confine their sales and service operations within national frontiers, leading to an uneconomic use of resources. Although the movement of goods between Member States is

Table 1.1

Key macroeconomic indicators for the Community

	1960-73	1973-80	1981	1982	1983 (estimate)	1984 (forecast)
Gross domestic product			*% change*			
Volume	4,6	2,2	−0,4	0,4	0,5	1,4
Deflator	5,0	10,9	9,1	9,1	6,3	5,1
Value	9,9	13,4	8,6	9,5	6,9	6,6
			%			
GDP gap (volume) [1]	—	—	−0,2	−1,1	−2,0	−2,0
Money and interest rates			*% change*			
Money supply (M2/3) [2]	11,4	13,3	11,9	11,1	10,5	8,7
			%			
Short-term interest rate	5,5	9,8	14,6	12,8	10,0	9,5
Long-term interest rate	6,9	11,1	14,7	13,5	11,8	10,8
Short-term interest differential rate [3]	0,9	2,2	0,6	2,2	1,0	−0,5
Changes in budget balance [4]			*% of GDP*			
Total change	—	—	−1,7	0,0	−0,2	+0,7
of which due to:						
Change in activity	—	—	−1,3	−0,7	−0,6	−0,1
Change in net interest payment	—	—	−0,5	−0,3	−0,5	−0,3
Residual change	—	—	+0,1	+1,0	+1,0	+1,1
Costs and income distribution			%			
Labour income ratio [5]	74,5	76,3	77,2	76,4	76,0	75,4
			% change			
Relative unit labour cost (manufacturing) [6]	2,1	2,2	−13,7	−5,8	0,3	3,0

1 Percentage difference between actual and the trend level of GDP (break in trend in 1973 and in 1980). Trend rate of growth from 1980 estimated at 1,4%.
2 Annual averages.
3 EC average over the New York rate.
4 See Chapter 5 for details; − = increase in deficit; a positive residual change indicates discretionary policies to reduce the budget deficit.
5 See Chapter 3.
6 In common currency terms.

in theory free, the administrative burden involved in shipping commodities from one country to another within the Community is no different from, and in some cases even more complex than, the routines to be followed when exporting to a third country. According to recent estimates the annual cost of red tape at the Community's internal frontiers may amount to above 0,5% of the Community's GDP or almost as much as the total cost of the common agricultural policy. The total cost of trade barriers, national protectionist policies and aid schemes is several times the total budget of the Community.

It is impossible to estimate how much of the 4,4% annual growth in productivity in the Community from 1960 to 1973 was due to the lowering of trade barriers within the EEC and EFTA but there is hardly any doubt that the effect was quite substantial. Since 1973 little further progress has been made in this respect apart from the temporary effects of the entry of Denmark, Ireland and the United Kingdom. One cannot rule out the possibility that somewhere between 0,5 and 1 point of the 2,3 percentage points slowdown in productivity growth since 1973 is attributable to the failure to make further substantial progress with respect to lowering the various national barriers in the internal market.

The past 10 years have seen a substantial decline in the profitability of investment and of the volume of investment in proportion to GDP throughout the Community. In fact, both the first and the second oil price shock resulted in very large terms of trade losses and a considerable change in the structure of relative prices. In sharp contrast to developments in the United States, wage and salary-earners in many Community Member States did not suffer substantial real income losses: as shown in Chapter 3 real *per capita* compensation of employees in the years 1980 and 1981 rose by 1,5 and 1,3% respectively despite terms of trade losses of 3,5 and 6,8% for the Community as a whole in these two years. The labour income ratio consequently rose steeply and the profitability of investment, which in most Community Member States had been on the rise again from the low levels of 1975, saw a new decline in 1980 and 1981.

Employment and growth in the Community was also hampered by a considerable deterioration of the international competitiveness of the Community's enterprises: unit labour cost during the 1970s rose faster than on average in competing countries and, in addition, the nominal effective exchange on average for the Community appreciated somewhat in the period from 1973 to 1980. These structural and distributive factors taken together are likely to have contributed importantly to the particularly disappointing employment and economic growth performance of the Community. They have probably exerted a considerable effect on developments in 1982 and 1983.

1.3 The economic policy issues for 1984 and beyond

Some of the factors referred to above as possible causes for the stagnation of economic activity since 1980 are still in operation; others have been reversed or can at least be taken to be inoperative for the time being. The Community's competitive position in particular is now much better than three years ago (although the yen remains substantially undervalued against the ECU) and the forecasts for 1984 suggest that an improvement of the profit situation is under way. Considering the central medium-term forecasts there are, however, risks that some of the key assumptions may not be fulfilled. One such assumption is that the US long-term rate of interest will be broadly stable in 1983 and 1984 (Chapter 2). In fact, on present prospects there would seem to be some doubt as to whether this assumption will be fulfilled: the general government borrowing requirement in the United States is expected to remain high despite the cyclical upturn in the economy in 1983 and 1984. The international economic and financial environment may therefore be less favourable for the Community than currently assumed.

In the present situation, financial policy in the Community should be determined with a view to two fundamental—but, as will be seen, related—criteria:

1. The outlook concerning the potential rate of growth of output in the Community over the next 5 years;
2. Policy with respect to the US dollar and reaction to interest rate changes in the United States.

With respect to the potential rate of growth of output over the medium-term, the analysis in the preceding section suggests that, pending greater success in solving the structural adjustment problems, to allow the Community's business sector to take advantage of the continental dimension of the internal market and to shift productive resources into growth industries, there is only a rather slender prospect of substantially increasing the Community's medium-term rate of growth of output above the 1,9% currently estimated according to the Comet projections for the years 1982-87 (Chapter 2). It would be unrealistic and, indeed, dangerous to base macroeconomic policy decisions on a more optimistic hypothesis with respect to medium-term economic growth as long as the basic questions concerning structural adjustment and the development of the common market remain unsolved.

Within the context of a given rate of growth of potential GDP, and assuming that the level of the budget deficit and the higher level of profits in the United States over the foreseable future will exert an upward pressure on interest

rates, several hypothetical combinations of budgetary and monetary policy stance may be considered:

	Monetary policy aims	
	Target for the ECU/dollar rate	Floating of the ECU/dollar rate [1]
Budgetary policy restrictive	A. Both budgetary and monetary policy restrictive	C. Budgetary policy restrictive but monetary policy accommodating
Budgetary policy stimulating demand	B. Budgetary policy expansionary but monetary policy restrictive	D. Budgetary policy expansionary and monetary policy accommodating

[1] Monetary policy assigned to domestic objectives.

Policy option A (both budgetary and monetary policy restrictive) represents the policy stands broadly taken by the Community in 1982 and part of 1983. Subsequently, however, the policy mix has moved towards option C with a somewhat more relaxed stance of monetary policy reflected in the preparedness of the Bundesbank to let the growth of central bank money move temporarily above the target range and to let the level of short-term interest rates remain relatively low even after the March realignment in the European Monetary System. Option B—involving a relaxation of the stance of budgetary policy—would imply a broad alignment of the Community on the policy stance in the United States and would thus, as far as its economic impact is concerned, be very similar to a scenario of generalized fiscal expansion. The cyclical upturn in the world economy would probably be even faster than is now the case but its composition as between consumption and investment would be compromised and the risk of rekindling inflation would be substantially higher. This risk would be even higher still under the—relatively unrealistic—hypothesis that a more relaxed stance of budgetary policy in the Community was accompanied by a monetary stimulus (option D).

Considering now these four 'stylized' policy options with their advantages and drawbacks, a central question in the design of economic policy for 1984 is to what degree Member States individually or as a group have a free hand to pick the combination of macroeconomic policies they might want, and in particular whether a relaxation of the budgetary policy stance would be desirable.

As shown in Chapter 5 the current stance of budgetary policy appears compatible with stability of the public debt burden in proportion to GDP in the medium term. However, this assessment is only a central estimate within a very wide range depending upon, in particular, the view taken with respect to the scope for GDP growth over the coming years and to the amount of government financial transactions which ought to be taken into account when estimating the structural budget balance. The less optimistic the assumption concerning GDP growth over the next few years and the larger the amount of financial transactions to be included, the larger the structural budget deficit would be.

Moreover, the budgetary policy stances of the individual Member States show very considerable divergence from one country to another with, in particular, an excessive level of monetary financing in several countries and a very large structural deficit in others. Only the FR of Germany and the United Kingdom are in a relatively healthy financial position and in both cases this reflects considerable efforts in recent years to dampen the growth of public expenditure. Belgium, Denmark and the Netherlands appear to record a very large structural budget deficit; Greece, Ireland and Italy manage to keep the public debt in check only through very heavy monetary financing with resulting inflation. France is in a middle position as between these groups of countries.

A shift to a less cautious budgetary policy stance, even if implemented within the framework of a coordinated policy initiative within the Community, would represent a reversal of the policy stance now adopted in most Member States and might have unfortunate effects on financial markets' anticipations. Moreover, in the majority of Member States a relaxation of efforts to compress public expenditure would probably result in a further aggravation of the medium-term adjustment problem and endanger the stability of the European Monetary System.

With a continuation of the current fairly cautious budgetary policy the upturn of activity in the Community is, however, likely to remain more timid than in the United States. However, the resulting slowdown in the rise of public debt and the restoration of balance in financial markets in the Community would be likely to allow a progressive reduction of interest rates.

In fact, with the Community deliberately choosing not to replicate the budgetary policy stance of the United States, monetary policy in the Community could aim to go as far as possible in relaxing monetary conditions without undermining the prospects for a declining inflation rate, while the ECU/dollar exchange rate could be allowed to adjust itself to market conditions (except for efforts to smoothen erratic fluctuations).

Even with a relatively rapid reduction of interest rates in response to a lowering of budget deficits in the Community, the resulting strengthening of private sector demand would probably take somewhat longer to come through. On the other hand, the upturn once under way would be soundly based in a recovery of productive investment and competitive

employment in the private sector in the medium term. The speed and profile of the upturn, however, would depend not on the stance of budgetary and monetary policy but rather on the accompanying structural adjustment policies. In fact, the more rapidly the basic medium-term adjustment policies are carried out and the more successful they are, the greater the degree of flexibility will be for the management of macro-economic policy.

As suggested in last year's *Annual Economic Report,* the combined micro-macro approach in economic policy calls for the setting up of a framework of policy management where financial policy (budgetary and monetary policy together) is set with reference to a medium-term trajectory for nominal GDP. This trajectory could, for example, represent the central no-policy-change forecast for the medium-term rate of growth of real GDP and the highest acceptable rate of inflation. Micro-policies in the widest sense—including efforts to dampen the increase in wage costs, supply policies, elimination of trade barriers and support to investment, etc.—would then address the problem of improving the split between the real component and the inflation component within a given rate of growth of nominal GDP.

Assuming that this approach is broadly followed over the next year or two—as recommended by the Commission in this year's *Annual Economic Report*—the most immediate policy issue for the Community would therefore be to make substantial progress on the micro-policy fronts and thereby gradually improve the conditions for non-inflationary growth. The key element of this policy would be measures to eliminate national subsidy schemes and protectionist systems, to open all national markets for competition from other Community countries and to make greater strides towards full exchange-rate stability within the Community.

The debate about nominal income norms

Last year's *Annual Economic Review* included, in Chapter 1, some discussion of monetary and budgetary policy with reference to norms, or reference trajectories, for the evolution of nominal income (or nominal GDP). In the course of the last year there have been a number of further contributions to economic policy analysis and debate on this subject. The following provides a general introduction to this subject in the context of a wider discussion of the relation between targets and instruments in economic policy.

Although there is an increasing degree of consensus that budgetary and monetary policy cannot in the short run or close medium term (the next two years) efficiently influence the split of a particular growth of nominal incomes as between real expenditure and the rise in prices, a high rate of real growth with the lowest possible rate of inflation must remain a fundamental objective of macroeconomic policy within the constraints given by environmental considerations, social policies, etc.

Ideally, therefore, governments would formulate a medium-term economic strategy involving on one hand a target for real growth and on the other a target for the rate of inflation.

Action to improve the real rate of growth might then typically involve a large number of measures aimed at strengthening business investment, increasing the propensity to save, reducing the weight of the public sector in the economy, improving the structure of public expenditure, eliminating waste and unproductive activities, and other initiatives at the microeconomic level.

Policies aimed at lowering the rate of inflation in the economy may also in many countries include measures to eliminate rigidities in the wage and price formation—notably indexation arrangements, wasteful price policies in the health sector and various forms of arrangements aimed at protecting commercial interest from the effects of competition. However, anti-inflation policies are unlikely to succeed unless supported by a credible medium-term financial strategy which explicitly allows for a gradual reduction in the rate of inflation within a realistic overall trajectory for nominal GDP. The chosen trajectories would therefore be supplemented by medium-term targets/trajectories for the key budgetary and monetary variables, also in nominal terms. A reduction in the growth of the monetary aggregates would be utilized actively as an instrument of anti-inflation policies.

Over the period of 18 to 24 months normally covered by short-term economic forecasting the medium-term trajectory for nominal income and expenditure and budgetary and monetary variables would provide a framework within which the policy-makers might decide how to react to price or supply shocks or to cyclical fluctuations in demand and output. Such decisions would always require a certain amount of value judgement, notably with respect to the distinction between cyclical fluctuations and changes in the medium-term trend which would have to be reflected in a revision of the medium-term financial strategy. However, despite the unavoidable uncertainty with respect to the identification of trend and cycle, an explicit formulation of policy assumptions in this field might afford a larger degree of credibility to the stabilization policies undertaken.

In the case of supply constraints leading to temporary productivity falls and increase in prices, the level of nominal GDP may remain approximately unchanged and discretionary budgetary or monetary policy measures would not be required. Where both prices and the volume of output fall temporarily short of the medium-term trajectory there would be some scope for letting the automatic budgetary stabilizers operate on the basis of a temporary increase in monetary financing. This would hardly allow a complete elimination of the cycles but would at least contribute to a smoothening of the fluctuations in the face of a temporary weakening of credit demand from the private sector.

These policy prescriptions, however, can only work efficiently if monetary and budgetary policy are geared fundamentally towards stabilization with, in particular, a realistic level of long-term interest rates, a sound position of the budget balance in a medium-term perspective, a balanced competitive position, and towards a satisfactory inflation performance.

Moreover, even in countries with comprehensive quarterly national accounts the level and growth of gross domestic product is known only with a timelag of several months. Also, the quarterly fluctuations of nominal GDP appear to be considerably more erratic than real GDP. In fact, only monetary policy can be modified with sufficiently short notice to give some degree of flexibility in the implementation of policies; but the effects of monetary policy on the level of GDP would typically come through with a certain delay – typically 6 to 9 months. Attempts to fine-tune movements of nominal GDP could therefore easily lead to an even greater instability of economic activity than before. Consequently, in the very short-term macroeconomic policy would still have to rely on the conventional instruments of monetary policy: changes in central bank money stock, discount rates, reserve requirements, etc. The nominal income framework, thus, would not reduce the responsibility of the central bank for day-to-day decisions on monetary conditions but perhaps make it easier for the monetary authorities to allow for changes in the velocity of circulation of money and structural changes in money demand without necessarily endangering the confidence of financial markets.

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2. Economic outlook in the short and medium term

The recovery in the world economy which had been looked for in the second half of 1982 did not materialize; instead output weakened in many countries and world trade fell back again. In the first half of 1983 output in the USA started to rise and the trend of world trade appears to have levelled off. Within the Community there is an increasing number of signs that a patchy recovery from recession is at last under way. However, of the three main external factors which at various stages either led to the onset of the recession or contributed to its unusual length—the oil price rises, high real interest rates and the weakness of world trade (in part because of developing country debt problems)—only the first has been substantially eased. The recovery in Europe is therefore likely to be slow and hesitant. The latest forecasts show rises in real gross domestic product in the Community of 0,5% in 1983 and 1,5% in 1984; this will not be fast enough to achieve any significant decline in the number of unemployed. In the medium term the central projection suggests annual average growth to 1987 in real gross domestic product of around 2,0%, only sufficient to reduce the unemployment rate very slightly.

2.1 Recent developments and short-term outlook

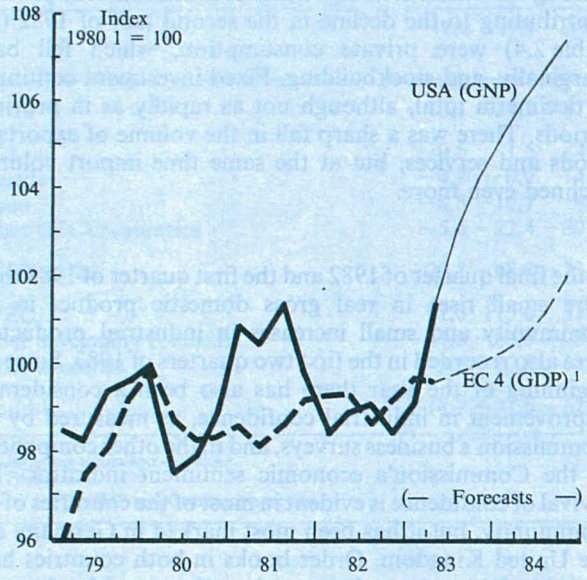
In 1983 indications of the beginning of an upturn in the world economy have as yet not been reflected convincingly in the Community economy. There have been output gains in some of the Community countries since the end of last year, but it is still uncertain whether these stirrings of growth are the prelude to a phase of sustained and balanced expansion. The danger remains, because of the continuance of a number of unfavourable factors, that the Community economy may revert to a further period of stagnation.

1982 was the third year of the recession in the Community. Expectations that a gradual recovery in the Community economy would get under way during 1982, which were based mainly on increases in Community real gross domestic product in the final two quarters of 1981 and on some strengthening of business confidence in the early months of 1982, were in no way fulfilled. Instead, against a background of continuing high real interest rates and a falling away of world trade, activity in the Community weakened, with especially sharp falls in output in the third quarter of 1982. A discussion of factors which led to the expected recovery in 1982 being aborted, and some of which still threaten the potential recovery in 1983 and 1984, is given in the next section.

In the developed economies outside the Community the second half of 1982 generally saw some steadying in activity, followed by a stronger trend in the first half of 1983. In the United States real gross national product stabilized in the final three quarters of 1982, after the very sharp falls at the end of 1981 and beginning of 1982 (see Graph 2.1). In the first half of 1983 a slowing in the rate of stock liquidation, an end to the falls in fixed investment, with housing investment notably buoyant, and a revival of consumer spending have been the main features in the rises in output achieved (real gross national product rose at an underlying annualized rate of around 5,5% in the first three quarters of 1983). Although the very rapid increases of the last few months are unlikely to be sustained, expansion is expected to continue and to become more broadly based in the second half of this year and into 1984. Private consumption should be given a boost by the mid-year personal tax cuts, and capital investment is expected to strengthen steadily. After a fall of 1,7% in 1982, real gross national product in the United States is forecast to rise by 3,5% in 1983 and 4,3% in 1984.

Japan managed to maintain moderate growth of output throughout 1982 and the early part of 1983, mainly due to the expansion of private consumpion. Fixed investment started to rise in the second half of 1982, but this upturn has not continued. The relatively slow growth of domestic demand during the first part of 1983 was partly compensated for by a rapid expansion of merchandise exports. Growth in real gross national product at an annual rate around 3% is forecast for both 1983 and 1984. In Canada there were sharp falls in output in both halves of 1982, and there were very large reductions in fixed investment. Some recovery appears to be under way in the early months of this year and output

GRAPH 2.1: **Comparison of cycle in real GNP/GDP in the USA and the Community, 1979-84**



[1] Based on quarterly national accounts data for the Federal Republic of Germany, France, Italy and the United Kingdom.

growth should accelerate through 1983 into 1984. The smaller non-Community developed countries, mainly in Europe, are highly dependent on developments within the Community for their own conjunctural trends. Several of them (Switzerland, Norway and Sweden) experienced a fall in output in 1982, but most should show somewhat stronger positive growth in 1983 and a further improvement next year.

In both halves of 1982 the volume of world trade fell sharply (see Table 2.1). Imports by the developed OECD countries fell throughout the year, mainly as a result of cuts in North American imports in the first half and exacerbated by lower Community imports in the second half. But the main contribution to the weakness of world trade last year came from falling imports by developing countries (both oil producers and non-oil). Both groups were faced by sharply declining export revenues. The OPEC countries experienced a 21% fall in export earnings, over three-quarters of which was due to a decline in export volumes consequent upon the large adjustment in world demand for oil. The export revenues of the non-OPEC developing countries fell by some 9%, mostly as a result of lower primary commodity prices, although many individual countries also experienced volume losses as well. In addition current account debits were swollen by high debt-servicing costs, and many countries faced extreme difficulties in financing new deficits or in refinancing maturing debt. The volume of imports by both OPEC and other developing countries fell at an annual rate of 7-8% in both halves of 1982 (for the OPEC countries the slight rise in volume when comparing the average of 1982 with the average for the previous year is due to the fact that OPEC import volumes were expanding very rapidly throughout most of 1981).

Preliminary estimates for the first half of 1983 suggest that the decline in world trade has halted and that the trend has become firmer. North American imports have begun to recover and, while OPEC import volumes have continued to shrink rapidly, it appears that imports by the other developing countries have fallen less sharply than during last year. Trends in world trade are likely to lack dynamism, but the latest forecasts suggest a gradual strengthening through to the end of 1984. Imports by the developed countries should rise faster as the recovery in activity proceeds, and the non-oil developing countries could start to increase their imports as the demand for their exports and the prices of commodities become firmer. More downward adjustments in OPEC imports are expected, as a further 20% cut in export revenues, due in almost equal proportions to volume and price falls, is likely for 1983. If there is some recovery in the demand for OPEC oil towards the end of this year and in 1984, then the decline in OPEC import volumes could tail off in the latter part of next year. In total the volume of world trade (imports of goods) is forecast to show almost no change in 1983 and then to rise by 3,7% in 1984, after falling by 0,7% in 1982.

The world recession and the increases in the value of the US dollar against most other currencies have led to some substantial changes in the prices of goods traded on international markets. There has been an appreciable reduction in world consumption of oil since the second oil price shock of 1979-80, substitution out of oil because of the high level of prices having been compounded by reduced demand because of the fall in activity during the recession. Average dollar oil prices already started to weaken during 1982, with falls in spot market prices and reduced premiums or wider discounts being offered by some OPEC countries. Faced by a continued deterioration of oil market conditions, and after an earlier unsuccessful attempt to hold prices through production discipline, the OPEC countries decided in March 1983 to reduce the official marker price from USD 34 per barrel to USD 29, and set an overall limit on output of 17,5 million barrels per day with production quotas allocated to individual countries. Although the picture is confused by large stock movements which have occurred, some stability does now appear to have returned to the oil market, and it seems that the OPEC price agreement is holding. For the purposes of the forecast it has been assumed that oil prices will remain at the nominal level reached after the agreement until at least the end of 1984.

The prices of other primary commodities fell back sharply in 1982. Since the beginning of this year, however, the spot prices of many commodities, both foods and raw materials, have tended to become firmer. Agricultural products in particular have scored some large price gains during the summer months influenced by the prospects of relatively poor harvests. By the middle of October 'The Economist' index of commodity prices (in dollar terms) was 24% higher than one year earlier; in ECU terms the rise was one third. Commodity prices are expected to continue rising throughout the remainder of 1983 and 1984 as demand picks up, but no runaway acceleration seems likely. Dollar prices of non-fuel primary commodities (UN index) are forecast to rise by 4,5% in 1983 and 11,2% in 1984 after a fall of 10,6% in 1982.

Because the United States is leading most other countries out of recession and because of the strength of the US dollar, the deficit on the US current account is expected to widen appreciably in 1983 and 1984 (see Table 2.2). Most other developed countries are expected to show some improvement in their current balance. The OPEC countries were probably marginally in current account deficit in 1982, and this deficit is likely to widen substantially in 1983 before steadying in 1984. The combined deficit of other developing countries, while remaining large should be smaller in 1983 and 1984 than last year.

In the Community there was a deepening of the recession in the middle two quarters of 1982 and industrial production continued to decline until the end of the year (see Table 2.3). Among the domestic components of gross domestic product contributing to the decline in the second half of 1982 (see Table 2.4) were private consumption, which fell back marginally, and stockbuilding. Fixed investment continued to decline in total, although not as rapidly as in previous periods. There was a sharp fall in the volume of exports of goods and services, but at the same time import volumes declined even more.

In the final quarter of 1982 and the first quarter of 1983 there were small rises in real gross domestic product in the Community and small increases in industrial production were also recorded in the first two quarters of 1983. Since the beginning of the year there has also been a considerable improvement in industrial confidence, as measured by the Commission's business surveys, and in the other components of the Commission's economic sentiment indicator. The revival of confidence is evident in most of the countries of the Community, but it has been most marked in Germany and the United Kingdom. Order books in both countries have been improving from their previous depressed levels.

Table 2.1

World output, foreign trade and EC export markets

(% change over previous period, seasonally adjusted annual rate)

	1979	1980	1981	1982	1983 [3]	1984 [3]	1982		1983 [3]		1984 [3]	
							I	II	I	II	I	II
GDP/GNP, OECD total	3,6	1,6	1,6	−0,3	2,1	3,1	−0,8	0,3	2,2	3,6	3,0	2,7
Imports of goods (volume)												
World	5,9	1,3	2,0	−0,7	0,1	3,7	−2,4	−3,6	1,1	2,6	4,2	4,2
EC 10 [1]	9,3	1,0	2,8	2,6	0,7	2,1	5,2	−4,5	3,3	1,1	2,7	2,2
World (excluding EC)	4,2	1,4	4,7	−2,3	−0,2	4,6	−6,0	−3,1	0,0	3,5	5,0	5,3
of which:												
OECD (excluding EC)	5,7	−3,2	0,8	−1,5	2,0	7,2	−10,4	4,6	6,0	9,0	7,0	6,0
OPEC	−11,3	10,5	27,4	1,2	−8,2	−0,8	−6,7	−7,5	−8,8	−7,8	0,0	5,1
Other developing countries	10,0	6,7	5,5	−6,5	−1,9	4,4	−8,6	−7,5	−1,4	3,0	4,7	5,1
Other countries	2,8	4,0	1,6	−2,3	2,4	4,3	−3,4	−0,8	3,0	4,4	4,2	4,3
EC export markets [2]												
Intra-EC markets	10,4	1,9	−2,7	2,4	0,3	2,0	:	:	:	:	:	:
Extra-EC markets	4,0	4,7	5,7	−1,7	−0,9	2,8	:	:	:	:	:	:
Total	7,4	3,2	1,3	0,3	−0,2	2,3	:	:	:	:	:	:
Exports of goods (volume), EC total [1]	7,4	2,7	4,0	0,8	0,7	3,5	−0,5	−3,8	1,3	4,0	3,4	3,5

1 Including intra-EC trade.
2 Import volumes by the various markets weighted together according to their shares in EC exports of goods.
3 Forecasts.

Source: OECD, IMF and Commission services.

Table 2.2

Balance of payments on current account

('000 million US dollars, seasonally adjusted annual rate)

	1979	1980	1981	1982	1983 [2]	1984 [2]	1982		1983 [2]		1984 [2]	
							I	II	I	II	I	II
EC 10	−10,1	−37,2	−17,9	−13,8	−4,1	0,6	−15,0	−12,7	−6,6	−1,6	−0,4	1,6
USA	−0,5	1,5	4,4	−11,2	−29,6	−44,8	5,0	−27,4	−28,0	−31,2	−48,2	−42,4
Canada	−4,2	−0,9	−4,5	2,4	3,2	2,4	−0,1	4,8	2,6	3,8	3,4	1,4
Japan	−8,8	−10,7	4,9	6,9	17,9	18,9	7,0	6,8	19,0	17,0	18,0	20,0
Other OECD countries	−5,6	−22,4	−20,6	−6,7	−3,4	−7,1	−5,1	−8,2	−3,4	−3,4	−6,0	−8,2
OECD, total	−29,2	−68,8	−33,8	−22,4	−16,0	−30,0	−8,2	−36,6	−16,4	−15,4	−33,2	−27,6
OPEC	61,0	115,0	51,0	−3,7	−21,7	−5,8	:	:	:	:	:	:
Other developing countries	−41,0	−63,0	−75,0	−65,1	−44,9	−42,6	:	:	:	:	:	:
Other countries	−9,5	−10,8	−4,4	6,3	6,2	6,9	:	:	:	:	:	:
World [1]	−18,7	−27,6	−62,2	−85,1	−76,5	−71,5	:	:	:	:	:	:

[1] Including errors and omissions.
[2] Forecasts.
Source: OECD, IMF and Commission services.

Table 2.3

Recent developments in GDP and industrial production in the Community

(% change on previous quarter, seasonally adjusted annual rate)

	1981				1982				1983	
	I	II	III	IV	I	II	III	IV	I	II
Real GDP (EC 4) [1]	0,6	−1,7	1,9	2,7	0,3	−0,1	−2,8	2,3	2,1	−0,2
Industrial production (EC 10)	0,1	−0,5	1,1	0,3	0,8	−0,1	−6,8	−6,6	2,8	0,7

[1] Estimates based on quarterly national accounts data for the Federal Republic of Germany, France, Italy and the United Kingdom.
Source: Eurostat and national statistics.

The improving outlook for the international environment, coupled with the rallying of economic sentiment and indications of a firming of the trend of output within the Community, suggest that this time the Community economy is at last starting on a gradual recovery from recession. But some indicators in the first halves of both 1981 and 1982 led then to hopes of recovery which were never fulfilled (see *Annual Economic Reviews* for 1981-82 and 1982-83). Additional evidence is required this time before there can be certainty that a recovery is under way. Furthermore, the potential recovery is likely to be very fragile and could easily be knocked off course by an adverse movement in, for example, interest rates.

The latest forecasts for the Community (see Table 2.4) show only very small additions to output this year, and a slightly faster rate of growth (but low for a recovery phase by historical standards) in 1984. The recovery in Europe is expected to proceed at a slower, more hesitant pace than in the United States (see Graph 2.1).

Table 2.4

Demand, output and external balance, EC 10

	1979	1980	1981	1982	1983 [2]	1984 [2]	1982 I	1982 II	1983 [2] I	1983 [2] II	1984 [2] I	1984 [2] II
	% change at constant prices (seasonally adjusted annual rate)											
Private consumption	3,7	1,6	0,2	0,5	0,4	0,5	1,0	0	1,1	−0,5	0,8	0,9
Government consumption	2,6	1,9	1,5	0,8	0,8	−0,1	0,9	0,6	1,7	−0,8	0,3	0
Gross fixed capital formation	3,8	1,7	−4,7	−1,8	−0,3	2,0	−2,9	0,4	−1,4	1,2	2,3	2,4
Stockbuilding (as % of GDP)	1,7	1,5	−0,2	0,7	0,9	1,2	1,0	0,3	0,8	0,9	1,0	1,3
Domestic demand	4,3	1,2	−2,1	0,9	0,5	1,0	2,7	−1,2	1,7	0	1,2	1,6
Exports (goods and services)	6,2	2,0	3,8	0,7	0,6	3,4	−0,7	−3,6	1,6	2,7	3,7	3,4
Imports (goods and services)	10,3	1,7	2,2	2,3	0,5	1,9	4,1	−3,6	2,0	1,6	2,0	2,0
Gross domestic product at market prices	3,3	1,3	−0,4	0,4	0,5	1,5	1,3	−1,2	1,6	0,3	1,7	2,0
Industrial production	4,9	−0,8	−2,2	−1,7	2,0	2,3	:	:	:	:	:	:
Unemployment rate [1]	5,4	6,0	7,9	9,6	10,4	10,9	:	:	:	:	:	:
	as % of GDP											
Trade balance (fob/fob)	−0,4	−1,2	−0,2	0,1	0,1	0,2	−0,1	0,1	0,1	0,2	0,2	0,2
Current balance	−0,4	−1,3	−0,7	−0,6	−0,1	0	−0,6	−0,5	−0,2	−0,1	0	0,1

[1] Unemployment as % of civilian labour force, EC 9.
[2] Forecasts.
Source: Eurostat and Commission services.

Most of the components of domestic demand should progressively strengthen this year and next. Real personal incomes should benefit from the slowing in the rate of inflation being experienced generally, and saving rates should tend to edge down because of wealth effects from the same influence, so that private consumption rises gradually. Fixed investment is expected to stabilize during this year and then to start to recover, becoming the most dynamic element of domestic demand in 1984. The rate of stockbuilding should increase, accompanying the rising trend in production, but high interest rates are likely to mean that additions to stocks are kept more carefully under control than has been usual in previous periods of recovery. Only government consumption is forecast to rise more slowly in 1983 and 1984 than during the recession years, as efforts are made to contain budget deficits.

The volume of exports are forecast to rise, benefiting both from the expected recovery in world trade and from a more competitive position while the US dollar is strong. Import volumes will also rise in line with the domestic recovery and at a rate not much different from exports, so that the net contribution from the real foreign balance to the growth of real gross domestic product will be marginal.

In total the year-on-year growth in real gross domestic product in the Community is forecast to be only 0,5% in 1983 and 1,5% in 1984, following a fall of 0,4% in 1981 and a slight rise of 0,4% in 1982. Not all countries are expected to record positive year-on-year growth in 1983; falls are forecast for Belgium, France, Luxembourg, Greece and Italy (see Table 2.5). The United Kingdom should have the highest growth rate this year. In 1984 all countries except Luxembourg should have positive growth, but only Germany and the United Kingdom are expected to achieve a rate of expansion of 2%.

The slow rate of recovery for the Community this year and next is likely to be below the rate of increase in labour productivity and so a further fall in employment is probable, of 0,9% in 1983 and 0,3% in 1984. With the labour force still rising very gradually, this implies some further additions to the number of unemployed throughout the forecast period. In response to the gradually improving economic situation

and to a variety of government schemes for youth training, early retirement, etc., which will have the effect of removing people from the unemployment registers, the rise in unemployment during the remainder of 1983 and in 1984 is expected to be relatively small compared with the massive increases which have occurred in the last three years. The total number of unemployed is expected to average almost 12,5 million in 1984, representing 10,9% of the civilian labour force, more than double the unemployment rate in 1979 before the recession began (EC 9 figures).

Table 2.5

Rates of growth of demand and output, 1971-84

(% change in volume)

		B	DK	D	GR	F	IRL	I	L	NL	UK	EC 10
Private consumption	1971-80 [1]	3,8	1,5	3,3	4,7	4,2	2,7	3,2	4,1	3,9	2,1	3,3
	1981	−1,4	−0,5	−0,4	0,7	1,9	−0,4	0,2	1,7	−2,1	−0,1	0,2
	1982	1,1	2,6	−2,2	0,6	3,5	−5,3	0,3	−1,6	−1,6	1,1	0,5
	1983 [2]	−3,1	0,9	0,5	0,1	0,3	−3,5	−0,8	−1,5	−1,5	3,1	0,4
	1984 [2]	−1,1	0,3	1,0	0,8	0,2	−0,8	−0,4	−2,5	−2,0	2,0	0,5
Government consumption	1971-80 [1]	4,2	4,3	2,8	6,1	3,1	6,1	3,0	3,7	2,7	2,5	2,9
	1981	0,6	3,0	1,7	6,5	2,4	−0,1	1,7	2,1	1,3	0,4	1,5
	1982	−1,6	3,3	−1,1	1,0	1,7	3,3	1,8	0,3	0,7	1,2	0,8
	1983 [2]	−1,6	1,2	−0,1	3,0	−1,1	0,0	1,8	−0,3	1,7	2,4	0,8
	1984 [2]	−0,8	−1,5	0,0	2,5	−1,2	−1,0	1,8	−0,7	−3,4	0,4	−0,1
Gross fixed capital	1971-80 [1]	2,2	−1,0	2,0	2,5	2,4	5,2	1,2	2,4	0,8	0,5	1,5
	1981	−16,2	−15,7	−3,9	−10,1	−2,3	7,5	−0,2	−13,3	−10,8	−8,2	−4,7
	1982	−2,6	3,7	−5,4	−1,0	1,1	−8,4	−5,3	−2,2	−5,0	5,1	−1,8
	1983 [2]	−1,9	1,9	3,3	−2,2	−3,8	−10,4	−5,1	−5,8	0,7	4,7	−0,3
	1984 [2]	0,4	1,0	4,7	2,8	−2,6	−1,2	3,7	−2,3	0,5	3,1	2,0
Change in stocks (as % of GDP)	1971-80	0,8	0,6	0,8	5,3	1,3	1,0	2,3	−0,9	0,9	0,5	1,2
	1981	0,2	−0,4	−0,1	7,3	−0,3	−1,0	0,8	1,9	−1,1	−1,7	−0,2
	1982	−0,3	0,0	0,4	4,2	1,1	0,1	0,8	1,4	−0,1	−0,7	0,7
	1983 [2]	0,2	−0,4	0,7	3,9	0,9	0,2	0,5	1,6	−0,1	0,3	0,9
	1984 [2]	0,4	−0,2	1,0	4,0	0,9	0,1	0,8	1,8	0,1	0,7	1,2
Domestic demand)	1971-80 [1]	3,3	1,5	2,8	4,5	3,6	3,6	3,1	3,5	2,8	1,7	2,7
	1981	−4,1	−2,1	−2,0	0,3	−1,1	1,2	−2,7	−1,2	−5,0	−1,7	−2,1
	1982	−0,1	2,8	−2,6	0,4	2,7	−5,0	−0,5	−1,5	−1,8	1,9	0,1
	1983 [2]	−2,5	1,1	0,9	0,2	−0,8	−4,7	−1,1	−2,4	−0,5	3,3	0,3
	1984 [2]	−0,7	−0,1	1,5	1,5	−0,5	−0,9	0,6	−2,2	−1,7	1,9	0,7
Exports (goods and services)	1971-80 [1]	5,4	4,8	6,2	10,5	8,0	8,0	7,0	3,0	5,4	4,1	6,0
	1981	2,4	5,4	7,7	5,4	4,6	2,0	6,0	2,0	0,8	−1,8	3,8
	1982	2,0	2,0	3,5	−5,8	−3,7	4,0	1,2	0,3	−0,9	0,6	0,7
	1983 [2]	1,0	4,6	−1,0	−2,8	−0,1	7,5	1,7	−3,3	2,9	0,3	0,6
	1984 [2]	2,9	2,4	3,2	2,2	3,0	8,3	4,5	0,4	3,8	3,0	3,4
Imports (goods and services)	1971-80 [1]	5,7	2,0	6,3	6,3	7,7	6,3	5,9	3,6	4,1	3,3	5,4
	1981	−1,4	−1,5	−0,5	9,0	−1,5	2,1	−5,4	1,8	−7,3	−0,9	−2,2
	1982	0,2	2,2	−0,1	5,9	4,8	−4,4	2,1	−0,9	1,1	5,0	2,3
	1983 [2]	−0,9	0,0	0,5	−1,3	−2,7	−1,5	−0,8	−3,0	1,7	4,8	0,5
	1984 [2]	1,0	−0,8	3,0	1,6	−0,9	3,7	2,9	−0,8	1,1	3,3	1,5
Gross domestic product at market prices	1971-80 [1]	3,2	2,3	2,9	4,7	3,6	4,1	3,1	3,0	2,8	1,9	2,9
	1981	−1,8	0,1	0,2	−0,7	0,2	1,1	−0,2	−1,8	−1,2	−2,0	−0,4
	1982	1,0	3,4	−1,0	0,0	1,8	1,2	−0,3	−1,1	−1,6	1,5	0,4
	1983 [2]	−0,9	2,2	0,7	−0,2	−0,3	0,5	−0,8	−2,4	0,3	2,8	0,5
	1984 [2]	−0,6	1,2	2,1	1,5	0,4	1,8	1,5	−1,0	0,0	2,2	1,5

[1] Annual average.
[2] Forecast.

Source: Eurostat and Commission services.

2.2 External influences on recession and recovery in the Community

The economies of the Member States have been experiencing the longest period of recession since the Community was founded. In 1974-75 the fall in output was sharper than occurred at any time during 1980-82, but the recession then was relatively short-lived and output bounced back upwards quite strongly in the course of 1975. Although a large part of the explanation of the latest recession must be looked for in the behaviour and reactions of economic agents within the Community, some has its origins in a series of related shocks which have hit the Community economy from outside.

The first of these shocks, which pushed the Community and world economy into recession, was the second huge rise in OPEC oil prices which occurred in a series of steps in quick succession between late 1978 and early 1981. The two-and-a-half-fold rise in oil prices adversely affected oil-consuming countries by cutting incomes, raising price levels, and pushing external balances towards deficit. The fall in output which would be expected to occur in any one country in response to this shock was greatly amplified by the international transmission mechanism, whereby initial falls in output and imports in many countries simultaneously led via shrinking world trade and reduced exports to further declines in output.

Some of the adjustment to higher oil prices would be bound to take place over a number of years, e.g. in cases where new investment is required to make energy savings or to substitute other fuels for oil, but the major part of the adjustment at the macroeconomic level, and more particularly to output, would normally be expected to occur within a period of 18 months-2 years. Thus it was that early in 1982 some signs of a slight upturn in output in the Community were interpreted as being the beginnings of the recovery phase. But three closely linked external factors played a part in aborting the potential recovery. These were high real interest rates in the United States, and the related strength of the US dollar and worsening debt situation of the developing countries.

In the classic business cycle, interest rates, nominal and real, are expected to decline during a period of recession, and thus to give some encouragement to consumption and investment demand. During 1982 nominal interest rates in the United States did fall substantially from the peak levels reached during the previous year, but this was not sufficient to reflect the rapidly declining rate of inflation, and real US interest rates (relative to the current rate of consumer price increases) were higher on average in 1982 than in 1981. Real short-term money market rates in the United States averaged 4% in 1982 and real long-term rates 5,4%. Furthermore, although there was some easing of nominal and real rates during the second half of 1982, they have tended to harden again in the first part of 1983. The causes of these high interest rates are not fully explained, but important elements are: a failure of inflation expectations to adjust downwards with current inflation performance; fears about the future size of the US federal budget deficit and its implications for domestic financing and inflation; and worries about the stability of the US banking system because of its exposure to more-than-usual risk domestically during the recession and, even more seriously, internationally because of the debt problems of many sovereign borrowers.

The effects of high US interest rates have been to keep the US dollar strong and so to severely constrain the opportunities for European interest rates to be brought down to more desirable levels. Although in real terms interest rates in the Community do not appear to be as high as in the United States, they are nonetheless at record levels, averaging about 3,0% for short-term rates during 1982 and early 1983 and 3,8% for long-term rates. This adds substantially to the real debt servicing costs of a large proportion of existing borrowing and discourages new borrowing to finance investment, stockbuilding and some forms of consumer spending.

The strong US dollar has advantages and disadvantages for the European economies. On the import cost side, prices denominated in dollars become more expensive in domestic European currencies. Thus, to the initial oil price shock of 1978-81 was added a dollar shock in 1981 and 1982 when the dollar appreciated by some 42% against the ECU (average for 1982 compared with average for 1980). The weakening during 1982 in oil and other commodity prices in dollars was not perceived as a price fall in terms of most European currencies. Thus although inflation has slowed appreciably in Europe, and this has been helped by an easing in the rate of increase of import prices, the strength of the dollar has prevented import costs from falling as rapidly as they might otherwise have done. [1] The continuing strength of the US dollar at the same time has made it very difficult for an active policy of interest rate reduction to be pursued in Europe, as such a policy could well imply a further depreciation of the European currencies against the US dollar so long as US interest rates remain high.

On the other hand, the strong dollar makes European suppliers more competitive in world markets relative to dollar-based suppliers. By the second quarter of 1983 the Community's price competitivity (based on wholesale prices) against other countries showed an improvement of 15% compared with the average for 1980, while the competitivity of the United States deteriorated by 28%.

[1] See Chapter 3 for further discussion on this point.

The third influence which played a major part in halting any recovery in Europe in 1982, was the worsening developing country debt crisis which had direct repercussions on developing country imports, world trade, Community exports and output. The enormous cumulative current account deficit of the oil-importing developing countries since 1973 had been financed with increasing difficulties. The prolonged world recession, which reduced demand and prices for developing country exports, and the high level of interest rates meant that many countries faced very large debt-servicing burdens and could not easily obtain further financing. In addition a group of high-absorbing oil exporters was hard hit by the fall in demand for oil and the weakening of oil prices. A sharp reduction in imports followed and had its repercussions and was amplified through the developed economies. Imports by the non-oil developing countries (which accounted for 21% of Community exports to extra-EC countries in 1982) fell by 6,5% in volume in 1982, and imports by the OPEC countries (19% of extra-EC exports by the Community) also declined steeply during 1982 and are expected to fall again markedly in 1983 (see Table 2.1).

In 1983 many of the factors mentioned have continued to restrain growth in Europe. It is true that oil prices have fallen back (although by relatively little compared with the earlier rises), and this should give some stimulus to output and trade. But the continuing strength of the dollar will limit to some extent the effects in Europe of a fall in dollar oil prices. Interest rates remain high and are showing a tendency to move higher; if this trend should be confirmed the recovery in Europe will be very seriously threatened. Community exporters will continue to be helped by their improved competitiveness, but in other areas the strong dollar places severe constraints on policy options. Finally, although the risk of major financial collapse seems for the moment to have been averted, serious difficulties remain for the developing countries which are bound to hold back the growth of world trade.

2.3 Medium-term prospects

Projections beyond the horizon of the short-term forecasts described in section 2.1 are made using the Commission's medium-term Comet model. The most recent projections look as far ahead as 1987. The first two years of the projection (1983 and 1984) are aligned with the short-term forecasts. The central medium-term projection for the Community as a whole is shown in Table 2.6.

Over the period between 1982 and 1987 the central projection suggests average gowth of real gross domestic product in the Community of about 2,0% per year. This is slightly stronger than the average growth of 1,75% per year during the nine years following the first oil shock in 1973, but it is well below the rate of expansion in the early years of the Community. Private consumption is projected to grow a little more slowly than gross domestic product, while the projected rise in government consumption is noticeably lower at only 0,5% per year. Fixed investment, which was lower in real terms in 1982 than in 1973, grows at almost 3% per year. The growth rate of gross domestic product over the period as a whole is the same as that of labour productivity, but some very slow rises in employment from 1985 onwards should be possible. As a consequence unemployment declines little from the peak expected to be reached in 1984, and, on the assumption of unchanged policies underlying the projection, the unemployment rate by 1987 is still as high as 10,4%. Inflation is shown as stabilizing at just under 6% per year. Over the period of the projection government net borrowing (as a percentage of GDP) is expected to fall back to below 3%.

Any projection for the medium term is highly sensitive to the assumptions made about the key exogenous variables in the model. The main assumptions about the international environment outside the Community relate to the price of oil, the growth of world trade and long-term interest rates in the United States. In the central projection it has been assumed that the nominal OPEC export price of oil in US dollars starts to rise again in 1985 but at a slower rate than the dollar prices of OPEC imports. The real oil price (relative to the cost of OPEC imports) is thus assumed to fall over the period by

Table 2.6

Medium-term projection to 1987, EC 10

(annual average growth rate in %)

	1973/1960	Central projection	
		1982/1973	1987/1982
Real GDP	4,8	1,7	1,9
Private consumption	4,8	2,0	1,5
Government consumption	3,7	2,3	0,6
Fixed capital formation	5,6	−0,4	2,7
GDP prices	4,9	10,7	5,7
Employment	0,2	−0,3	−0,1
Unemployment rate (% of labour force) [1]	2,4	9,6	10,4
Real wages per employee	5,0	2,4	1,1
General government net lending (% of GDP) [1]	−0,8	−5,2	−2,7
Balance of trade in goods and services (% of GDP) [1]	0,5	0,3	1,1

[1] At end of period.
Source: Comet model.

an average 2,5% per year. The volume of world imports (excluding the Community) is assumed to grow at an annual rate of 3,9%, which, while faster than the average for the last five years, is still slow in a longer-term historical perspective. The US long-term interest rate is assumed to show a gradual and fairly small reduction until 1987.

A number of exogenous assumptions are also made for each of the member countries. These relate principally to government consumption and investment expenditures, residential construction investment, rates of direct and indirect taxes and of social security contributions and payments of subsidies. Generally in the central projection these variables are set to reflect no change in policies other than those which have already been announced. Exchange rates against the US dollar are also set exogenously; it is assumed in the central projection that from 1984 onwards there is a gradual small appreciation (averaging only about 0,5% per year) in the value of the ECU against the dollar; but some larger movements in individual currencies are introduced to reflect differential inflation rates.

The central medium-term projection for the Community suggests that economic growth during the remainder of this decade will be much slower than achieved in the years before the first oil shock in 1973, but slightly faster than in the years since that divide. Two alternative approaches to assessing what has been the underlying growth in production potential in Community countries in recent years are given in Table 2.7. The comparative cyclical positions of the Member States can be more clearly seen where abstraction is made from the varying underlying growth rates in each case. Medium-term average growth rates differ significantly from one member country to the next, so that attempts to analyse relative cyclical positions by making comparisons of recent GDP growth rates can be misleading: what might appear to be a good recent performance in a country with high growth potential may, in terms of the use of available production factors and technological opportunities, be less effective than a slower growth rate in a country with more limited possibilities for expansion.

There are two well-known methods of circumventing this problem in the measurement of relative cyclical performance. The first requires the measurement of trend GDP growth rates, deviations from which indicate the cyclical element in economic activity; and the second uses a straightforward comparison of plant capacity-utilization levels, as an indication of the degree to which available factor supplies are absorbed in current production.

The available capacity-utilization indicators refer to manufacturing industry only but, to the extent that the recession is attributable to weak aggregate demand, trends in this series are probably indicative of capacity use in the economy at large. On the basis of this criterion, it can be concluded (see Table 2.7) that, as of the second quarter of 1983 (the date of the most recent observation of capacity utilization levels), the effects of the recession on productive capacity use were most severe in the United Kingdom, Germany, Ireland and Italy (in that order), with Belgium, France and the Netherlands being much closer to normal activity levels.

However, as suggested above, normal activity levels (and the equivalent high rates of capacity utilization) imply substantially different growth performances as between the countries in question here. This follows from the fact that production potential (based on such factors as investment and technological progress) is advancing at different rates in the Member States. The estimates of underlying GDP growth and of GDP expansion between points in time of equal capacity utilization in consecutive cycles, presented in Table 2.7 are designed to indicate the growth of production potential in this broad sense.

Table 2.7

Growth trend and capacity-utilization levels

(% change)

	EC	B	D	F	IRL	I	L	NL	UK
Underlying GDP growth trend [1]	1,7	1,6 [2]	1,8	0,7	:	2,6	:	−0,4 [2]	0,9
Decline in industrial capacity-utilization levels during present recession (since 1979-80)	−7,4	−4,3	−10,3	−4	−8,9	−7,2	−0,5	−2,7	−11,3
Recent inter-cyclical growth in GDP between periods of equal industrial capacity utilization [3]	1,3	1,2	1,6	1,2	:	2,6	:	1,8	0,5

1 Based on 5-year moving averages, adjusted for average cyclical performance.
2 Based on industrial production.
3 For details of methodology see *European Economy*, Supplement B, June 1983.

Source: Eurostat and EC business surveys. Data not available for Denmark and Greece.

Perhaps the most striking aspect of these growth potential estimates is the fact that they are everwhere low, both in historical terms, and with reference to the economic growth necessary to reduce unemployment. GDP annual growth potential appears in fact to have fallen to about 1,5% for the Community, with country estimates varying from 2,5% in Italy to less than 1% in the United Kingdom.

As can be seen from Table 2.8, the share of net investment (gross fixed capital formation less depreciation) in GDP, one of the principal factors determining production potential, has fallen steadily in recent years. From an average of 13,2% in the 1960-73 period, the net investment ratio for the Community has declined from 12% in 1974 to 7,1% in 1982; the forecast net investment ratio for 1983 is again somewhat lower, at 6,7%. At the individual Member State level, there is a marked clustering of net investment ratios around 7,0% (1983 forecasts), exceptions being Ireland with relatively high net investment (10% of GDP), with Greece and the United Kingdom at the lower extreme (2,9% and 4,3% of GDP, respectively).

The weakness of investment activity in the Community not only limits the growth of production potential through its effects on the expansion of the capital stock; it also slows down the absorption into production processes of new and more efficient techniques, thus rendering Community output less price competitive than it might otherwise be. In these circumstances, the importance of encouraging investment, promoting a more efficient industrial structure and supporting technological progress is clear.

Table 2.8

Share of net investment in GDP, 1974-83

(% of GDP)

	1974	1980	1981	1982	1983
B	13,2	11,6	8,4	7,5	7,2
DK	16,0	9,4	6,4	6,6	6,4
D	10,4	10,2	8,9	7,3	7,3
GR	14,9	12,6	10,3	9,8	10,0
F	13,8	9,4	8,4	7,7	6,9
IRL	15,6	18,2	19,9	17,9	15,2
I	13,3	10,1	9,7	8,3	7,3
L	12,6	13,5	10,5	9,9	9,0
NL	12,7	9,9	7,7	6,8	6,6
UK	9,5	6,0	4,2	4,4	4,3
EC	12,0	9,5	8,1	7,1	6,7

Source: Eurostat and Commission services.

3. Prices and costs

The slowdown of inflation in the Community which started in 1982 proceeded further in 1983 and is forecast to continue, albeit at a more modest pace, in 1984. Price increases have, however, slowed down quickly and by large amounts in the main trading partners since the second oil shock. The poor price performance of the Community on an international comparison, is largely attributable to transitory elements, notably the effect of exchange rate changes and an increase in profit margins in 1982. The direct contribution of unit labour costs to the rise in the deflator of final expenditure in 1982 was in fact the same in the Community as in the United States, but higher than in Japan. The real product wage (unit labour costs deflated by the GDP deflator) in the Community, fell both in 1982 and 1983 and is expected to decline further in 1984. Within the Community, all Member States have recorded a substantial slowdown of inflation, but only very partial results were obtained in the reduction of divergences between countries. With respect to adjustment of the income distribution, the development has been uneven with marked declines in the labour income ratio in some Member States, but smaller declines or even in some cases, an increase in 1983 (Greece, Italy, Luxembourg).

3.1 Inflation: trends and prospects

The process of disinflation in the Community since the second oil shock in 1980 proceeded further in 1983. The deflator of private consumption for the Community as a whole, which rose by 8,7% in 1982, is estimated to have increased by 6,3% in 1983, representing a slowdown of 2,4 percentage points or substantially more than the 1,4 points slowdown from 1981 to 1982 (Table 3.1). The rise in the deflator of total final expenditure decelerated even more strongly (from 8,5% in 1982 to 6,0% in 1983) as a consequence mainly of a pronounced slowdown of the price increase for exports of goods and services (in ECU terms). The GDP deflator, the broadest expression of the domestic cost developments, after an increase of 9,1% in 1982, is estimated to rise by 6,3% in 1983. Despite the depreciation of the ECU in trade-weighted terms, both in 1982 and in 1983, the terms of trade of the Community (measured on total

Table 3.1

Price developments for GDP components, EC 10

(Percentage change in implicit price index, national accounts definition)

	1961-73	1974-79	1980	1981	1982	1983 [1]	1984 [2]
Private consumption	4,6	10,8	11,2	10,1	8,7	6,3	5,6
Government consumption	7,1	12,3	13,6	11,7	9,0	6,2	4,8
Gross fixed asset formation	5,0	11,6	12,0	9,3	7,0	5,7	5,1
Export of goods and services	3,0	10,2	11,4	10,8	8,4	5,3	5,2
Total final expenditure	4,6	11,2	11,7	10,2	8,5	6,0	5,4
Import of goods and services	2,7	11,5	15,5	14,0	6,0	4,6	6,1
Gross domestic product	5,0	10,9	10,8	9,1	9,1	6,3	5,1
Terms of trade (goods and services)	0,3	−1,1	−3,5	−2,8	2,3	0,6	−0,8

[1] Estimates.
[2] Forecasts.

Source: Eurostat and Commission services.

external and internal trade in goods and services) improved by 2,3% in 1982 and should improve a further 0,6% in 1983.

Although the rate of inflation in the Community in 1983 is estimated to have declined to within reach of the rate experienced on average for the years 1961-73, the divergence of inflation among Member States remains considerably larger than before the first oil-price shock. Thus the difference between the highest and the lowest rate of increase in the deflator of private consumption in 1983 amounted to 17,7 percentage points against 3,1 points in the 1961-73 period and the standard deviation of the rates of change in 1983 amounted to 5,1 as against 1,8 on average in the reference period.

Table 3.2

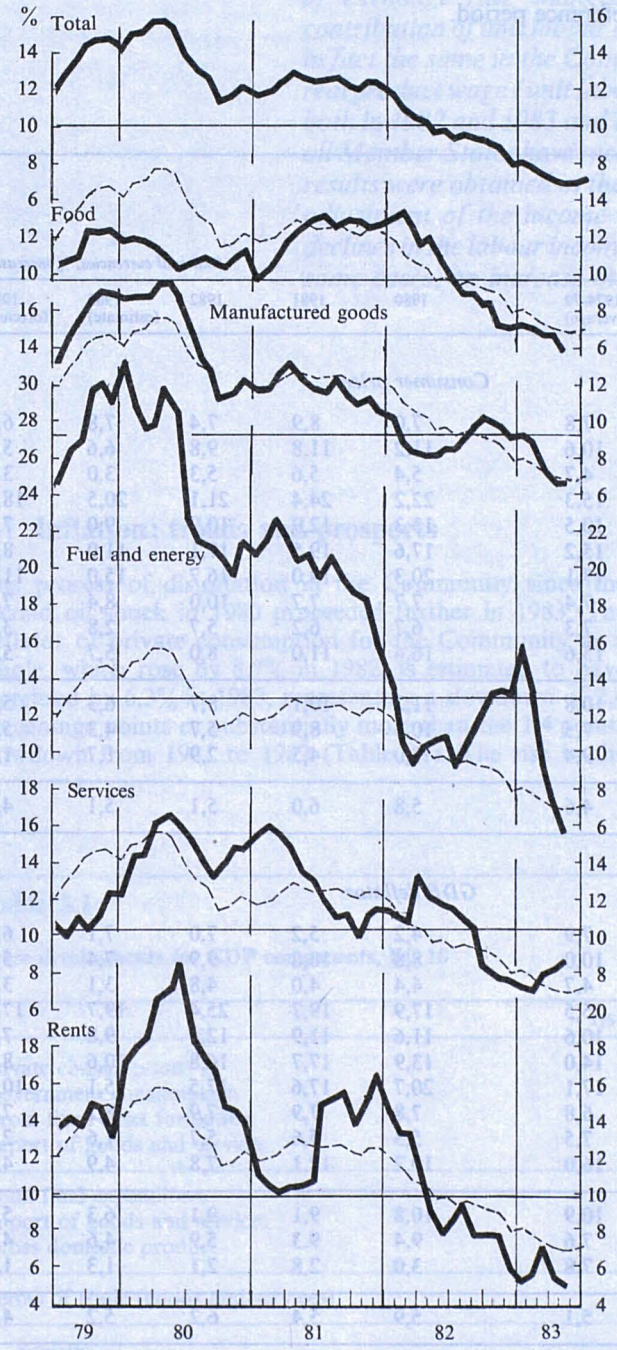
Consumer prices and the GDP deflator

(national currencies, % increase)

	1961-73 (average)	1974-79 (average)	1980	1981	1982	1983 (estimate)	1984 (forecast)
			Consumer prices				
B	3,7	7,8	7,0	8,9	7,4	7,8	6,5
DK	6,1	10,6	11,2	11,8	9,8	6,6	5,4
D	3,7	4,7	5,4	5,6	5,3	3,0	3,2
GR	3,5	15,3	22,2	24,4	21,1	20,5	18,5
F	4,7	10,5	13,3	12,9	10,9	9,0	7,2
IRL	5,9	15,2	17,6	19,5	17,1	11,0	8,8
I	4,8	17,1	20,3	19,0	16,7	15,0	11,5
L	3,0	7,4	7,7	7,7	10,0	8,4	7,7
NL	5,2	7,3	6,7	6,2	5,7	2,8	3,6
UK	4,9	15,6	16,4	11,0	8,0	5,7	5,8
EC 10	4,6	10,8	11,2	10,1	8,7	6,3	5,6
USA	3,1	7,5	10,4	8,9	5,7	4,3	5,0
Japan	6,1	9,4	7,0	4,5	2,9	1,7	1,6
Standard deviation EC 10	1,7	4,6	5,8	6,0	5,1	5,1	4,2
			GDP deflator				
B	4,1	7,9	4,2	5,2	7,0	7,1	6,3
DK	6,7	10,0	8,8	10,8	9,9	7,4	5,2
D	4,3	4,7	4,4	4,0	4,8	3,1	3,0
GR	4,5	15,5	17,9	19,7	25,4	19,7	17,9
F	4,9	10,6	11,6	11,9	12,8	9,8	7,3
IRL	7,2	14,0	13,9	17,7	16,8	10,6	8,2
I	5,4	17,1	20,7	17,6	17,5	15,1	10,4
L	4,1	6,8	7,8	7,9	7,9	8,2	7,4
NL	6,0	7,5	5,3	5,6	5,7	1,6	2,4
UK	5,1	16,0	19,2	12,1	7,8	4,9	4,8
EC 10	5,0	10,9	10,8	9,1	9,1	6,3	5,1
USA	3,5	7,6	9,4	9,3	5,9	4,6	4,7
Japan	5,8	7,8	3,0	2,8	2,1	1,3	1,7
Standard deviation EC 10	2,0	5,1	5,9	5,4	6,2	5,2	4,2

Note: Consumer prices = implicit price index of consumers' expenditure; GDP deflator = implicit price index of GDP.
Source: Eurostat and Commission services.

GRAPH 3.1: **Consumer prices and main components, EC 9**
Change on six months (s.a.) expressed as an annual rate



Source: Eurostat, OECD and Commission services. —— = Total.

Nonetheless since 1980 there has been some progress in reducing the problem of divergent inflation rates. Among the four larger countries the deceleration has (in percentage points) been greater in the countries which had double-digit rates of inflation in 1980. By mid-1983 the reduction in inflation had been 3 points in the Federal Republic of Germany, 4 points in France, 6 points in Italy, and 14 points in the United Kingdom. Indeed, by mid-1983 no EC countries except Italy and Greece any longer had double digit inflation. In 1982 Denmark, France and Ireland were in double digits and in 1981 this was also true of the United Kingdom.

With an end to the weakening of primary commodity prices further progress in reducing inflation is likely to be much more difficult to accomplish. The monthly index of consumer prices in the Community in the six months to July 1983 rose at an annual rate of 8,1% [1] or almost the same rate as at the beginning of the year with, notably, the rise in food prices and services showing a tendency towards acceleration in 1983 while the prices of manufactured goods and fuel and energy, which had shown a tendency to accelerate from mid-1982, have risen more moderately in the spring of 1983 (see Graph 3.1).

A continued fall in inflation in the Community is forecast for 1984, with the deflator of private consumption easing to 5,6%, a figure close to the levels recorded at the beginning of the 1970s, but still above the average for the period 1961-73 (4,6%). Divergence is also expected to narrow with inflation rates falling rapidly in the higher inflation countries and modest rises in the trend of consumer prices in the lower inflation countries. Among these Member States, the increase in inflation will be marginal in the Federal Republic of Germany and the United Kingdom, but in the Netherlands, which recorded the lowest inflation rate in the Community in 1983, the rise in prices will accelerate to 3,6%. In the Federal Republic of Germany, Denmark and the Netherlands, inflation in 1984 will be below the average rates of the period 1961-73, while in the United Kingdom, France and Ireland, this pre-oil shock level is expected to be exceeded by between 1 and 3 percentage points. In Luxembourg, Italy and Greece, inflation in 1984 will be 5, 7 and 15 percentage points higher than in 1961-73. Some slight worsening in the terms of trade of the Community will result in the GDP deflator rising 5,1% in 1984, the lowest rate recorded in the Community since 1969.

[1] The monthly index of consumer prices in the Community is calculated by Eurostat as a fixed weight (Laspeyre) index (base year 1975) while the deflator of private consumption is calculated as a current weight index. The difference between the two estimates will increase with the distance from the base year and is at present (in 1983) almost 2 percentage points.

3.2 The Community's price performance in an international perspective

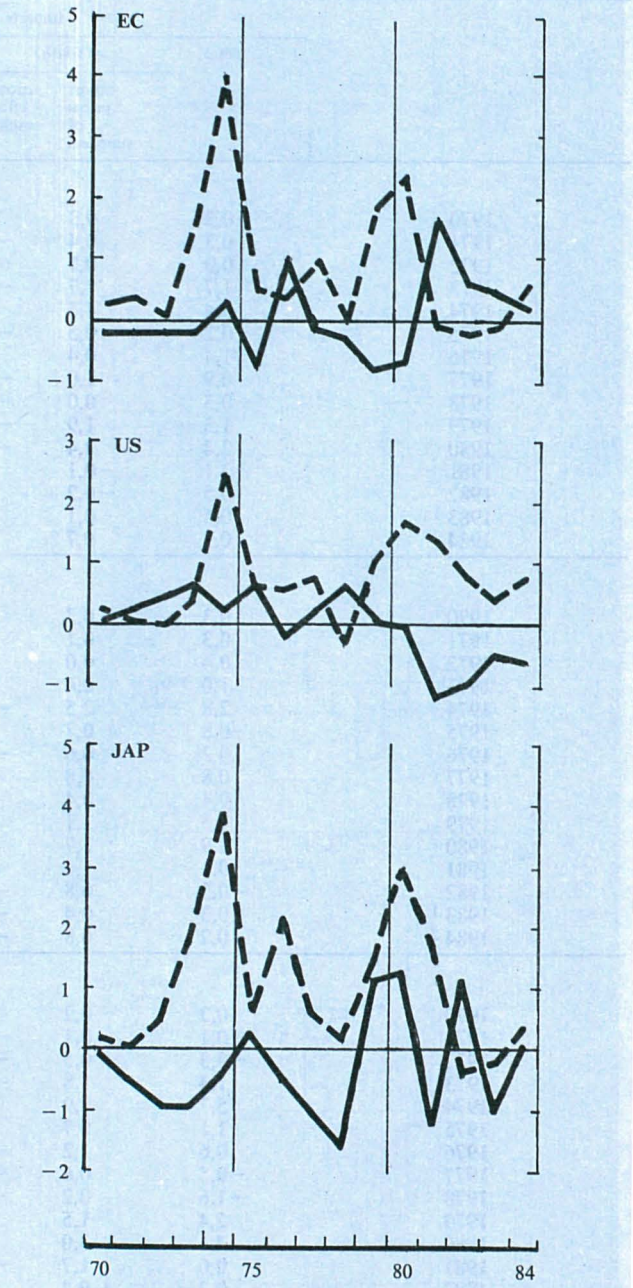
The Community is not alone in having reduced its rate of inflation towards the level recorded in the years 1961 to 1973. In fact the United States made even faster progress than the Community in this respect and Japan—whose inflation rate in the 1960s was substantially higher than that of the Community—may have a lower rate of inflation in 1983 than even Germany and the Netherlands.

However, while the apparent rate of inflation (deflator of private consumption) in the Community in 1983 remained 2 and 4,6 points above the rates recorded in the United States and Japan respectively, a more detailed analysis of the origin of price increases shows that the underlying price performance of the Community may, in fact, be relatively more favourable. One element, which in 1981, 1982 and 1983 has worked to boost prices in the Community, is the depreciation of the Community currencies against the dollar while, on the other hand, the United States has benefited from the substantial appreciation of the dollar in effective terms. Thus, as shown in Table 3.3, changes in the real effective exchange rate may, for the Community as a whole in 1981, 1982 and 1983, have added 1,7, 0,6 and 0,5 percentage points respectively to the increase in the deflator of total expenditure. [1] In the United States, on the other hand, real exchange rate appreciations in 1981, 1982 and 1983 is estimated to have reduced the rise in the deflator of total expenditure by 1,2, 1,0 and 0,5 points respectively. Thus the real exchange rate movements go quite a long way towards explaining the faster price deceleration in the United States than in the Community over the past two and a half years.

However, the exchange rate changes have been absorbed in part by changes in the profit margins of exporters. The estimates of the impact on the final expenditure deflator of changes in the export prices of suppliers, in fact, in recent years have shown a tendency to vary inversely with real exchange rate changes. For example, as seen from column 2 in Table 3.3, changes in the export prices of suppliers in 1981 (in dollars) exerted a negative impact of 0,1% on the domestic price level in the Community while for the United States export prices of suppliers raised the final expenditure

[1] The contribution to the rise in prices of real exchange rate changes, can be regarded as a rough measure of the influence on inflation of monetary policy via its external impact. The difference between figures for the nominal and real exchange rates is the movement in exchange rates which would be necessary to maintain competitiveness in that year. This gives an idea of the secondary impact of domestic cost pressures on prices through exchange rate movements to compensate for cost developments which are out of line with partner countries. The technical annex discusses the interpretation of these figures and reviews certain statistical and methodological problems associated with the data.

GRAPH 3.2: **External impacts on the final expenditure deflator**



Source: Estimates by the Commission services.

Table 3.3

Origin of price increases (final expenditure)

	Imports				Unit labour costs	Indirect taxes	Other factors	Total [3]	
	Total	*of which:*		*of which:*					*of which:*
		export prices of suppliers	nominal effective exchange rate	real exchange rate					Domestic factors [4]
					EC 10				
1970	0,3	0,3	0,0	−0,2	4,8	0,2	1,4	6,4	6,3
1971	0,3	0,4	−0,1	−0,2	4,3	0,5	1,9	7,1	6,9
1972	0,0	0,1	−0,1	−0,2	3,5	0,4	2,2	5,9	6,0
1973	1,7	1,7	−0,2	−0,2	4,8	0,5	2,6	9,4	7,9
1974	5,4	4,1	0,3	0,3	7,4	0,6	2,4	16,8	12,4
1975	0,2	0,5	−0,3	−0,8	8,2	0,9	2,8	13,2	13,5
1976	1,4	0,4	1,0	1,1	3,7	1,1	3,3	11,0	9,5
1977	0,9	1,0	−0,1	−0,2	4,2	0,9	2,4	9,6	8,8
1978	−0,3	0,0	−0,3	−0,3	3,6	0,8	2,2	7,2	7,5
1979	1,3	1,9	−0,6	−0,8	4,3	1,2	2,4	9,6	8,5
1980	2,4	2,4	−0,3	−0,7	6,1	1,4	2,2	11,8	10,1
1981	2,1	−0,1	2,0	1,7	5,2	1,1	2,2	10,0	8,4
1982	0,5	−0,2	0,7	0,6	3,5	0,9	3,1	8,5	8,1
1983 [1]	0,5	−0,1	0,6	0,5	2,3	0,7	2,1	6,0	5,6
1984 [2]	0,9	0,7	0,2	0,2	1,9	0,5	1,8	5,4	4,3
					USA				
1970	0,3	0,3	0,1	0,1	4,2	0,8	0,2	5,4	5,0
1971	0,3	0,1	0,1	0,3	2,0	0,6	2,4	5,2	4,8
1972	0,4	0,0	0,4	0,5	2,6	0,0	1,5	4,3	3,8
1973	1,0	0,4	0,5	0,7	3,3	0,4	1,6	6,3	5,2
1974	2,8	2,5	−0,1	0,3	5,9	0,8	1,5	11,0	8,2
1975	0,8	0,7	0,1	0,7	4,0	0,7	3,7	9,1	7,7
1976	0,2	0,6	−0,4	−0,2	3,4	0,3	1,6	5,5	5,1
1977	0,8	0,8	0,0	0,2	3,2	0,2	2,1	6,4	5,4
1978	0,4	−0,4	0,8	0,7	4,4	0,1	2,3	7,2	6,9
1979	1,5	1,1	0,3	0,1	5,3	0,3	2,4	9,5	8,3
1980	1,9	1,7	0,0	0,0	5,6	0,9	2,1	10,3	8,6
1981	0,1	1,4	−1,3	−1,2	4,5	1,1	2,8	8,5	8,3
1982	−0,3	0,8	−1,1	−1,0	3,6	0,4	1,3	5,0	5,2
1983 [1]	−0,3	0,4	−0,7	−0,5	1,8	0,1	2,3	3,9	4,0
1984 [2]	0,2	0,8	−0,5	−0,6	2,9	0,2	1,2	4,5	4,3
					Japan				
1970	0,2	0,2	0,0	0,0	4,2	0,6	1,9	6,8	6,6
1971	−0,1	0,1	−0,1	−0,5	5,3	0,2	−0,8	4,7	5,1
1972	−0,3	0,5	−0,9	−0,9	2,8	0,2	1,8	4,4	4,8
1973	1,4	1,8	−0,4	−0,9	6,7	0,7	3,6	12,1	11,2
1974	5,7	3,9	0,6	−0,4	12,2	0,4	6,2	24,4	20,9
1975	1,1	0,7	0,4	0,3	6,1	0,1	0,5	7,9	6,9
1976	0,6	1,2	−0,5	−0,5	3,7	0,4	1,6	6,3	5,6
1977	−0,5	0,6	−1,2	−1,0	3,0	0,6	1,4	4,5	4,9
1978	−1,6	0,2	−2,0	−1,6	1,3	0,1	2,7	2,4	3,8
1979	2,4	1,5	0,6	1,2	1,4	0,6	0,4	4,7	2,0
1980	4,1	3,0	0,5	1,3	2,1	0,2	0,3	6,5	2,2
1981	0,0	1,7	−1,7	−1,2	2,2	0,1	0,1	2,4	1,9
1982	0,3	−0,4	0,6	1,2	1,8	0,1	−0,0	2,1	1,3
1983 [1]	−1,3	−0,2	−1,2	−1,0	1,1	0,0	−0,0	−0,1	1,1
1984 [2]	0,3	0,4	−0,1	0,0	1,5	0,1	−0,1	1,8	1,4

1 Estimate.
2 Forecast.
3 Excluding intra-Community trade.
4 Total, excluding the effect of export prices of suppliers and real exchange rate changes. The factors were regarded as additive.

Source: Eurostat and Comission services. For methods used and comments on the interpretation of figures, see technical annex.

deflator by 1,4%. Although these differences may be due, to some extent, to divergences with respect to the structure of foreign trade, it would also seem likely that foreign suppliers have reacted to the large exchange rate changes by reducing their profit margins in markets where the currency has depreciated and by raising their sales prices (in their own currency) in the United States in 1981 and 1982. Symmetrical developments appear to have occurred in the past for the EC and the US but much less so for Japan (see Graph 3.2).

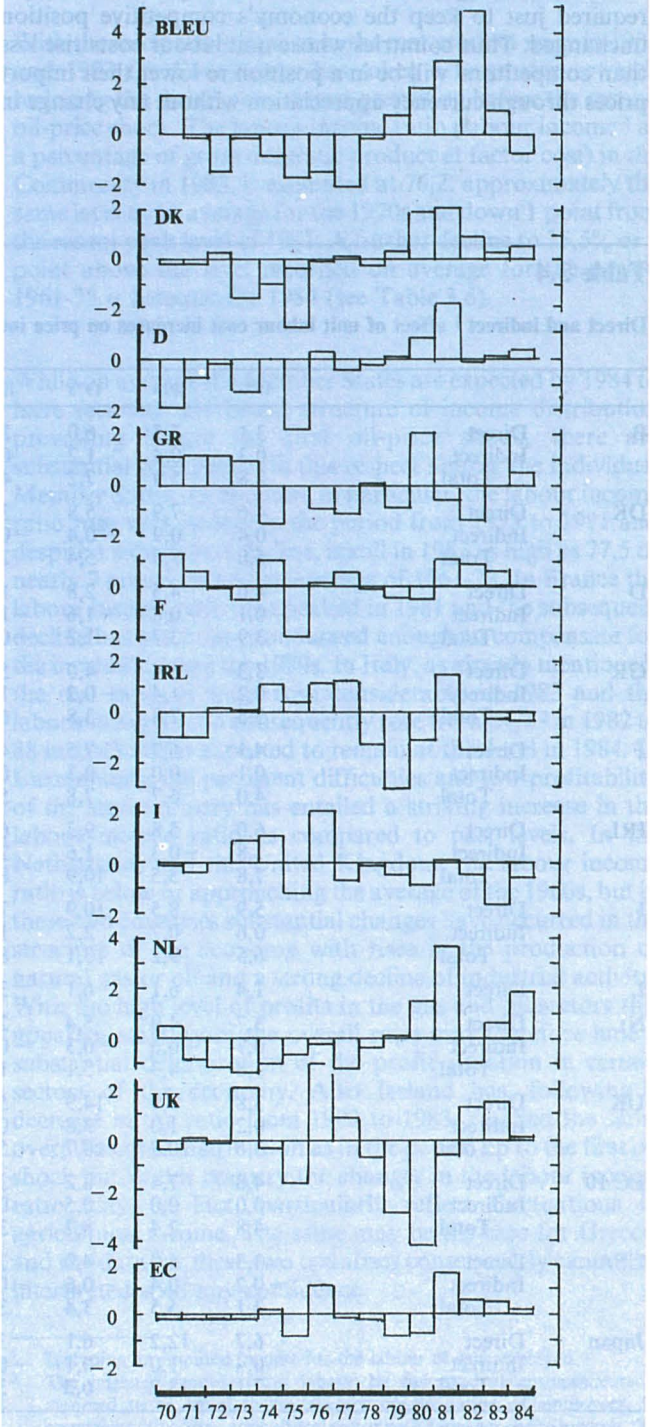
When external factors are eliminated from the comparison, the price performance of the Community indeed compares more favourably with that of the United States: as seen from the last column in Table 3.3, the domestic factors in 1983 contributed 5,6% to the final expenditure deflator in the Community and 4,0% in the United States. The similar figure for Japan, however, was as low as 1,1% and has in fact been 2% or below in all years since 1978. The 5,6% impact from domestic factors in the final expenditure deflator of the Community in 1983 also includes a 0,7% impact from increases in indirect taxes—which have been used much more extensively in the Community than in the United States for stabilization purposes. The contribution of domestic cost increases excluding indirect taxes in 1983 can be estimated at 4,9% in the Community—a lot closer to the US figure of 3,9%. In recent years, the contributions from unit labour costs and the residual item (including profit margin changes) have actually contributed similar amounts to the final expenditure deflator in the Community and the United States (see also Table 3.3).

3.3 The cost performance of individual Member States

The relative price performance of the individual Member States is likewise heavily influenced by real exchange rate changes. Graph 3.3 reveals several instances in which real effective exchange rate depreciations have at times resulted in a considerable boost to the overall price rise: Belgium (1980, 1981 and 1982), Denmark (1981), Germany (1981), Greece (1980 and 1983), Ireland (1981), the Netherlands (1981), and the United Kingdom (1976 and 1983). On the other hand, the larger real appreciation of sterling in 1979 and 1980 is estimated to have lowered the final expenditure deflator in the United Kingdom by 3 and 4 percentage points respectively.

The underlying price trend of the individual countries is, therefore, better identified in the domestic cost develop-

GRAPH 3.3: Contribution of the real exchange rate to total final expenditure deflator



Source: Eurostat and Commission services.

ments, and notably, the contribution of unit labour costs. The latter operates, however, not only *directly* but also *indirectly* through the nominal exchange rate changes required just to keep the economy's competitive position unchanged. Thus countries whose unit labour costs rise less than competitors' will be in a position to lower their import prices through currency appreciation without any change in competitive position while, in contrast, countries with higher-than-average unit labour cost increases suffer additional cost increases due to the depreciation of their currencies required to maintain competitiveness. Although in the short term a country may prefer to take a real exchange rate change (such as has been the case in several periods) the underlying cost performance eventually has to compensate

Table 3.4

Direct and indirect [1] effect of unit labour cost increases on price increases

(total final expenditure)

		1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
B	Direct	3,1	5,5	6,0	3,5	3,0	1,7	1,7	2,1	2,4	1,8	1,6	2,1
	Indirect	−0,3	0,4	1,2	0,7	0,1	−0,9	−1,1	−1,6	−0,7	−0,9	0,0	0,9
	Total	2,8	5,9	7,2	4,2	3,1	0,8	0,6	0,5	1,7	0,9	1,6	1,2
DK	Direct	4,6	7,9	5,8	3,1	3,7	3,8	3,4	4,7	3,5	3,3	2,0	1,5
	Indirect	0,4	0,9	−0,4	−0,4	0,0	0,3	−0,1	0,1	−0,3	0,1	−0,1	−0,2
	Total	5,0	8,8	5,4	2,7	3,7	4,1	3,3	4,8	3,2	3,4	1,9	1,3
D	Direct	4,0	4,5	2,8	1,0	1,8	1,6	1,6	2,8	2,0	1,5	0,4	0,4
	Indirect	−0,1	−0,8	−1,6	−1,2	−1,0	−0,8	−0,8	−0,9	−1,2	−1,0	−1,0	−0,8
	Total	3,9	3,7	1,2	−0,2	0,8	0,8	0,8	1,9	0,8	0,5	−0,6	−0,4
GR	Direct	3,3	6,4	4,0	5,0	5,7	4,9	6,1	5,6	7,1	8,3	5,5	5,2
	Indirect	0,2	1,4	−0,2	1,9	1,6	1,7	2,0	0,8	2,7	3,1	2,1	2,4
	Total	3,5	7,8	3,8	6,9	7,3	6,6	8,1	6,4	9,8	11,4	7,6	7,6
F	Direct	4,1	6,7	7,5	4,9	4,7	4,4	4,4	6,1	6,0	5,2	4,0	3,1
	Indirect	−0,1	0,0	0,3	0,3	0,3	0,3	0,2	0,5	0,6	0,7	0,6	0,4
	Total	4,0	6,7	7,8	5,2	5,0	4,7	4,6	6,6	6.6	5,9	4,6	3,5
IRL	Direct	6,0	5,8	9,3	6,4	3,6	4,2	6,9	6,7	5.8	4,4	3,2	2,2
	Indirect	1,8	−0,3	1,6	2,2	0,0	1,1	3,1	1,9	1,9	1,9	1,3	0,6
	Total	7,8	5,5	10,9	8,6	3,6	5,3	10,0	8,6	7,7	6,3	4,5	2,8
I	Direct	5,9	8,5	10,9	7,1	8,9	6,2	6,4	8,2	9,6	7,6	7,2	5,1
	Indirect	0,6	0,7	2,2	1,3	2,3	1,3	1,1	1,7	2,7	2,1	2,5	1,5
	Total	6,5	9,2	13,1	8,4	11,2	7,5	7,5	9,9	12,3	9,7	9,7	6,6
L	Direct	1,4	6,1	6,1	3,7	3,2	0,5	1,2	2,6	3,4	3,0	2,8	1,9
NL	Direct	3,7	4,9	5,4	2,3	2,6	2,2	2,2	2,0	1,2	1,7	0,2	−0,5
	Indirect	0,1	−0,6	−0,3	−0,7	−0,6	−0,6	−0,7	−1,6	−1,9	−0,8	−1,5	−2,0
	Total	3,8	4,3	5,1	1,6	2,0	1,6	1,5	0,4	−0,7	0,9	−1,3	−2,5
UK	Direct	3,8	9,9	14,9	5,1	4,5	4,8	7,2	9,6	5,0	2,2	1,8	1,8
	Indirect	−0,2	1,0	3,8	0,4	0,3	0,6	1,6	2,2	0,4	−0,4	−0,1	−0,1
	Total	3,6	10,9	18,7	5,5	4,8	5,4	8,8	11,8	5,4	1,8	1,7	1,7
EC 10	Direct	4,8	7,4	8,2	3,7	4,2	3,6	4,3	6,1	5,2	3,5	2,3	1,9
	Indirect	0,0	0,0	0,5	−0,1	0,1	0,0	0,2	0,5	0,3	0,0	0,1	0,0
	Total	4,8	7,4	8,7	3,6	4;3	3,6	4,5	6,6	5,5	3,5	2,4	1,9
USA	Direct	3,3	5,9	4,0	3,4	3,2	4,4	5,3	5,6	4,5	3,6	1,8	2,9
	Indirect	−0,2	−0,4	−0,6	−0,2	−0,2	0,1	0,2	0,0	−0,1	−0,0	−0,2	0,1
	Total	3,1	5,5	3,4	3,2	3,0	4,3	5,1	5,6	4,4	3,6	1,6	3,0
Japan	Direct	6,7	12,2	6,1	3,7	3,0	1,3	1,4	2,1	2,2	1,8	1,1	1,5
	Indirect	0,4	1,0	0,1	−0,1	−0,1	−0,4	−0,5	−0,8	−0,5	−0,6	−0,2	−0,2
	Total	7,1	13,2	6,2	3,6	2,9	0,9	0,9	1,3	1,7	1,2	0,9	1,3

[1] Effect on prices of the effective exchange rate change required to maintain constant competitiveness. See technical annex for method of calculation and qualifications. Factors assumed to be additive in totals.

Source: Eurostat and Commission services.

this if a serious disequilibrium is to be avoided in the balance of payments.

As seen from Table 3.4 the direct effect of unit labour costs on the final expenditure deflator in 1983 was as low as 0,4 points in the Federal Republic of Germany and 0,2 points in the Netherlands. Taking account of the indirect effects, labour costs in these two countries in 1983 actually exerted a *negative* influence on price (0,6 and 1,3 points respectively for the two countries). Belgium, Denmark and the United Kingdom in 1983 recorded total (direct and indirect) labour cost impacts below the Community average of 2,4 percentage points while Ireland, France, Greece and Italy form a group with the labour cost impact on the final expenditure deflator in the range of 4 to 10 points.

As could be expected, the four countries in this group were also those recording the highest rate of increase in *per capita* compensation of employees ranging in 1983 from 17,3% in Greece to 9,7% in France—see Table 3.4. In Italy, which had the second highest rise of *per capita* compensation in the Community in 1983 (15,6%), prices were kept in check by the real effective appreciation of the lira and real *per capita* compensation, after an increase of 0,4% in 1982, rose further in 1983. As domestic profit margins are being compressed without being compensated by productivity increases, the real product wage in Italy is estimated to actually show a strong increase (3,9%) in 1983—a development which can be considered normal in a year with a weak economic activity but which nevertheless is substantially out of line with developments elsewhere in the Community. In Ireland consumer prices in 1983 rise nearly as fast as *per capita* compensation but unlike in Italy the relative price and cost movements entail a reduction in the real product wage—following a large fall (3,3%) in 1982. Like Italy and Ireland, France in 1983 recorded a rise in real *per capita* compensation of employees but in contrast to the Italian experience, productivity increases and profit margins develop so as to entail a decline in the real product wage for the second consecutive year.

The remaining Member States (Denmark, Belgium, the Federal Republic of Germany, Luxembourg, the Netherlands and the United Kingdom) in 1983 record increases in *per capita* compensation below or (in the case of Denmark and the UK) only marginally above the Community average. Apart from Luxembourg, where adverse developments in the steel sector have influenced output, these countries all record a substantial decline in real wage costs as measured by the real product wage—although in the Federal Republic of Germany, Denmark, the Netherlands and the United Kingdom (largely due to a favourable productivity development) *per capita* compensation of employees actually rises faster than consumer prices and even substantially so (2,0 points) in the UK.

3.4 Income distribution and profitability of investments

With the fairly sharp decline in the real product wage in 1982 and 1983 the Community has taken a large step towards restoring the distributive shares prevailing before the second oil-price shock. The labour income ratio (labour income [1] as a percentage of gross domestic product at factor cost) in the Community in 1983, is estimated at 76,2, approximately the same level as on average for the 1970s and down 1 point from the recent peak level of 1981. A further decline to 75,5% or 1 point above the level recorded on average for the period 1961-73 is forecast for 1984 (see Table 3.6).

While on average the Member States are expected by 1984 to have restored this broad structure of income distribution prevailing before the first oil-price shock, there are substantial divergences in this respect among the individual Member States. In Belgium, in particular, the labour income ratio rose very steeply in the period from 1973 to 1981 and despite a subsequent decline, is still in 1983 as high as 77,5 or nearly 7 points above the average of 1961-73. In France the labour income ratio also peaked in 1981 and the subsequent decline has not been pronounced enough to compensate for the increase during the 1970s. In Italy, as already mentioned, the real product wage rose considerably in 1983 and the labour income ratio consequently rose from 84,7 [2] in 1982 to 88 in 1983 and is expected to remain at this level in 1984. In Luxembourg the persistent difficulties and low profitability of the steel industry has entailed a striking increase in the labour income ratio as compared to past levels. In the Netherlands and the United Kingdom, the labour income ratio is below or approaching the average of the 1960s, but in these two countries substantial changes have occurred in the structure of the economy with rises in the production of natural gas or oil and a strong decline of industrial activity. With the high level of profits in the gas and oil sectors this apparent stability of the overall ratio may therefore hide a substantial deterioration of the profit situation in certain sectors of the economy. Also Ireland has, following a decrease in the ratio from 1982 to 1983, reached the same overall income distribution as in the period up to the first oil shock but in this country the changes in the labour income ratio may, in fact, particularly reflect fluctuations in agricultural income. The same may be the case for Greece, and the data for these two countries consequently cannot be interpreted with any confidence.

1 Including an imputed income for the labour of self-employed.

2 The imputed income from labour by independent entrepreneurs is assumed to be equal to the average compensation of employees. In countries with a large agricultural sector with a low *per capita* income, this method of calculation may give an exaggerated estimate of 'labour income' as compared to more mature economies, but will not effect comparisons over time.

Table 3.5

Compensation of employees

(% change)

	1961-73 (average)	1974-79 (average)	1980	1981	1982	1983 [1]	1984 [2]
			Per capita *compensation of employees*				
B	8,9	12,0	8,8	7,3	8,0	6,0	7,7
DK	10,6	12,0	9,9	10,2	11,1	7,5	5,5
D	9,2	7,4	6,8	5,3	4,4	3,8	3,5
GR	10,5	21,6	14,8	23,9	26,2	17,3	18,5
F	9,9	14,8	14,8	14,5	14,5	9,7	8,2
IRL	11,5	18,5	19,5	18,5	14,9	12,2	8,9
I	11,5	19,9	22,2	22,0	17,1	15,6	12,4
L	7,5	11,0	7,8	7,7	6,9	7,1	5,9
NL	11,3	10,2	5,5	3,3	5,7	3,2	0,1
UK	8,3	17,3	20,2	14,7	8,8	7,9	6,3
EC 10	9,7	13,7	12,9	11,5	9,6	7,2	6,1
USA	5,6	8,1	9,3	9,5	6,0	5,0	6,7
JAP	14,1	12,4	6,4	7,1	5,1	4,7	5,1
			Real per capita *compensation of employees* [3]				
B	5,0	3,9	1,6	−1,5	0,5	−1,7	1,1
DK	4,3	1,3	−1,2	−1,5	1,2	0,9	0,1
D	5,3	2,6	1,4	−0,3	−0,8	0,8	0,3
GR	6,8	5,5	−6,1	−0,4	4,2	−2,6	0,0
F	5,0	3,9	1,4	1,5	3,3	0,6	1,0
IRL	5,3	2,9	1,6	−0,9	−1,9	1,1	0,1
I	6,4	2,4	1,6	2,5	0,4	0,5	0,8
L	4,3	3,3	0,1	0,0	−2,8	−1,2	−1,7
NL	5,8	2,7	−1,1	−2,8	0,0	0,4	−3,4
UK	3,2	1,5	3,2	3,3	0,7	2,0	0,5
EC 10	4,9	2,7	1,5	1,3	0,9	0,8	0,4
USA	2,4	0,5	−1,0	0,6	0,3	0,6	1,6
JAP	7,5	2,8	−0,6	2,5	2,2	2,9	3,5
			Real product wage [4]				
B	0,3	1,5	1,4	1,7	−1,7	−2,2	0,1
DK	0,3	0,7	1,4	−3,1	−3,0	−2,7	−2,1
D	0,3	−0,4	1,5	0,2	−1,3	−1,9	−1,7
GR	−2,2	2,5	−4,2	1,7	1,6	−1,2	−0,5
F	−0,3	1,0	1,7	1,1	−1,0	−1,1	−0,6
IRL	−0,2	0,1	6,5	0,3	−3,3	0,6	−1,0
I	−0,1	0,4	−1,0	4,1	−0,2	3,9	0,3
L	0,0	3,3	0,5	2,4	1,2	−0,6	−0,9
NL	1,0	0,2	−0,1	−2,4	−1,3	−0,9	−3,3
UK	0,2	0,1	2,1	0,3	−1,5	−1,1	−0,5
EC 10	0,0	0,3	1,1	1,1	−1,0	−0,3	−0,8
USA	0,0	−0,1	1,0	−0,6	1,3	−1,9	0,3
JAP	−0,8	1,5	0,0	1,8	1,0	1,6	1,3

[1] Estimates.
[2] Forecasts.
[3] *Per capita* compensation of employees deflated by the consumer price deflator.
[4] Real compensation of employees per unit of output (deflator - GDP price deflator).

Source: Eurostat and Commission services.

Table 3.6

Normalized labour income ratio [1]

	1961-73 (average)	1974-79 (average)	1980	1981	1982	1983	1984 (forecast)
B	70,6	76,8	79,2	80,6	79,2	77,5	77,6
DK	76,1	78,1	79,4	76,9	74,6	72,6	71,1
D	72,0	73,5	72,9	73,1	72,1	70,8	69,5
GR	91,2	83,0	85,0	86,5	87,9	86,8	86,4
F	72,1	74,1	75,7	76,6	75,8	74,9	74,5
IRL	87,4	86,5	90,8	91,0	88,1	87,6	86,7
I	80,0	83,6	81,5	84,9	84,7	88,0	88,2
L	67,7	80,1	81,1	83,1	84,1	84,6	83,9
NL	71,0	74,4	74,1	72,3	71,3	70,7	68,4
UK	73,6	74,8	75,7	75,9	74,7	73,9	73,6
EC 10	74,5	76,3	76,4	77,2	76,4	76,2	75,5

[1] Labour income, including an imputed income from labour of self-employed as a % of gross domestic product at factor cost.
Source: Eurostat and Commission services.

Two countries, Denmark and the Federal Republic of Germany have, through wage restraint in recent years, brought their labour income ratio considerably below the average of the 1960s. Denmark, in particular, where this ratio by 1980 had reached 79,4—or more than 3 points above the 1961-73 average—reduced the real product wage by 3,1, 3,0 and 2,7 points respectively the three following years, and is expected—after a further reduction in 1984—to record a labour income ratio of 71,1—5 points below the 1961-73 average. In the Federal Republic of Germany, the development has been very similar, albeit less pronounced. Nevertheless, by 1984 the German labour income ratio may be reduced to below 70%, the lowest level recorded there since 1960.

Although for the Community as a whole, the labour income ratio is now approaching the level prevailing before the first oil-price shock, considerable real wage adjustments may well be required to solve the problem of unemployment and the low investment propensity. In fact, as indicated in the box to Chapter 4 (real wages and employment) an excessive real wage level will not necessarily show up in a change in the income distribution, but may be reflected in a fall in employment, a rise in the capital intensity, and a decline in the profitability of invested capital—which is in fact what seems to have happened in the Community over the last 15 years.

Admittedly, statistical data on profitability are particularly uncertain. There are important methodological problems involved in the evaluation, both of profits, and of the value of capital against which to measure the rate of return. Thus profits may be measured as the gross or net operation surplus (entity concept of profits) according to the national accounts concept which is calculated before deduction of interest payments and company taxes. After deduction of net interest payments and taxes, one obtains the so-called equity concept of profits which is a measure of the remuneration of the equity capital.

The most commonly used macroeconomic profit ratio, measures the gross or net operating surplus against the stock of fixed capital estimated, either at historical cost or at replacement (current) cost.This profitability indicator is broadly consistent with the macroeconomic income distribution indicators utilized above (real product wage or labour income ratio), but will rarely give an appropriate measure of the relative profitability of investment in risk capital as opposed to investment in, say, government bonds.

The decline in profitability in the enterprise sector in European countries for which comparable data are available is shown in Table 3.7 which reproduces estimates prepared by the Deutsches Institut für Wirtschaftsforschung. Profitability, measured as the net rate of return on fixed capital stock at replacement cost, in the Community was, in the 1980s, less than half the level recorded, on average, in the period 1960-73. The fall in profitability was particularly pronounced in France, Italy, Belgium and the United Kingdom while in the Federal Republic of Germany and the Netherlands, profit rates declined less significantly. The current low estimates of rates of return may be somewhat

Table 3.7

Net rate of return on fixed capital (enterprises excluding construction) [1]

	1960-73	1974-80	1978	1979	1980	1981
B	11,0	6,8	6,2	6,0	3,6	2,8
D	11,6	8,3	9,1	9,6	8,6	7,6
F	14,2	7,7	7,1	6,8	4,8	5,1
I	7,5	1,9	0,8	2,9	3,6	0,7
NL	10,1	8,4	10,1	9,0	7,7	6,8
UK	8,0	2,8	4,5	2,5	0,7	0,2
EC 6	10,6	5,9	6,2	6,1	4,9	4,0

[1] Net operating surplus as % of the capital stock calculated at replacement cost.
Source: Estimates of the Deutsches Institut für Wirtschaftsforschung.

biased in this data due to the statistical difficulties in measuring profits and capital in a time of rapidly-changing technologies and deep recession. It should, in particular, be noted that the national accounts estimates, on which most measures of profitability are based, make no allowance for accelerated depreciation of obsolete capital. This results in a substantial downward bias in the measured rate of return, since the capital stock actually in use or potential use is lower than recorded (although this is partially compensated for by higher consumption of fixed capital than recorded). Another factor depressing recorded profits in the short term (through redundancy payments which are deducted from profits in the national accounts) is the closure of uneconomic parts of enterprises, decisions about which are taken on the basis of the need to restore corporate profit in the longer run. A final element which should be kept in mind in analysing these figures is that they are pre-tax figures, while the post tax figures are unlikely to show such a steep downward trend.

The level of profitability, on the basis of the figures in Table 3.7, was lowest in the United Kingdom in 1981 followed by Italy and Belgium, while it was highest in the Federal Republic of Germany and the Netherlands followed by France. However, the factors cited above make the comparison of levels between countries hazardous and, in addition, sectoral classifications can introduce distortions in the comparison (e.g. inclusion of oil sector in the United Kingdom).

Despite the factors mentioned above, which exert a downward bias on recorded figures of rates of return, a substantial profitability problem has undoubtedly been present in the late 1970s and early 1980s in the Community. The evidence cited earlier in this chapter on the behaviour of the labour/income ratio in more recent years and in the balance-of-payments chapter on the competitiveness of the Community *vis-à-vis* its principal trading partners, would suggest that some easing of the pressure on enterprises is under way.

Inflation and wages in the Community [1]

The literature on the determination of wages is extensive. Much empirical and theoretical work has been done on the interrelation between unemployment and money wage inflation since A.W. Phillip's paper 25 years ago [1] and its extension by Lipsey [2] two years later using standard statistical techniques. This explanation gave reasonable predictions of the behaviour of money wages both in the short and long run-up to the late 1960s but thereafter its predictive power failed with rising unemployment and inflation. About this time concentration shifted to the natural rate of unemployment, based on the work of Friedman [3] and Phelps [4] and the role of price expectations in the wage setting process was emphasized. This led to the concept of the expectations augmented Phillips curve which, when later combined with rational expectations as in Lucas [5], implied that the long-run Phillips curve was vertical and even questioned the proposition of a short-run tradeoff, as the slope could, under certain circumstances, be positive. Recent experience of rising unemployment and falling wage inflation has tended to rehabilitate the Phillips curve, although now with an expectations content. Analysis has generally concentrated on the employment effects of changes in real wages with negative relationships being found by Grubb, Layard and Symons [6], Bruno [7] and Sachs [8], while Geary and Kennan [9] find no link. [2] Other analysis of wage behaviour has emphasized cost pressures, highlighting competing wage claims by different groups of labour, real wage resistance and maintaining that the inflation of the 1970s has emerged from a struggle over the distribution of income. Recent econometric work by Artis and Ormerod [10] using the real wage approach, which as they point out, can also be considered in the Phillips curve tradition if the inclusion of a lagged real wage term is considered as an alternative way of measuring the excess demand for labour, suggests that, except for the Federal Republic of Germany, there is no long-run tradeoff, as wage claims generally take expected inflation completely into account.

In general, global econometric models for Community countries have tended to express labour market conditions and expected inflation rates as the main determining factors of changes in wages. The graph shows the relationship suggested by theory and previous studies. The results, which express real expected wages as a function of unemployment, are mixed. Only for France and, to a lesser extent Belgium, have results emerged which obviously support a fairly stable tradeoff between unemployment (representing the level of demand) and expected real wage increases. For most countries, however, inflation expectations or lagged inflation rates, where indexation was applied, are an important element in pay increases. When a variable for lagged inflation rates is included in regressions for wage determination, it has been found that it is not usually statistically significant, but if the dependent variable is redefined as expected real wage increases, the statistical parameters of most equations are improved.

No significant structural shift has been found in the relationship covered over time but what does emerge in the French and Belgian case is the non-linear nature of the tradeoff with little evidence that, on the basis of the figures for this period, real wage increases will be negative at any level of unemployment. For most other countries the evidence is less clear but there does appear to be a inverse relationship between real wage increases and the level of unemployment. Individual incomes policy episodes show up quite clearly in the data. They had moderated wage increases substantially in 1976/77 in the United Kingdom (Healey/TUC 5%) and the Netherlands in the same period (6 months wage freeze), but subsequent 'catch up' phases have tended to compensate for these periods of restraint.

The overall conclusion to be drawn from country developments shown above must be that current levels of deficient demand (as measured by unemployment) have a depressing effect on wage increases. However it is also clear that anticipated inflation also plays a significant role, with wage-earners endeavouring to maintain the real expected value of their incomes. Little evidence exists for any significant change in the relationship over the period shown and, while incomes policies have had substantial effects on wage settlements, avoiding catch-up wage increase after the removal of controls, remains a problem.

[1] The figures in brackets in the text refer to the following bibliography.

[2] On this aspect see also box on real wages and employment in Chapter 4.

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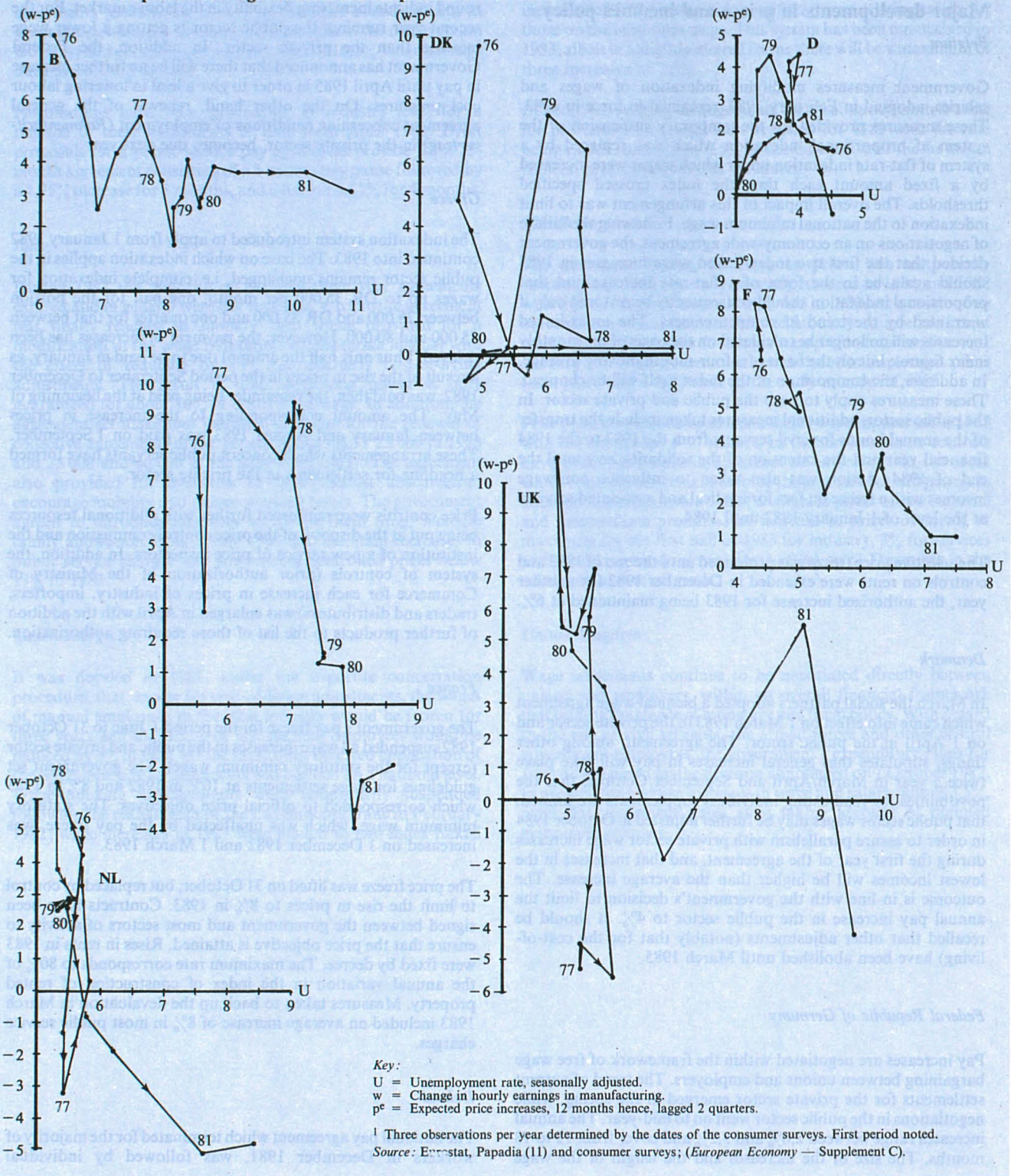
GRAPH 3.4: **Expected real wage increases and the pressure of demand** [1]



Key:
U = Unemployment rate, seasonally adjusted.
w = Change in hourly earnings in manufacturing.
p^e = Expected price increases, 12 months hence, lagged 2 quarters.

[1] Three observations per year determined by the dates of the consumer surveys. First period noted.
Source: Eurostat, Papadia (11) and consumer surveys; (*European Economy* — Supplement C).

Major developments in prices and incomes policy

Belgium

Government measures modifying indexation of wages and salaries, adopted in February 1982, remained in force in 1983. These measures provided for the temporary suspension of the system of proportional indexation which was replaced by a system of flat-rate indexation under which wages were increased by a fixed amount each time the index crossed specified thresholds. The overall impact of this arrangement was to limit indexation to the national minimum wage. Following the failure of negotiations on an economy-wide agreement, the government decided that the first two index-linked wage increases in 1983 should again be in the form of a flat-rate increase and that proportional indexation should consequently be restored only if warranted by the trend in competitiveness. The index-linked increases will no longer be calculated on the basis of the monthly index figures, but on the basis of a four-month moving average. In addition, the composition of the index itself will be changed. These measures apply to both the public and private sector. In the public sector, additional measures taken include the transfer of the annual bonus for civil servants from the 1983 to the 1984 financial year and the extension of the solidarity levy until the end of 1984. Action was also taken to influence non-wage incomes with a freeze on fees for medical and associated services at the level of 1 January 1982 until 1984.

The selective price freeze was prolonged until the end of 1983 and controls on rents were extended in December 1982 for another year, the authorized increase for 1983 being maintained at 6%.

Denmark

In March the social partners adopted a biennial wage agreement which came into effect on 1 March 1983 in the private sector and on 1 April in the public sector. The agreement, among other things, stipulates that general increases in pay will take place twice a year in March/April and September/October, that the possibilities for readjusting individual supplements are limited, that public sector wages may be further adjusted in October 1984 in order to assure parallelism with private sector wage increases during the first year of the agreement, and that increases in the lowest incomes will be higher than the average increase. The outcome is in line with the government's decision to limit the annual pay increase in the public sector to 4%. It should be recalled that other adjustments (notably that for the cost-of-living) have been abolished until March 1985.

Federal Republic of Germany

Pay increases are negotiated within the framework of free wage bargaining between unions and employers. The trend of current settlements for the private sector emerged in the spring, while negotiations in the public sector went on to mid-year. The annual increases range between 2,6% and 3,2% and cover from 12 to 18 months. The size of the increases and the length of the wage round indicate increasing flexibility in the labour market. For the second year running, the public sector is getting a lower wage increase than the private sector. In addition, the Federal Government has announced that there will be no further increase in pay until April 1985 in order to give a lead in lowering labour cost pressures. On the other hand, renewal of the general agreement concerning conditions of employment (*Rahmentarifvertrag*) in the private sector, becomes due next year.

Greece

The indexation system introduced to apply from 1 January 1982 continued into 1983. The base on which indexation applies in the public sector remains unchanged, i.e. complete indexation for wages up to DR 35 000 per month, one half for the portion between 35 000 and DR 55 000 and one quarter for that between 55 000 and 80 000. However, the payment of increases has been delayed. Thus only half the amount due to be paid in January, as a result of the rise in prices in the period September to December 1982, was paid then, the remainder being paid at the beginning of May. The amount corresponding to the increase in prices between January and August 1983 was paid on 1 September. These arrangements which concern public servants have formed a headline for settlements in the private sector.

Price controls were reinforced further with additional resources being put at the disposal of the price control commission and the institution of a new service of price inspectors. In addition, the system of controls (prior authorization of the Ministry of Commerce for each increase in prices of industry, importers, traders and distributors) was enlarged in April with the addition of further products to the list of those requiring authorization.

France

The government's pay freeze for the period 1 June to 31 October 1982 suspended all wage increases in the public and private sector (except for the statutory minimum wage). The government set guidelines for wage settlements at 10% in 1982 and 8% in 1983 which corresponded to official price objectives. The statutory minimum wage, which was unaffected by the pay freeze, was increased on 1 December 1982 and 1 March 1983.

The price freeze was lifted on 31 October, but replaced by control to limit the rise in prices to 8% in 1983. Contracts have been signed between the government and most sectors of activity to ensure that the price objective is attained. Rises in rents in 1983 were fixed by decree. The maximum rate corresponds to 80% of the annual variation in the index of construction of rented property. Measures taken to back up the devaluation in March 1983 included an average increase of 8% in most public service charges.

Ireland

The national pay agreement which terminated for the majority of workers in December 1981, was followed by individual

agreements (collectively known as the 22nd round) which, in general, extended for 15 months (16 months in the construction industry) and provided average increases of 16,2% for an average duration of 15.2 months.

Negotiations have been proceeding at industry level for a renewal of these agreements to date from April 1983. Draft proposals for a public service pay agreement provide for a 15-month agreement consisting of a 6-month pay pause followed by a 4,75% increase for 5 months, and a further 3,25% for 4 months.

Italy

During 1982 the majority of national three year agreements expired and in general were not renewed. A tripartite agreement was finally reached in January 1983 which provided for a modification in the wage indexation system (*scala mobile*) with the effect of reducing by 15% the quarterly cost-of-living adjustments. The result is that purchasing power is only guaranteed for about 70% of the average wage. In addition, the agreement set maximum increases of wages for the renewal of collective agreements in the period 1983-85 (LIT 25 000 in 1983 and 35 000 and 40 000 in the following years). The agreement also provided for measures to fight against absenteeism, encourage mobility and reduce working hours. The government agreed to introduce measures to reduce fiscal drag, increase family allowances from 1 July 1983 and maintain increases in public service charges and government controlled prices below 13% in 1983.

Luxembourg

It was decided in 1981, under the tripartite concertation procedure, that, except for cost-of-living adjustments, the wages of manual employees in the steel industry would be frozen for three years and that those of non-manual employees would be reduced by 3% in 1981. At the same time, deferred application of the wage-indexing arrangements was decided on a national level. Wage-indexing arrangements were temporarily suspended following the realignment of the Luxembourg franc in February 1982; wage increases in 1982 were limited to two index-linked increases of 2,5% each, with specific measures being taken for those on the minimum wage. This system has been maintained in 1983, albeit in a slightly altered form; there will be a maximum of three increases of 2,5%.

In addition, existing arrangements for a solidarity contribution for professional incomes were renewed for 1983 with the rate being raised from 5% to 6,5% of net incomes, and the freeze on traders' profit margins was extended.

The Netherlands

The automatic linking of wages to prices was temporarily suspended in 1980 and only partially restored in 1981 and 1982 with the top range of incomes excluded in 1982. As a result of an agreement between the two sides of industry on a reduction of working hours in return for the giving-up of indexation due on 1 January 1983, the government decided not to implement plans for a price and wage freeze in the early months of 1983.

Price controls in industry and commerce were suppressed in 1983 with the exception of 17 sectors. In the services sector controls have been maintained in all except seven sectors. In the areas where controls still remain in force the government will permit in addition to the incorporation of changes in prices of raw material and intermediate products, an increase in prices of 1,15% at maximum for the first half of 1983 for industry, 3% for services and the maintenance of margins in effect on 31 December in the wholesale and retail trade.

United Kingdom

Wage settlements continue to be negotiated directly between unions and employers, within an overall financial framework that reflects the stance of monetary and fiscal policy. With regard to the pay of civil servants, the armed forces and other central government employees, the government's expenditure plans for 1983-84 are based on the decision announced on 1 October 1982, to provide for average increases in wage and salary bills of 3,5%, from due settlement dates after taking account of planned manpower changes.

4. The labour market

The labour market once more recorded increasing unemployment in 1982 and 1983, although signs of stabilization began to appear from April 1983. A longer-term view based on the results of labour force surveys highlights the complexity of the situation and implies that it is caused by a combination of various factors. At a time when the labour market is especially slack, socio-economic factors that increase participation rates and demographic trends resulting in an increase in the population of working age magnify the effects of a contraction in employment due to stagnation. The employment situation of women has deteriorated as well as that of men, although male and female unemployment show different features. With the growth of unemployment generally, the problems of youth unemployment and long-term unemployment have been accentuated. All this means that there cannot be a single quick solution to the problem: even a stronger recovery than the one at present emerging would not produce a substantial improvement in the labour market. Measures on several fronts to deal with the structural aspects of unemployment are still as necessary as ever.

4.1 Trends and prospects on the labour market

Against a background of slack economic activity ever since 1980, total employment has once more contracted in the Community as a whole (see Table 4.1); the contraction of 1,4% in 1982 will probably be followed by a further drop of 0,9% in 1983. This decline in 1983 affects practically all the Member States, with contractions ranging from 0,4% in Denmark to 2,1% in the Netherlands; the only exception is Italy, where employment is likely to expand by 0,5% in 1983. A further contraction of 0,2% for the Community as a whole is expected in 1984, the only Member State where a slight expansion is predicted being Italy. Employment trends are particularly disturbing in the manufacturing sector, where

Table 4.1

Employment and unemployment in the Community

	Total employment % change					Rate of unemployment as % [3]				
	1970-80 (average)	1981	1982	1983 [1]	1984 [2]	1970	1981	1982	1983 [1]	1984 [2]
B	0,3	−2,1	−2,0	−2,0	−0,8	(2,1)	(11,2)	(13,1)	14,9	15,9
DK	0,7	−1,9	0,1	−0,4	−0,9	1,0	8,2	8,8	9,7	10,6
D	−0,1	−0,7	−1,8	−2,0	−0,4	0,6	4,7	6,8	8,5	8,7
GR	0,6	0,1	−1,3	−1,0	−0,2	:	(4,1)	(6,1)	(7,8)	(8,7)
F	0,4	−0,7	−0,8	−1,0	−0,7	1,3	7,8	8,8	9,0	9,8
IRL	1,0	−1,9	−1,4	−1,8	−0,8	5,3	10,2	12,3	15,4	17,6
I	0,5	0,5	−0,4	0,5	0,6	4,4	8,8	10,5	10,9	11,4
L	1,3	0,2	0,1	−1,1	−1,2	0,0	1,0	1,3	1,9	2,4
NL	0,2	−1,3	−2,2	−2,1	−1,4	(1,3)	(8,8)	(11,7)	14,3	16,2
UK	0,0	−5,3	−2,5	−0,6	0,0	2,3	9,6	11,2	11,9	12,0
EC	0,2	−1,6	−1,4	−0,9	−0,2	(2,0)	7,8	9,4	10,4	10,9

1 Estimate.
2 Forecast.
3 Number of unemployed as % of civilian labour force. Eurostat definition (for Greece: national definition and Commission services).

Sources: Eurostat, and Commission services.

the employed labour force is expected to contract by 0,7% in 1984 after 3,3% in 1982 and 2,4% in 1983.

This decline in employment is one of the factors in the expansion of the unemployment rate from 7,8% in 1981 to 10,4% in 1983 and a predicted 10,9% in 1984. After March 1983 there were some signs that the index was stabilizing, but not sufficiently strongly to imply a real improvement. The trend is unfavourable in all the Member States to a greater or lesser extent: excepting Luxembourg, where the rate is very low, and Greece, for which strictly comparable figures are not yet available, the rate of unemployment ranges from 8,5% in the Federal Republic of Germany to 15,4% in Ireland. It is expected to rise in all the Member States in 1984.

Productivity gains were fairly low in the Community in 1983, and are not expected to be better in 1984. Gross domestic product per person employed will expand by only 1,5% this year (compared with an annual average of 2,1% from 1973 to 1980: see Table 4.2). However, trends vary from one country to another. In Denmark, Ireland and the United Kingdom, productivity has increased faster in recent years than it did from 1973 to 1980. Other countries, particularly France, Italy, Luxembourg, Belgium, Greece and the Netherlands, have recorded very small productivity gains in the past few years. The latest forecasts indicate that no country except Italy is likely to see a genuine improvement in 1984, and the rate of productivity gains is even expected to slow down somewhat in 1984 compared to 1983 in Denmark, Ireland, the Netherlands and the United Kingdom.

Productivity has fared better in manufacturing industry. Value added per employee at constant prices will show an increase of 3,5% in 1983, and probably 2,9% in 1984. The longer-term trend is shown in a comparison between annual average growth rates for 1960-73 and 1973-82 in Table 4.3. The figures indicate that, while annual productivity gains slowed down from 4,8% in the earlier period to 3,2% in the latter, they were still relatively high, especially when compared to the average of 1,3% in the USA. The reason why manufacturing productivity has been better than that in the economy as a whole is clearly apparent from Graph 4.1, which shows the post-1960 trend in seven Member States. For three countries, Belgium, Denmark and the United Kingdom, the rate of gain is higher from 1981. Indeed, although it is lower than the rate observed in the late 1960s and early 1970s, the annual average increase in productivity in manufacturing industry in these three countries is tending upwards again and is even more stable in the United Kingdom. In Belgium and the United Kingdom especially, there has been evidence of a substantial degree of rationalization in manpower utilization.

More recently, the rate of growth of productivity recovered in the Federal Republic of Germany and the Netherlands, in 1983. Only in France and Italy was there no significant change, with productivity since 1980 progressing at a less rapid pace than previously. No significant change in trend is expected for 1984, except a slowdown in the United Kingdom.

Table 4.2

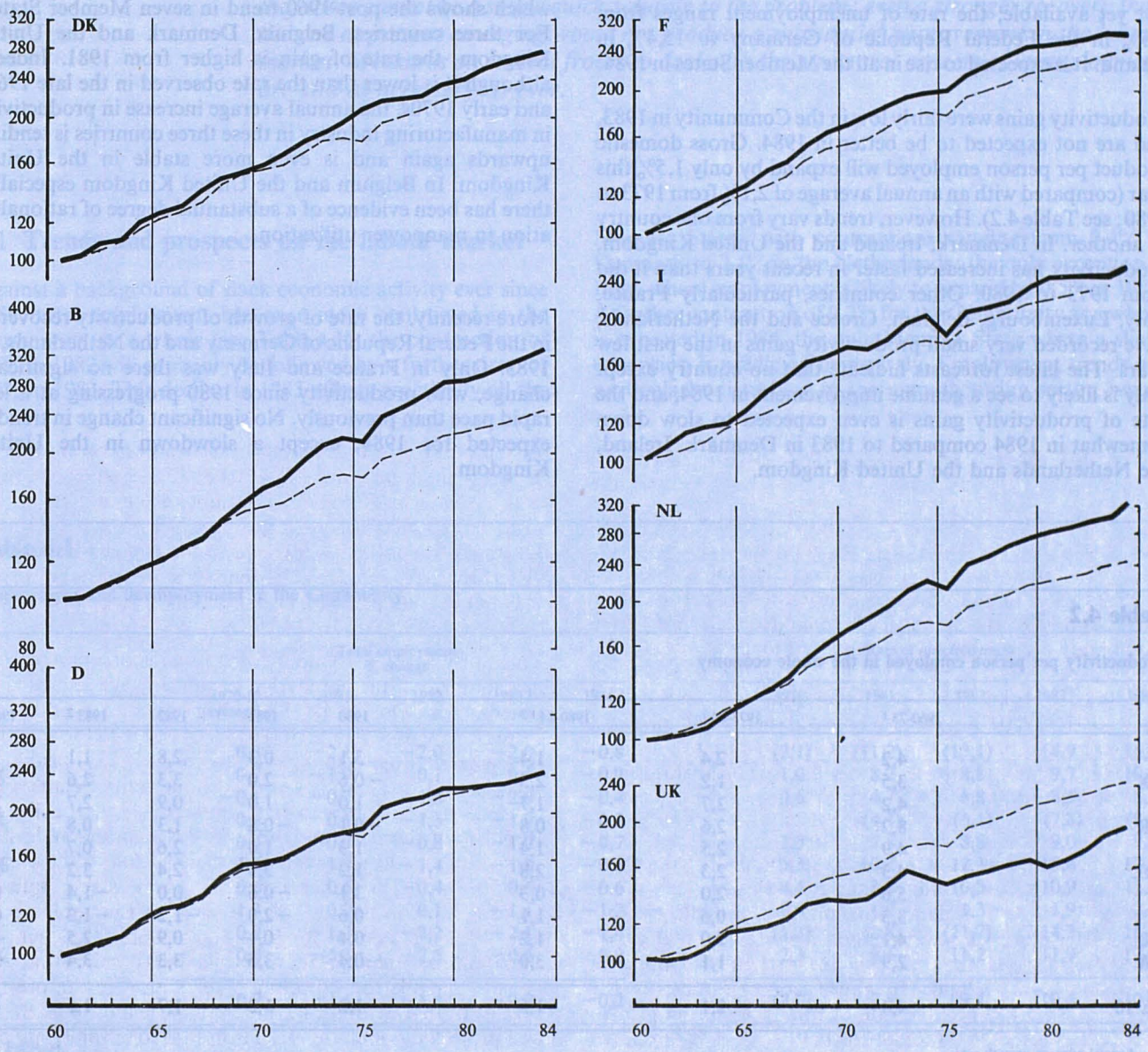
Productivity per person employed in the whole economy

	1960-73 [1]	1973-80 [1]	1980-84 [1 3]	1980	1981	1982	1983 [2]	1984 [3]
B	4,2	2,4	1,4	3,1	0,3	2,8	1,1	1,5
DK	3,5	1,2	2,5	−0,6	2,0	3,3	2,6	2,1
D	4,2	2,7	1,7	1,0	1,0	0,9	2,7	2,5
GR	8,2	2,6	0,8	−0,1	−0,8	1,3	0,8	1,8
F	4,9	2,5	1,4	1,3	1,0	2,6	0,7	1,3
IRL	4,3	2,3	2,8	1,2	3,1	2,4	3,2	2,6
I	5,6	2,0	−0,3	3,1	−0,6	0,0	−1,4	0,9
L	3,3	0,6	−1,1	0,6	−2,0	−1,2	−1,3	0,2
NL	4,1	2,0	1,2	0,4	0,1	0,9	2,5	1,5
UK	2,9	1,1	3,0	−0,4	3,5	3,3	3,4	2,2
EC 10	4,4	2,1	1,5	1,2	1,2	1,7	1,5	1,7

1 Annual average growth rate.
2 Estimate.
3 Forecast.

Sources: Eurostat and Commission services.

GRAPH 4.1: **Productivity per employee in manufacturing industry** [1] 1960 = 100



[1] Semi-logarithmic scale.

Table 4.3

Working hours and productivity in manufacturing industry

	Working hours				Productivity			
	Total hours [4]		Average hours [2]		Per employee [5]		Per hour	
	1960-73 [1]	1973-82 [1]	1960-73 [1]	1973-82 [1]	1960-73 [1]	1973-82 [1]	1960-73 [1]	1973-82 [1]
B	−0,5	−4,7 [3]	−1,0	−1,1 [3]	5,9	4,9 [3]	7,0	6,1 [3]
DK	−1,1	−2,1	−1,4	−0,4	5,0	3,7	6,4	4,0
D	−0,2	−2,6	−0,8	−0,9	4,7	3,1	5,4	4,2
F	0,6	−2,5	−0,5	−1,0	5,3	3,5	6,0	4,5
I	−0,1	−0,7	−1,5	−0,4	5,3	3,2	6,9	3,7
NL	−1,1	−3,2 [3]	−1,1	−0,8 [3]	6,4	4,3 [3]	7,6	5,2 [3]
UK	−1,2	−4,4	−0,7	−1,0	3,5	1,4	4,3	2,5
EC	−0,3	−2,7	−0,8	−0,9	4,8	3,2	5,6	4,1
USA	1,6	0,0	0,1	−0,3	3,2	1,3	3,0	1,5
Japan	2,1	−0,2	−0,9	0,1	9,7	6,3	10,7	6,2

1 Annual average growth rate.
2 Average hours worked per employee (USA: per employes person).
3 1973-81.
4 Number of employed (USA: employed persons) multiplied by average number of hours worked.
5 USA: per employed person.

Sources: Eurostat, US Bureau of Labour Statistics, and Commission services.

4.2 Population trends and participation rates

The present disequilibrium in the labour market is still due not only to the contraction of employment, but also to the fairly rapid increase in the labour force, determined both by demographic factors and by changes in the participation rate. Until 1982, the labour force expanded faster than total population (see Table 4.4): from 1970 to 1980, the annual average rate of expansion of the labour force was 0,6% compared with 0,4% for total population. Both rates slowed down in the 1980s, but the gap between them only narrowed temporarily in 1982 and 1983. It is expected that the rate of expansion of the labour force in 1984 will be again double that of total population.

Labour force trends vary from one Member State to another. During the 1970s the rate of expansion was 1% or more in Denmark, Greece, Ireland, Luxembourg and the Netherlands. The labour force expanded faster than total population in all countries except the Federal Republic of Germany and Ireland. In those countries, as in the Netherlands and Italy, the rate of total population growth speeded up after 1980 (except for the negative figure in the Federal Republic of Germany in 1983), while it declined in the other Member States and actually became negative in the United Kingdom (1981 and 1982), in France (1983) and in Luxembourg (1983). The trend has now been reversed in the United Kingdom, but the forecast is still negative for France and Luxembourg. No other significant change in growth rates is expected in 1984, except a substantial decline in Denmark and a further increase in the Federal Republic of Germany. In eight of the 10 Member States the labour force will still expand as fast as total population, or faster.

This fairly sustained labour force trend is due partly to the development of the population of working age and partly to other factors. During the 1970s, the population aged 15 to 64 increased by an average of 0,6% a year. Since then the rate increased slightly to stabilize at about 0,8% after peaking at 1,1% in 1981 (see Graph 4.2). The Community figure reflects a higher rate of growth in Denmark, Italy, the Federal Republic of Germany and the United Kingdom—indeed the present rate in the latter three countries is double the average for 1970-80. The other countries show stable rates of expansion or, in the case of France, a considerable decline after 1982. Projections for 1984 do not imply any change in the situation, and longer-term projections confirm that there are no grounds for expecting a relaxation in the pressure exerted by demographic factors until the end of 1986. Recent and projected population trends in the Community are thus particularly important in that they lead to an expansion of age-groups in the middle of the pyramid, and thus to potential growth of the labour force.

Table 4.4

Total population, labour force, working-age population in the Community

(% change)

	Total population					Working age population [3]					Civilian labour force				
	1970-80 (average)	1981	1982	1983 [1]	1984 [2]	1970-80 (average)	1981	1982	1983 [1]	1984 [2]	1970-80 (average)	1981	1982	1983 [1]	1984 [2]
B	0,2	0,1	0,0	0,1	0,1	0,6	0,1	0,3	0,4	0,4	0,8	0,1	0,5	0,0	0,2
DK	0,4	0,0	−0,1	−0,1	−0,1	0,4	0,7	0,5	0,5	0,4	1,2	0,8	0,6	0,7	0,3
D	0,1	0,2	−0,1	0,0	0,0	0,6	1,5	1,3	1,2	0,8	0,1	0,8	0,4	−0,1	0,2
GR	0,9	0,9	0,6	0,8	0,8	1,0	1,5	0,8	0,7	0,8	1,3 [1]	0,8 [1]	0,8 [1]	0,8	0,8
F	0,6	0,5	0,5	0,5	0,4	0,8	1,2	0,2	0,3	0,3	0,8	0,3	0,7	−0,3	−0,1
IRL	1,4	1,2	1,2	1,1	1,1	1,7	1,9	:	:	:	1,0	2,0	1,5	1,6	1,4
I	0,5	0,2	0,2	0,2	0,1	0,5	1,0	1,1	1,1	0,8	0,9	1,3	0,3	1,1	1,2
L	0,7	0,1	0,1	−0,1	0,0	1,1	0,0	0,0	0,0	−0,1	1,3	0,4	0,3	−0,5	−0,6
NL	0,8	0,7	0,5	0,4	0,4	1,4	1,3	0,5	0,5	0,4	1,2	3,0	2,7	1,1	1,0
UK	0,1	0,0	0,0	0,1	0,1	0,3	0,6	0,6	0,7	0,7	0,6	−0,6	−0,9	0,1	0,2
EC	0,4	0,3	0,2	0,2	0,2	0,6	1,1	0,8	0,8	0,6	0,6	0,5	0,3	0,3	0,4

[1] Estimate.
[2] Forecast.
[3] Population aged 15-64.

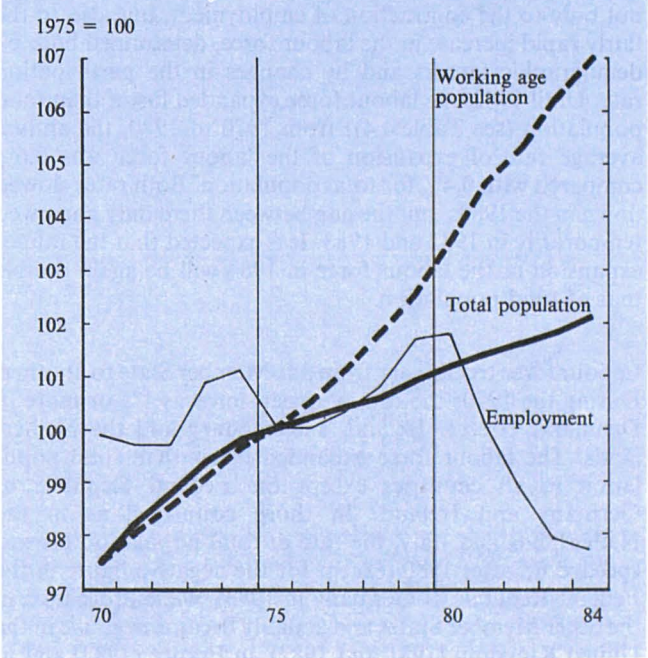
Sources: Eurostat and Commission services.

The supply of labour is also affected by the participation rate, defined as the proportion of the population of working age who are part of the labour force. The rising trend of this rate over the past few years is a net result of the decline in the male participation rate and the increase in the female participation rate.

Since the participation rate is so important a factor in the labour supply, a detailed long-term analysis is required. The role of structural factors is preponderant; valuable information on this aspect is supplied by the finding of the two-yearly labour surveys, of which the 1981 results have just been made available. [1] They confirm the rising trend of participation rates in the central age groups (ages 25 to 54) already noted in 1975, 1977 and 1979 (see Table 4.5). They also confirm that the rising trend is due to the net effects of an increase in the female participation rate and a decrease in the male rate, except in the 25 to 29-year-old group. Among younger age groups (ages 14 to 24), the situation is different: in 1981, their participation rate increased (after having declined in earlier years), mainly owing to a higher rate among young men.

The decline in participation rates among adult males would seem to be mainly attributable to the depressed nature of the

GRAPH 4.2: **Population and employment**



[1] See the methodological annex for a detailed description of the survey.

labour market (the 'discouraged worker' effect) and to the negative correlation between participation and real wage rises. The increase in female participation is due to a whole set of factors such as the development of the tertiary sector, a higher level of education, the development of back-up facilities such as creches and nursery schools and, sometimes, a reaction to the recession (the 'added worker' effect). The rising trend of participation rates among the young age groups, particularly young men, seems to be due to earlier entry to the labour market (see section 4.3). The net result of these trends is an increase in the aggregate participation rate that combines with unfavourable population trends, against a background of economic stagnation, to swell the labour supply at a time of weak labour demand, and to accentuate disequilibrium on the labour market.

4.3 The features of Community unemployment

The results of the labour force survey are also useful in analysing in more detail the structure and nature of Community unemployment, and in assessing more accurately its component elements. Although it is difficult to draw definite conclusions from the data available, it would seem that the cyclical trends of male and female unemployment are different. [1] Male unemployment rates were fairly stable from 1977 to 1979, after the large increase from 1973 to 1975, following the first oil shock. There was a further upsurge after 1979, due to the cyclical downturn that followed the increase in oil prices and the adoption of restrictive anti-inflationary monetary policies. Female rates, on the other hand, increased steadily from 1973 to 1981. These developments imply that male unemployment is more sensitive to the level of economic activity, in line with the view that male unemployment is mainly due to a decline in the demand for labour whereas female unemployment is mainly determined by an increase in the supply. Consequently, a sustained recovery could be expected to result in a relatively larger expansion in male than in female employment, while female employment would benefit in the longer term by the gradual increase in the tertiary sector's share in the economy.

The expansion of unemployment from 1973 to 1981 accentuated the difficulties facing certain categories of workers, who were already at a disadvantage: young people (and especially young women: see below) and older people. Chances of older workers have diminished also because of the lack of occupational and geographical mobility; at the same time young workers' chances of finding stable jobs have not increased (see Table 4.7). In 1981 the rate of unemployment among 14 to 24-year-olds was 14%: 2,3 times the aggregate rate, and over 3 times the adult rate. The updating of the survey at the end of March 1983 assessed the rate of unemployment among young people at 26,4%, or 2,4 times the aggregate rate. The situation of workers aged 25 to 29 also appears to be worsening; these workers were in the lower age group at the beginning of the period, and their chances of finding a job have not improved as they have grown older. Although the rate of unemployment among young people did not increase faster than the aggregate rate

[1] The trend of unemployment emerging from the survey data is strictly parallel to the trend of registered unemployment. The survey figures are lower than those for officially registered unemployment because some people may have provisionally or permanently withdrawn from the labour force, or be in precarious temporary jobs, on the date of the survey (thus appearing as non-participants or employed in replies to the questionnaire), without having signed off the register, where they appear as registered unemployed.

Table 4.5

Participation rates by age and sex, [1] total for EC 9

	Total					Male					Female				
	1973	1975	1977	1979	1981 [2]	1973	1975	1977	1979	1981 [2]	1973	1975	1977	1979	1981 [2]
14-24	46,0	44,9	44,0	43,4	47,6	51,4	49,2	47,7	47,1	51,8	40,7	40,7	40,3	39,8	43,4
25-29	69,8	71,8	73,4	74,1	75,0	93,4	93,0	92,3	91,7	92,2	45,5	50,9	54,8	57,0	57,7
30-39	69,7	71,7	72,6	73,8	74,7	97,6	97,3	96,9	96,6	96,5	40,9	45,4	47,8	50,6	52,5
40-49	69,6	71,2	71,8	72,3	72,9	96,3	96,2	95,7	95,6	95,4	43,6	46,3	47,7	48,8	50,1
50-54	65,8	66,9	66,9	67,1	67,4	92,3	92,5	91,8	91,4	90,5	43,2	43,9	43,9	43,9	44,7
55-59	53,7	59,0	59,6	57,4	55,3	84,5	85,4	84,2	81,4	78,4	34,1	36,2	38,0	36,7	34,9
60-64	40,3	38,7	35,5	33,6	29,2	64,6	62,1	56,8	53,6	46,9	20,6	19,2	17,8	16,8	14,6
65 +	7,6	7,5	6,6	5,2	4,1	12,9	12,9	11,2	8,2	6,9	4,2	3,9	3,6	2,8	2,2

[1] Persons having a main occupation and unemployed persons (labour force) as a percentage of total population of the relevant age and sex.
[2] Excluding Luxembourg.

Source: Eurostat: Community labour force sample surveys 1973, 1975, 1977, 1979, 1981.

Table 4.6

Unemployment rates by age and sex,[1] total for EC 9

	Total					Male					Female				
	1973	1975	1977	1979	1981 [2]	1973	1975	1977	1979	1981 [2]	1973	1975	1977	1979	1981 [2]
14-24	4,7	8,1	10,0	10,1	14,0	4,7	8,0	9,0	8,5	12,8	4,7	8,2	11,3	12,0	15,5
25-29	2,3	4,2	5,0	5,2	7,1	2,0	3,7	4,3	4,4	6,4	2,9	5,1	6,1	6,6	8,3
30-39	1,2	2,8	2,8	2,9	4,0	1,0	2,3	2,3	2,3	3,5	1,4	3,7	3,7	4,1	4,9
40-49	1,2	2,3	2,4	2,3	3,1	1,1	2,0	2,1	2,0	2,9	1,2	2,8	2,8	2,9	3,5
50-59	1,7	2,3	2,6	2,5	3,9	1,1	2,0	2,4	2,3	3,7	1,4	2,7	3,0	3,0	4,4
60-64	1,9	3,1	3,5	2,8	4,8	2,0	3,5	3,9	3,0	5,8	1,3	2,0	2,6	2,2	2,3
65+	0,9	2,2	1,4	0,6	0,7	1,1	2,7	1,5	0,8	0,6	:	1,1	1,1	:	(0,7)
Total	2,0	3,7	4,2	4,2	6,1	1,8	3,3	3,5	3,4	5,3	2,3	4,4	5,3	5,6	7,4

[1] Unemployed as % of labour force of the relevant age and sex.
[2] Excluding Luxembourg.

Source: Eurostat: Community labour force surveys 1973, 1975, 1977, 1979, 1981 and Commission services.

from 1973 to 1981, the problem has become much worse in absolute terms. Statistical data show that over 4 million young people under 25 were registered as unemployed in the Community in June 1983 (in gross terms); they accounted for 37% of total unemployment.

Young men are as much affected as young women. In 1981, the rate of unemployment for young women under 25 was 15,5%, which means that on average in the Community young women are three times as likely as adult women to find themselves unemployed. But while the situation of women gradually deteriorated in relation to that of men until 1979, it has not done so since. The unemployment rate among young women was about 40% higher than that among men of the same age in 1979; by 1981, it was only 20% higher, and is estimated at only 13% higher in 1983. Nevertheless, it is fairly clear that this is not so much an improvement as a reflection of increased male unemployment, since the effects of the recession have been more keenly felt in the manufacturing sector, where relatively more men are employed, than in the services sector.

Although the unemployment situation of young people is quite serious in the Community as a whole, there are differences from one Member State to another. The 1983 updating of survey data shows that one out of three young people is unemployed in four Member States: the Netherlands (35%), Italy (34%), Denmark (34%) and Belgium (33%). Three other countries have youth unemployment rates around the Community average of one out of four young people: the United Kingdom (28%), France (27%) and Ireland (26%). The rate is much lower in Germany (15%). It is striking to note that in 1973, unemployment affected one young person out of 20; by 1979 it was one out of 10, and by 1983 one out of four. The gap between the young male unemployment rate (25% in 1983) and the young female unemployment rate (28,3%) has not increased substantially in recent years in the Community as a whole, but considerable differences occur between the Member States, with the young female rate ranging from 13% in the Federal Republic of Germany to over 40% in Italy. However, it should be borne in mind that differences in female unemployment from one country to another are often due more to differences in eligibility for benefits, particularly for married women, than to real differences in the supply of (or demand for) female labour.

The general picture, nevertheless, is one of a substantial deterioration in youth unemployment over the past decade. Obviously the low rate of economic growth is partially responsible for the deterioration, but other factors are also important. Among them are the following.

(i) The generation born during the baby boom of the 1960s has reached working age just when the demand for labour is in a cyclical trough; this has led to permanent adjustment problems in the younger section of the labour market.

(ii) The participation rate of young people increased considerably in 1981 after declining steadily from 1973 to 1978. Although a correct interpretation of this trend is difficult, it may be that young people at first reacted to the adverse employment situation by continuing with full-time education and delaying—but only temporarily—their entry to the labour market.

Table 4.7

Unemployment rates among adults and young people under 25

%

Unemployment rates among adults

	Total					Male					Female				
	1973	1975	1977	1979	1981	1973	1975	1977	1979	1981	1973	1975	1977	1979	1981
B	1,3	2,2	4,5	5,8	9,1	1,0	1,5	2,4	3,2	6,0	2,1	3,9	9,1	11,3	15,2
DK	:	5,5	5,7	5,0	8,6	:	5,9	5,0	3,6	8,9	:	5,2	6,8	7,0	8,2
D	0,4	2,4	2,4	2,2	2,5	0,3	2,3	2,0	1,6	2,0	0,7	2,6	3,1	3,3	3,4
F	1,3	2,3	2,9	3,8	4,6	1,1	1,9	2,4	3,2	3,6	1,7	3,0	3,9	4,9	6,1
IRL	:	7,5	7,3	5,8	9,3	:	8,2	8,1	5,5	10,2	:	5,6	5,4	7,1	6,1
I	1,9	1,6	1,9	2,5	2,3	1,6	1,4	1,5	1,9	1,6	2,8	2,2	3,0	4,1	3,8
L	:	:	:	0,8	:	:	:	:	0,8	:	:	:	:	:	:
NL	1,6	2,6	2,7	2,6	3,9	1,6	2,7	2,8	2,6	4,0	1,1	2,3	2,4	2,5	3,7
UK	1,9	3,9	3,8	2,8	6,1	2,1	3,5	4,1	3,2	7,3	1,5	4,6	3,3	2,2	4,3
EC 9	1,3	2,7	3,0	3,0	4,3	1,3	2,5	2,6	2,5	3,9	1,5	3,3	3,6	3,9	4,9

Unemployment rates among young people

	Total						Male						Female					
	1973	1975	1977	1979	1981	1983 [1]	1973	1975	1977	1979	1981	1983 [1]	1973	1975	1977	1979	1981	1983 [1]
B	3,1	7,8	11,3	12,8	20,8	32,6	2,3	6,0	6,9	7,8	15,7	30,0	4,0	9,8	16,4	18,5	26,5	36,0
DK	:	13,9	13,4	11,2	17,9	33,9	:	14,4	9,3	7,5	15,0	29,2	:	12,7	18,1	15,6	21,1	38,8
D	0,9	5,3	5,3	3,8	4,7	14,9	0,8	5,6	4,8	3,1	4,1	16,6	1,0	4,9	5,9	4,6	5,4	13,1
F	4,1	7,8	11,5	14,2	17,5	26,5	3,4	6,8	8,6	10,4	12,6	19,9	4,9	9,0	14,6	18,2	22,7	33,2
IRL	:	15,1	14,4	11,4	14,5	25,5	:	16,3	16,5	11,7	16,7	28,7	:	12,8	11,7	11,0	11,5	21,4
I	14,9	13,0	18,0	21,0	21,5	34,2	14,6	12,3	16,1	18,0	18,0	28,0	15,4	13,9	20,3	24,8	26,0	41,7
L	:	:	:	4,2	:	:	:	:	:	3,9	:	:	:	:	:	4,6	:	:
NL	2,9	5,7	5,6	6,4	10,7	35,0	3,4	7,4	6,3	5,8	12,0	36,1	2,4	3,8	4,8	7,0	9,2	33,8
UK	3,2	7,7	8,6	6,8	15,4	27,6	3,6	7,6	8,8	7,0	17,1	29,0	2,6	7,8	8,4	6,6	13,1	25,8
EC 9	4,7	8,1	10,0	10,1	14,0	26,4	4,7	8,0	9,0	8,5	12,8	25,0	4,7	8,2	11,3	12,0	15,5	28,3

[1] Estimate.

Sources: Eurostat: Community labour force sample surveys 1973, 1975, 1977, 1979, 1981 and Commission services.

(iii) Wage and non-wage labour costs for young workers have moved closer to those for adult workers as a result of rules governing minimum wages and apprentices' wages; employers are therefore sometimes unwilling to recruit and train young people.

(iv) The attitude of young people to work may have changed in several ways: according to studies, [1] young people, particularly those from privileged socio-economic backgrounds, set more and more store by interesting, non-repetitive and non-monotonous jobs, which does not make it any easier for them to find work. It would also appear that less well-qualified young people, in particular, have got into an 'unemployment rut', and passively accept a situation seen as widespread and inevitable.

From 1973 to 1979, the general expansion of unemployment and the aggravation of youth unemployment were accompanied by an increase in long-term unemployment (see Table 4.8.). After declining from 1973 to 1975, the proportion of job seekers who had been out of work for a year or more increased to a peak of 37,4% in 1979. The survey for 1981 shows some improvement to 33,4%, no doubt due to vocational training programmes to combat structural unemployment, and to the withdrawal from the labour market of discouraged workers.

Long-term unemployment affects both adults and young people. Among the adult unemployed, the percentage of

[1] OECD: *Youth unemployment: The causes and consequences.* Paris, 1980.

Table 4.8

Unemployed by duration, total EC 9

Total unemployed

	Total					Male					Female				
	1973	1975	1977	1979	1981 [2]	1973	1975	1977	1979	1981 [2]	1973	1975	1977	1979	1981 [2]
Months:															
1 [1]	13,6	16,1	11,6	10,5	9,2	13,0	14,4	11,5	10,5	9,1	14,4	18,3	11,9	10,4	9,5
1-2	16,1	20,4	15,5	13,5	13,6	14,8	20,9	15,8	14,2	14,2	18,2	19,8	15,1	12,8	12,8
3-5	18,6	21,6	17,9	16,0	18,3	18,6	22,7	18,3	16,8	19,1	18,6	20,1	17,4	15,2	17,4
6-11	22,0	23,5	22,4	22,6	25,5	21,2	22,6	20,6	21,5	25,6	23,3	24,6	24,5	23,8	25,3
12+	29,7	18,4	32,6	37,4	33,4	32,4	19,3	33,8	36,9	32,0	25,5	17,2	31,1	37,9	35,0
	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Unemployed aged 14 to 24

	Total					Male					Female				
	1973	1975	1977	1979	1981	1973	1975	1977	1979	1981	1973	1975	1977	1979	1981
Months:															
1 [1]	13,0	16,7	12,2	11,9	9,8	13,5	16,8	13,1	13,2	10,5	12,3	16,7	11,4	10,9	9,2
1-2	16,0	20,9	16,0	13,5	13,6	16,2	22,0	16,8	15,1	14,3	15,8	19,6	15,4	12,2	12,8
3-5	17,8	20,0	17,5	15,7	17,2	18,7	21,1	18,1	16,9	17,9	16,6	18,7	17,0	14,8	16,6
6-11	27,2	26,3	26,1	26,8	28,3	25,9	23,8	23,5	24,8	28,3	28,9	29,2	28,5	28,3	28,3
12+	26,0	16,1	28,2	32,1	31,1	25,7	16,3	28,5	30,0	29,0	26,4	15,8	27,7	33,8	33,1
	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

[1] Including those who have not yet started to look for a job.
[2] Excluding Belgium, Luxembourg and Ireland.

Source: Eurostat: Community labour force sample surveys 1973, 1975, 1977, 1979, 1981, and Commission services.

those unemployed for more than a year was 35,2% in 1981 compared with 41,2 % in 1979. The relative improvement in the aggregate figures is almost entirely a reflection of this decline. The percentage of long-term unemployed among young job seekers did not change much from 1979 (32,1%) to 1981 (31,1%). It should also be noted that while long-term unemployment accounted for 3,2% of the young labour force in 1979, the percentage had risen to 4,4% in 1981. This seems to confirm the view that while the majority of young school-leavers change jobs frequently at first before settling down to a stable career, there is a class of young unemployed workers who are caught in a vicious circle and suffer from a set of social and cultural handicaps that are difficult to overcome. In assessing the real dimensions of the problem of youth unemployment, this structural hard core must be taken into account; it involves young women as well as young men, since over 33% of young female job seekers had been unemployed for more than a year in 1981.

4.4 Employment policy problems and alternatives

The complexity and breadth of the unemployment phenomenon is a challenge to Member States' policies on several fronts. Obviously there is no single employment policy answer, and no single solution to the problem: a package is required on both the supply side and the demand side.

A strong recovery would no doubt eliminate a large proportion of present cyclical unemployment, to the extent that employment is correlated to activity. But the effects of an expansion of demand are closely limited by structural factors. In view of the size of the non-cyclical components of unemployment, further measures are required in several areas. The role of real wage increases in unemployment trends is a controversial point (see box), but there are

grounds for expecting favourable, if modest, results from restraining the growth of real wages in relation to productivity. The *Annual Economic Review* for 1982-83 shows that employment and productivity trends in the Community are diametrically opposed to those in the USA, which implies that the rigidity of real wages in Europe could be one of the factors in the Community's poor performance on the employment front since 1970. It would be wrong to conclude that a fall in real wages would decisively solve the problem, however, because the fall would have to be considerable and adjustment would take time. Moreover, a number of experts agree that a real wage adjustment could not exercise the desired effects on unemployment against a background of insufficient demand. But beyond the immediate boost to labour demand directly attributable to wage restraint, favourable effects could be expected in the longer term as investment became more profitable and more dynamic.

On the supply side, several Member States have already introduced compulsory education programmes and vocational training measures (see box on employment policy). These measures have a twofold purpose: first, to cancel out the effects of unfavourable population trends, and secondly, to give young people the opportunity of improving their qualifications and to make it easier for them to find jobs. Almost everyone agrees that such measures are useful, especially so as the present pace of technological progress will aggravate structural mismatch on the labour market if appropriate training is not available.

The problem of qualifications is not confined to young people, for many job-seekers are without the background employers require. Although mismatch is not by any means eliminated by boom conditions, it is much more troublesome in a stagnant labour market. One of its consequences then is to increase individual periods of unemployment, since the lack of qualifications that makes it difficult to find a job in the first place is an even more important factor as time passes for the job-seeker. Training programmes specially designed for the long-term unemployed are another useful approach. But it is difficult to measure the favourable effects of all these initiatives—although favourable effects do seem to have resulted—particularly in the experimental stages.

The effects of early retirement schemes, on the other hand, are clearly apparent in the reduction in participation rates among the over-54s. These measures, which are increasingly costly to implement, are intended to provide an alternative to laying-off older workers, who are not only those hardest hit by long-term unemployment, but also those least likely to benefit from training schemes; the measures are also intended to create new jobs. The schemes are apparently widely used at present in labour-shedding operations, but the job-creating effects are not clearly demonstrable.

Another approach adopted by governments is to encourage the reduction and reorganization of working time, and part-time working. Measures along these lines have been introduced by most of the Member States. It is not easy to assess the results to date, and even less so to estimate how an even greater reduction in working hours would affect the situation. As to part-time working, which has become much more common over the past few years, it is not known how far the trend is a response to workers' wishes and how far it is the result of the slackness on the labour market. It is also difficult to determine to what extent part-time jobs are new jobs, and to what extent they correspond to previous full-time jobs that have been transformed without leading to new recruitment.

The trend towards shorter working hours is apparent in the annual average reduction of about 1% in working hours over a long period, in response to the demand for a better standard and quality of living. The issue of accelerating this trend so as to increase employment has assumed major importance in recent years. In some Member States there have been, or are to be, negotiations between the two sides of industry on this point. In September 1983 the Commission adopted a draft recommendation inviting the Member States to consider the reduction and reorganization of working time among employment policy instruments, and setting out general guidelines to be followed by national governments, These guidelines concern, in particular, simultaneous reduction and adjustment, so as to avoid an increase in unit production costs and ensure better use of capital, and restrictions on overtime, with the generalization of arrangements for time off in lieu (while at the same time taking account of the flexibility required in certain industries). It is recommended in addition that the public sector should set an example by adopting the recommended arrangements.

Governments do not therefore have a wide choice of action, and the approaches open to them cannot always be justified on the grounds of verifiable and clear results.

While an economic recovery policy should help to reduce the share of unemployment at present attributable to the slackness of demand, its implementation runs up against several obstacles.Firstly as there is no general consensus on the extent of this component of unemployment, there is no way of determining the extent of expansion required to eliminate it or the results that such expansion might achieve. Secondly, policies of austerity can only be relaxed where progress made towards mastery of inflation and budget aggregates permits, which is not the case in countries where inflationary expectations and inflation rates are still not controlled.

In addition, structural adjustment policies seem to be required everywhere: as the structural component of unemployment will not respond to economic recovery,

government action is required to improve the quality and mobility of labour and to eliminate rigidities and constraints that prevent firms from stepping up recruitment.

Finally, government policies to adjust the structure of the labour market will operate within the context of the rapid changes in social and demographic structures, and in particular the major change that will take place in demographic patterns over coming decades. This implies that some employment policy instruments will need to be handled with care. For example, the rate of growth of the population of working age will start to decline after 1986, and will become negative by the end of the 1980s. This is a major consideration which should influence such decisions as to how far to adjust working hours or retirement age over the next few years.

Employment policies

Belgium

The Belgian Government has not changed its employment policy stance since the middle of 1982. Apart from wage restraint (see box of Chapter 3), policy has concentrated on three points: early retirement, job creation and measures to combat youth unemployment. Since 1 January 1983, early pensions for workers aged 60 and over are granted only on production of proof that the retiring worker has been replaced. A Royal Decree of December 1982 encourages the recruitment of the first employee by temporarily reducing employers' social security contributions. Another measure, also taken in December 1982, enables small and medium-sized firms which recruit unemployed workers in receipt of benefit for certain types of development project to avail of government grants. On the initiative of the Minister for Employment and Labour, negotiations have been launched at branch or company level to discuss the proposal for a 5% reduction in working hours accompanied by a compulsory 3% increase in recruitment. In March 1983, the government approved a bill raising the age for compulsory education to 18 (with full-time education compulsory until the age of 16). Changes in regulations for unemployment benefit have been introduced to promote personal initiative and self-employed activity.

Denmark

Denmark's employment policy was reviewed when the new government took office in September 1982. The previous government had concentrated on a package of measures from the economic policy programme for 1982-85, intended to create 50 000 new jobs a year and to provide all young people with either a job or a training opportunity after 1984. The new government's aim is to follow its predecessor's commitments on training and employment (particularly employment for young people), while changing the form and the spirit of its implementation. In particular, the new government has announced its intention of relaxing conditions of access to all types of education, gradually removing age limits for admission, and eliminating distortions between various financial aid schemes, so that the students' choice will not be affected by the authorities' administrative rules. A law on the creation of new jobs has been passed enabling private firms, local authorities and central government bodies to apply for government aid to recruit job seekers aged 18 to 25 who have been unemployed for a certain period to undertake work of community benefit, on condition that the new work cannot be done in any other way and does not lead to any major distortion of competition.

Federal Republic of Germany

During 1982, measures were taken to stimulate employment directly (youth training programmes) or indirectly (investment subsidies); the impact of these measures is expected to continue in 1983 and 1984. In early 1983, the Government stepped up its job-creation activity (*Arbeitbeschaffungsmaßnahmen*) and changed certain social security arrangments. Job-creation measures, which are intended to assist about 56 000 people, include grants normally for one year, with the possibility in certain circumstances of an extension to three years. The cost of these arrangements is not expected to exceed the saving on unemployment benefits. On the vocational training side, two programmes have been introduced: one, involving expenditure of about DM 3 000 million, is organized by the Federal Labour Office and will provide retraining for 125 000 unemployed workers; the other, costing DM 124 million, will provide training and work experience for 11 000 young people.

Greece

The government has made funds available to the National Employment Office to safeguard existing jobs and create new ones. A special job-creation proramme was set up in this framework for the benefit of young people under 25, for whom 15 000 new jobs are planned, and aged 25 to 29, for whom 5 000 new jobs are planned. In the area of vocational training, it is planned to reorganize apprenticeships, introducing new syllabuses and new teaching systems, as well as a special syllabus for 15 to 18-year-olds. Working hours were reduced to 40 hours a week from 1 January 1983.

France

In line with the approach adopted in late 1981 and followed throughout 1982, government action has concentrated on the issues of long-term unemployment, vocational training and youth unemployment, the reduction of working hours and unemployment insurance schemes, Specific measures are planned for long-term unemployment. For training and youth, the government has decided to change the *Avenir Jeunes* plan, which was brought to a close in mid-1982 and to abandon automatic aid, giving priority to bilateral negotiations with individual firms. The 'job-training contract' arrangements, under which employers receive financial aid if they undertake either to train a worker or to guarantee a job for a certain period, have been retained. In January 1983, the government finalized the main features of a plan to help with the occupational and social integration of young people aged 16 to 25; this plan concentrates on prolonging the effects of school and university education, measures to help young people find jobs (including 'job-training contracts' and traineeships in large firms) and improving career counselling for young people. New arrangements for solidarity contracts were adopted, guaranteeing aid for three years from 1 January 1983 to firms that considerably reduce working hours, while maintaining production capacity, and undertake to maintain or increase staffing levels. It is also planned to increase the period of post-natal leave without pay, and to encourage fixed-term contracts by making the rules more flexible.

Ireland

The government that took office in December 1982 retained some of the measures already in operation and, in particular, the Youth Employment Agency, whose task is to increase the number of young participants in training and work-experience programmes. It is estimated that these programmes involved 33 700 young people in 1982, and 45 000 in 1983. New measures have been announced, including setting-up a special task force of ministers, a National Planning Board and a National Development Corporation. The first two bodies will work out measures to protect and create jobs, while the Development Corporation will invest directly in commercially profitable projects designed to substitute domestic goods for imports and to promote exports.

Italy

In April 1982, an investment and employment fund was set up with resources of LIT 5 350 000 million. These resources are to be shared between projects to help with the recovery of investment and with job creation, comprising: an automatically renewable fund for the purchase of shares issued by special credit establishments to finance industrial capital investment, housing construction and business modernization; investment in energy by the ENEL (national electricity company); modernization and construction of infrastructure in rural areas; grants to small and medium-sized firms, production cooperatives and wage-earners' cooperatives; a reduction in VAT; deductibility of interest payments on loans to finance the development of services in agriculture; an increase in the resources of the technological innovation fund set up in February 1982; an increase in the resources of the Mezzogiorno credit institution. Furthermore, an agreement was reached in January 1983 between the two sides of industry and the government on: changes in the automatic indexation system (*scala mobile*); the renewal of collective agreements; a reduction in working time by 40 hours by mid-1985; compensatory tax and social measures to protect workers' purchasing power; measures to improve the efficient use of productive capacity by combating absenteeism and improving mobility.

Luxembourg

Special measures have been planned to protect employment and economic competitiveness in general: a new system of aids for geographical mobility, specific aid for the recruitment of long-term unemployed workers, the extension to other categories of workers of the reemployment grant for steelworkers, a tighter ban on overtime, stricter supervision of the laws on a 40 hour week in the case of workers with more than one part-time job, opportunities for the authorities to employ unemployed workers in receipt of benefits on jobs in community services. At the end of 1982, two agreements were reached at the national tripartite conference: one concerns wage restraint, higher minimum wages and the continuation of the solidarity levy; the other concerns a reduction in hours and a corresponding reduction in pay in the steel sector.

The Netherlands

A package of vocational training measures in favour of unemployed young people was adopted in 1982; it involved setting-up courses and introducing grants for employers that allow under 23-year-olds to follow apprenticeship courses for the long-term unemployed. On taking office in November 1982, the new government developed a three-fold approach to unemployment: the reorganization of public finance, the reinforcement of private enterprise and the promotion of employment. The measures planned include an adjustment of working hours and a single plan for the employment of young people, involving financial aid to further training projects and short vocational training courses. To improve young peoples' job opportunities, education and employment contact centres have been set-up with the purpose of matching the qualifications of newly-trained young people to the need of firms. The two sides of industry reached a nation-wide agreement in principle on a socio-economic policy that provides for the option, at the level of a sector or an individual firm, of a reduction in working hours in lieu of wage indexation.

United Kingdom

The government's employment measures have continued along the same lines as those adopted in 1981 and 1982, concentrating mainly on measures to reduce unemployment among young people. The Youth Opportunities Programme has been replaced by the Youth Training Scheme, which guarantees from September 1983 12 months' training and work to all 16-year-old school-leavers and some 17-year-old job-seekers. The estimated cost for 1983/84 totals UKL 950 000 million, and 460 000 young people should be involved. Two other schemes are also in operation: the Community Programme Scheme, introduced in October 1982 to provide jobs (some part-time) of community benefit for 130 000 long-term unemployed persons aged over 18, and the Job Splitting Scheme, introduced in January 1983 to encourage employers to split existing full-time jobs into two part-time jobs. This scheme is open for applications until March 1984, and 60 000 subsidies are planned. It is estimated that these and other existing measures had covered 657 000 people by May 1983.

Real wages and employment

Over the past few years there has been much discussion of the role of real wage levels in determining the level of employment. A number of empirical studies have been carried out, to test equations where the explanatory variable is either real wages (wages deflated by a cost-of-living index), or the real wage gap (the gap between actual real wages and a reference wage that would, for example, leave factor income distribution unchanged [1]).or the share of real wages in national or sectoral income. The real wage gap and the share of wages are theoretically equivalent, but may differ in practice because of the data used. It should be noted in addition that studies on this subject have applied inappropriate deflators to nominal wages (the deflator of GDP at factor cost being the only valid deflator) and that the results have sometimes been substantially different. Some studies have taken account only of the direct effects on employment of a change in real wages, while others have included indirect effects through changes in profits and investment.

The basic specifications and results of some representative studies, are considered to give an idea of the range of discussions.

Geary and Kennan (1982) inspect quarterly data for employment and real wages in manufacturing industry in 12 OECD countries. They test several lag assumptions, but in no case do they find a statistically significant correlation between the two variables. The validity of their findings is compromised, however, because they use the wholesale price index to deflate nominal wages. A similar criticism applies to the studies by Neftci (1978) and Sargent (1978), both of whom use the consumer price index and reach the contradictory conclusion that real wages and employment are positively correlated in the USA.

Grubb, Layard and Symons (1982) also use nominal wages deflated by the index of wholesale prices; they find a negative correlation between real wages and employment. According to the authors, the result is due to the introduction of import prices as one of the explanatory variables. This explains why Geary and Kennan, who do not include import prices, reach different conclusions. The authors also consider the influence of aggregate demand on the determination of employment, but only in France do they find a positive correlation. Both studies obviously suffer from the same criticisms concerning the choice of deflator.

Jeffrey Sachs (1983) studies the relationship between unemployment rates in the economy as a whole and either real wages (deflated by value-added prices) on the real wage gap (defined as the gap betwen the observed value of the ratio of real wages to full employment productivity on the one hand, and the average value of this ratio for 1965-69 on the other).Testing the equations for six countries from 1961 to 1981, Sachs finds significant correlations in Canada, Germany, Japan and the United Kingdom. There is no positive correlation in France or the United States. The equations also incorporate the real money supply, so as to monitor the effects of monetary policy changes on the employment situation. Although there is a negative correlation in all cases between unemployment and money supply, the findings for real wages are not significantly modified.

A recent report by Dornbusch, Basevi, Blanchard, Buiter and Layard (1983) questions whether the problem of real wages can be defined and measured by using the real wage gap—and thus whether it is possible to distinguish between 'classical' and 'Keynesian' unemployment. The report argues that the measured effects of an increase in real wages relative to productivity gains on the share of wages in GDP depend on the basic assumption adopted concerning the production function. If a Cobb-Douglas function is used, the distribution of income between wages and profits remains constant, so that a decline in employment due to an increase in labour costs is entirely offset by productivity gains. As firms cannot adjust their labour force and capital stock without some delay, there may be a short-term wage gap. However, in the longer run, technology is adjusted towards greater capital intensity, labour productivity increases and the wage gap tends to narrow. If no gap is found, this does not mean that the real wages problem does not exist any more. The report attempts to assess the problem from a different angle, by estimating the size of the increase in real wages compatible with maintaining full employment. The results for manufacturing industry in three European countries confirm that from 1975 to 1980, the expansion of unemployment was partly due to an excessive increase in real wages; the evidence for 1981-82 apparently implies that slack demand played a much greater role in the expansion of unemployment during those years.

The conclusions of these studies are sometimes divergent, as are the economic policy measures they imply. From several points of view, such as the choice of variables, the form of the equations tested and the quality of the findings, the most satisfactory studies are those which take a midpoint position: the trend of real wages is not entirely responsible for mounting unemployment, but there is little doubt that real wage growth (accompanied by declining profits) was excessively rapid during the 1970s, and that it was at least partly responsible for the slackness of productive investment and the stagnation of employment. There are grounds for concluding that a certain proportion of present unemployment cannot be eliminated unless real *per capita* wages decline, although some studies add that this would not have the desired effects as long as aggregate demand remained insufficiently strong.

[1] This is the variable used in Chapter 3, where it is called the 'real product wage'.

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5. Budgetary policy

In 1983, the net borrowing of general government in the Community as a whole was roughly stable. Given the shortfall of receipts caused by the persistence of the recession, and the increase in the cost of debt service, this result was obtained only through a marked effort to control the growth of public expenditure. In certain Member States this effort was accompanied by an increase in the burden of indirect taxes and social secuity contributions. The search for economies bore as much on government consumption and social transfers as on gross capital formation. In many cases, productive expenditures have not escaped the economy effort. The share of taxes and parafiscal payments in GDP again increased. The magnitude of budget deficits is reflected in an increase in the ratio of public debt to GDP on average for the Community. This movement, together with the high levels of interest rates over the past few years, has led to a sharp rise in payments of interest on public debt, which now constitute an important financial constraint on budgetary policy in a number of Member States.

5.1 Budgetary trends and policies

The budget deficit in the Community as a whole is likely, on the basis of latest Commission estimates, to be little changed as a proportion of GDP in 1983: 5,4% as against 5,2% in both 1982 and 1981. This outturn should be viewed in the context of a slowdown in the growth of nominal GDP: 6,9% this year as against 9,5% in 1982, while real activity grew at the very modest rate of 0,5% (0,4% in 1982).

Three main elements have dominated the development of general government accounts in 1983: the persistence of the recession, which reduced the growth of receipts and swelled transfers to households; the effort made by the Member States to squeeze the growth of public expenditure; and the big increase, caused by the regular accumulation of deficits, in interest payments on public debt. In 1983, the current receipts of general government in the Community grew by 9% as against 12,2% in 1982. Of these receipts, only indirect taxes grew at a rate close to that of the previous year (9,1% in 1983, 10,7% in 1982), as a result of an increase in the weight of such taxes in a number of Member States (see Table 5.1). Rates of social security contributions were often similarly increased, but direct tax rates were little changed, direct tax receipts growing faster than nominal GDP only as a result of fiscal drag. In sum, overall tax pressure (including social security contributions) has continued to increase for the Community as a whole, reaching 42,8% of GDP in 1983 as against 41,9% in 1982.

Efforts to control the increase in public expenditure have been even more determined and more general than in 1982: on average for the Community, current expenditure has risen by 8,7% in 1983, compared with 12,3% in 1982, continuing the slowdown already evident in the earlier year. This slowdown was particularly marked in the case of social transfers and government consumption (growth of, respectively, 8,2% and 7,1% in 1983 and 13,1% and 9,6% in 1982). The reduction in the inflation rate has certainly contributed to this outturn, but, given the development of unemployment, a strict control of administrative and personnel expenditure and of transfers to households (up 8,4% in 1983, 13,6% in 1982) has been required for it to be achieved. Net capital transfers have increased substantially, but expenditure on gross capital formation has grown only very slightly faster than last year (6,9% in 1983, 5,6% in 1982).

Debt interest payments have continued to grow much faster than other categories of expenditure, even if the very gentle decline in interest rates in Europe has moderated the increase, one of 18,1% in 1983 against one of 20,4% in 1982. The sharp rise in debt interest payments as a percentage of GDP on average for the Community (from 4,2% in 1982 to 5,1% in 1983), and the high level of such payments in certain Member States, reflects the fact that public debt has been growing significantly, even as a percentage of GDP, for a number of years.

In its communication of 1 July 1982, 'Budgetary discipline and economic convergence' (COM(82)422 final), the

Table 5.1

Income and outlay transactions of general government,[1] EC 10

	'000 million ECU	% change					% of GDP					
	1983 [2]	1980	1981	1982	1983 [2]	1984 [3]	1979	1980	1981	1982	1983 [2]	1984 [3]
Indirect taxes	370,7	16,5	11,7	10,7	9,1	6,6	12,7	13,4	13,5	13,7	14,0	14,0
Direct taxes	352,8	17,5	11,8	13,3	9,2	9,2	11,4	12,7	12,6	13,0	13,6	13,6
Social security contributions	412,5	14,6	12,8	12,4	9,4	8,0	13,5	14,9	14,8	15,2	15,5	15,8
Total taxes and social security contributions	1 136,0	16,1	12,1	12,1	9,2	7,9	37,5	40,3	40,9	41,9	42,8	43,4
Other current receipts [4]	100,1	17,1	19,2	12,8	6,0	8,5	3,1	3,5	3,7	3,8	3,8	3,8
Total current receipts	1 236,1	16,2	12,7	12,2	9,0	8,0	40,6	43,8	44,6	45,7	46,6	47,2
Current transfers	620,1	13,0	18,1	13,1	8,2	6,8	19,8	20,8	22,4	23,1	23,4	23,4
Actual interest payments	136,3	27,5 [4]	26,6	20,4	18,1	11,5	3,0 [4]	3,5 [4]	4,2	4,6	5,1	5,4
Government consumption	515,0	18,0	13,6	9,6	7,1	4,9	17,2	18,7	19,4	19,4	19,4	19,1
Total current expenditure	1 271,4	16,2	16,8	12,3	8,7	6,5	40,0	43,0	45,9	47,1	47,9	47,9
Gross saving	−35,3						0,7	0,8	−1,3	−1,4	−1,3	−0,7
Net capital transfers	26,4	13,0	−1,4	12,6	32,9	2,8	1,0	1,0	0,8	0,8	1,0	1,0
Gross capital formation	80,8	13,1	3,8	5,6	6,9	5,7	3,0	3,3	3,1	3,0	3,0	3,0
Net lending (+) or borrowing (−)	−142,5	—	—	—	—	—	−3,4	−3,5	−5,2	−5,2	−5,4	−4,7
For information: Nominal GDP	—	12,2	8,7	9,5	6,9	6,6	:	:	:	:	:	:

1 National accounts definition, excluding loans, advances and participations.
2 Estimates.
3 Forecasts.
4 Actual interest received and miscellaneous.

Commission underlined the importance of better control of the budgetary aggregates in achieving a greater convergence of economic developments in the Community. The Commission stressed, notably, the need for a reduction in, or, at the very least, a stabilization of, net borrowing, a deceleration in the growth of public expenditure; for a restructuring of taxes and social security contributions; and for a more frequent use of charges for public sector services. From this point of view, the general government budgetary outturn in 1983 is encouraging. In the majority of Member States, the growth of spending in nominal terms has been less than was forecast a year ago. Spending has also slowed down in real terms, clearly pointing up the generally restrictive stance of budgetary management. At the same time, however, the growth of receipts has been not only slower than in 1982 but has also fallen short of initial estimates (except in Denmark and Italy), despite, in some cases, higher tax rates.

Budgets for 1983 were in fact based on macroeconomic assumptions about activity in 1983 which were slightly more favourable than the actual outturn. It soon became apparent, in many cases in the first few months of the year, that receipts had been overestimated. In all the Member States, the fact that the economic outturn was weaker than had been assumed was not considered reason for allowing budget deficits to stray off target: the authorities decided to maintain their budgetary objectives and have taken additional measures in order to be able to respect them. Thus the Belgian Government decided in March on budget economies of BFR 39 400 million and an increase in social security contributions. Following the March realignment of EMS parities, the French Government decided on a programme of measures to back up the devaluation of the franc. These measures included economies in central government, social security and public enterprises. In

Table 5.2

Income and outlay transactions of general government,[1] 1982-84

(% change)

	Total current receipts			Indirect taxes			Direct taxes			Social security contributions			Other current receipts		
	1982	1983[2]	1984[3]	1982	1983[2]	1984[3]	1982	1983[2]	1984[3]	1982	1983[2]	1984[3]	1982	1983[2]	1984[3]
B	12,2	5,7	9,4	8,7	4,0	7,1	17,2	3,1	9,1	7,7	11,9	12,7	15,8	2,1	5,5
DK	12,0	12,5	8,0	9,7	7,8	4,7	12,2	13,3	9,6	32,1	42,6	12,6	11,6	10,8	8,0
D	4,9	4,0	5,3	1,8	4,6	6,2	2,7	4,4	5,2	5,9	3,1	6,5	21,7	5,5	−3,7
GR	39,5	27,4	22,1	36,4	32,0	23,0	61,0	30,0	23,0	27,6	19,0	19,7	61,5	26,0	22,5
F	16,2	11,8	9,8	15,4	8,6	7,3	18,2	14,4	9,0	17,4	13,8	12,4	7,9	7,4	6,8
IRL	24,7	16,5	11,4	21,9	13,1	11,0	20,5	19,7	15,2	31,5	17,2	7,4	39,3	18,4	7,0
I	23,7	22,0	17,3	22,8	34,2	8,0	30,1	21,4	23,6	21,1	16,1	11,2	9,8	11,0	67,8
L	11,1	8,6	7,8	15,8	8,6	11,8	9,4	9,2	6,2	6,7	6,6	5,3	17,6	11,4	9,8
NL	5,4	6,1	0,8	2,1	4,4	5,9	2,6	−2,5	−1,6	9,5	14,1	−1,2	5,9	5,0	3,2
UK	12,2	6,6	6,5	11,7	4,6	7,7	12,3	8,5	6,7	13,7	10,6	6,8	11,3	2,1	1,2
EC	12,2	9,0	8,0	10,7	9,1	6,6	13,3	9,2	9,2	12,4	9,4	8,0	12,8	6,0	8,5

	Total expenditure			Current transfers			Actual interest payments			Government consumption			Net capital transfers and gross capital formation		
	1982	1983[2]	1984[3]	1982	1983[2]	1984[3]	1982	1983[2]	1984[3]	1982	1983[2]	1984[3]	1982	1983[2]	1984[3]
B	9,9	6,3	7,0	9,2	7,1	6,4	25,9	13,1	14,5	5,6	3,4	6,1	4,9	−0,9	−3,3
DK	16,2	11,5	6,0	16,3	8,2	7,8	29,3	51,9	13,5	14,8	7,9	3,1	8,6	−5,1	−1,2
D	4,0	3,6	2,9	5,4	3,4	3,0	23,1	17,4	10,4	2,2	2,5	2,3	−3,8	0,9	−0,7
GR	24,4	25,9	21,7	32,9	22,4	20,2	4,1	47,1	26,0	26,8	23,4	20,8	1,5	38,6	27,8
F	18,2	12,6	10,2	19,4	12,8	10,2	13,3	39,5	30,0	16,9	9,9	7,3	17,5	7,0	8,0
IRL	23,8	9,8	8,1	29,2	11,7	7,2	39,4	19,1	14,4	18,6	9,6	6,3	11,0	−5,5	6,8
I	22,8	20,3	12,4	21,4	17,5	12,2	35,5	30,6	14,9	18,5	16,8	11,2	25,9	27,8	12,9
L	10,5	10,0	5,4	11,8	9,8	7,7	17,1	13,6	24,8	7,2	7,1	6,0	11,9	15,6	−5,0
NL	8,4	5,3	1,5	10,8	5,8	1,6	21,8	17,6	16,1	4,0	2,4	−3,2	−1,9	0,2	−0,2
UK	10,1	6,9	6,3	12,4	6,3	9,0	8,7	−1,1	0,1	9,2	8,1	5,4	5,4	18,6	8,6
EC	11,9	9,0	6,4	13,1	8,2	6,8	20,4	18,1	11,5	9,6	7,1	4,9	7,1	12,3	5,0

1 National accounts definition, excluding loans, advances and participations.
2 Estimates.
3 Forecasts.

Source: Commission services.

addition, direct taxation was raised through the creation of an exceptional tax of 1% on incomes and the establishment of a compulsory loan equivalent to 10% of income tax payments. In Ireland, where VAT rates had been raised in the 1983 budget, there was announced in July an IRL 70 million economy package and an increase in excise duties. In Italy, a number of levies, mostly of a one-off nature, were introduced at the beginning of 1983. In Luxembourg, the financial support to the steel industry decided in April was accompanied from July by an increase in VAT rates and excise duties. Various expenditure reductions, amounting to HFL 2 000 million were decided in the Netherlands in April, and certain taxes were increased. The United Kingdom Government took similar steps in July, in announcing a series of measures aimed at reducing the 1983/84 borrowing requirement by UKL 1 100.

Table 5.2 shows percentage changes in the main items of receipts and expenditures of general government in the Member States. While a slowdown in the growth of current receipts has been evident in eight of the ten countries, there was a slight acceleration in Denmark and the Netherlands. In the Federal Republic of Germany, Italy and the Netherlands, the increase in indirect tax receipts accelerated, as did the increase in direct tax receipts, in Denmark and the Federal Republic of Germany. The increase in social security

contributions accelerated in Belgium, Denmark and the Netherlands. Elsewhere, taxes and social security contributions decelerated. Table 5.3 expresses the same general government operations as percentages of GDP, taking 1979 as a reference year. In four years the overall rate of taxation (that, is including social security contributions) for the Community as a whole has risen by 5,6 points of GDP. The increase has been particularly sharp (more than 8 points) in Ireland and Italy, where, however, the overall rate of taxation was in 1979 significantly lower than the Community average. The increase has been equal to or more than 5 points in Greece and Luxembourg, and around 4 points in France and the United Kingdom. It has been more modest in the other Member States, and particularly in Denmark and Belgium, in which countries the overall rate of taxation was already particularly high in 1979. However, Luxembourg and the Netherlands had even higher rates in 1979 and have nonetheless registered a significant further increase since then. The general upward movement in the Community has been coupled with a reduction in the dispersion of overall rates of taxation among the Member States. It can also be seen that the weight of social security contributions has increased most between 1979 and 1983 (by 2 points of GDP), followed by that of indirect taxes (up by 1,9 points).

As for public expenditure, Table 5.2 shows for 1983 a slowing of the increase in all the Member States except Greece. The share of public expenditure in GDP (see

Table 5.3

Income and outlay transactions of general government,[1] 1979-84

(% of GDP)

	Total current receipts			Indirect taxes			Direct taxes			Social security contributions			Other current receipts		
	1979	1983[2]	1984[3]	1979	1983[2]	1984[3]	1979	1983[2]	1984[3]	1979	1983[2]	1984[3]	1979	1983[2]	1984[3]
B	45,7	46,7	47,8	12,0	11,8	11,8	19,0	18,9	19,3	12,6	13,4	14,1	2,0	2,6	2,6
DK	51,4	52,4	53,2	19,1	17,2	16,9	24,3	25,8	26,5	1,6	3,1	3,3	6,4	6,4	6,5
D	43,5	46,1	46,2	12,9	12,7	12,9	12,6	12,2	12,2	15,4	17,6	17,9	2,6	3,6	3,3
GR	30,6	35,7	36,4	15,2	16,3	16,8	4,8	6,5	6,7	8,4	9,5	9,5	2,2	3,3	3,4
F	44,5	48,9	49,9	14,4	14,5	14,5	7,9	9,5	9,6	19,4	21,5	22,4	2,5	3,4	3,4
IRL	37,6	45,7	46,3	15,8	18,2	18,4	11,9	15,2	15,9	4,7	6,2	6,0	5,1	6,2	6,0
I	36,0	44,7	46,8	9,5	12,0	11,6	9,7	15,0	16,6	14,4	15,5	15,4	2,5	2,1	3,2
L	52,5	58,4	59,3	13,1	14,8	15,5	18,8	19,9	19,9	15,3	16,3	16,1	5,4	7,5	7,7
NL	53,1	56,8	56,0	11,9	11,7	12,1	16,3	14,4	13,8	17,8	22,1	21,3	7,1	8,7	8,8
UK	38,5	43,0	42,7	15,7	16,8	16,9	13,0	15,0	14,9	6,0	6,8	6,8	3,8	4,3	4,1
EC	40,6	46,6	47,2	12,7	14,0	14,0	11,4	13,3	13,6	13,5	15,5	15,8	3,1	3,8	3,8

	Total expenditure			Current transfers			Actual interest payments[4]			Government consumption			Net capital transfers and gross capital formation		
	1979	1983[2]	1984[3]	1979	1983[2]	1984[3]	1979	1983[2]	1984[3]	1979	1983[2]	1984[3]	1979	1983[2]	1984[3]
B	53,1	58,9	58,9	24,7	26,9	26,7	5,3	9,8	10,4	18,6	18,3	18,1	4,4	4,0	3,6
DK	54,5	61,2	61,0	20,2	22,4	22,7	4,9	8,1	8,7	24,9	27,5	26,6	4,5	3,2	3,0
D	46,6	49,4	48,3	19,2	21,7	21,3	1,7	3,1	3,2	20,0	20,1	19,6	5,6	4,5	4,3
GR	34,1	42,0	42,7	8,9	15,8	15,9	4,5	3,3	3,4	16,3	18,7	18,9	4,4	4,2	4,5
F	45,3	52,0	53,2	25,7	29,9	30,6	1,6	2,7	3,3	14,8	16,1	16,1	3,3	3,3	3,3
IRL	49,1	59,1	58,1	16,2	20,4	19,9	6,6	10,0	10,4	19,5	21,9	21,1	6,8	6,8	6,6
I	45,4	56,6	56,8	19,2	22,3	22,4	6,0	9,6	9,8	15,7	18,8	18,7	4,5	5,8	5,9
L	52,5	61,3	60,8	28,0	32,5	33,0	0,9	1,0	1,2	15,2	17,4	17,4	8,3	10,3	9,3
NL	55,0	63,6	63,0	29,9	34,5	34,3	3,0	5,9	6,7	17,9	17,9	16,9	4,2	5,2	5,1
UK	41,7	45,1	44,8	14,2	15,8	16,1	4,6	4,9	4,5	19,9	22,1	21,7	3,1	2,4	2,4
EC	44,0	52,0	51,9	19,8	23,4	23,4	3,0	5,1	5,4	17,2	19,4	19,1	4,1	4,0	4,0

1 National accounts definition, excluding loans, advances and equities.
2 Estimates.
3 Forecasts.
4 Including miscellaneous current transfers for 1979.

Source: Commission services.

Table 5.3) has increased by 8 points between 1979 and 1983, reaching 52% for the Community as a whole. In three Member States, Denmark, Luxembourg and the Netherlands, it is above 60% in 1983; it is close to 60% in Belgium and Ireland; is above 50% in France and Italy; is close to 50% in the Federal Republic of Germany; and exceeds 40% in Greece and the United Kingdom. Of the main categories of expenditure, current transfers have contributed most to the rising share of public expenditure in GDP in the Community, while interest payments have contributed almost as much as public consumption. The weight of current transfers is highest in France, Luxembourg and the Netherlands (close to or above 30% of GDP).

The virtual stability in 1983 of net borrowing of general government as a percentage of GDP in the Community masks an increase in Belgium, France, Luxembourg and the United Kingdom, no change in Italy, and a fall in Denmark, the Federal Republic of Germany, Greece, Ireland, Italy and the Netherlands (see Table 5.4).

While the main concern of the budgetary authorities for 1983 has been to provide themselves with additional means of respecting their original budget targets in the face of the persistent weakness of activity, a number of Member States have set out broad guidelines covering several years ahead.

Public finance objectives over several years:

Belgium:	Reduction of central government borrowing requirement to 7% of GDP by 1985.
FR of Germany:	Quantified plan for federal government budget up to 1987. Regular reduction in deficit, going from DM 40 900 million in 1983 to DM 22 500 million in 1987.
Ireland:	Gradual reduction in current budget deficit and elimination by 1987.
The Netherlands:	Reduction of general government borrowing requirement to 7,5% of net national income by 1986.
United Kingdom:	Medium-term financial strategy setting public sector borrowing requirement at 8 000 million UKL (2,5% of GDP) for financial year 1984/85 and at UKL 7 000 million (2% of GDP) for financial year 1985/86.

In general, the preferred mode of action of the budgetary authorities is a moderation of public expenditure rather than an increase in taxes or social security contributions. No category of expenditure is spared in the search for economies. While a restructuring of expenditure in favour of productive expenditure is in principle being sought, the constraints imposed by the reduction of budget deficits do not always allow such forms of expenditure to be favoured or even to

Table 5.4

General government budgetary aggregates,[1] EC and Member States, 1981-84

(% of GDP)

	Gross saving (+) or dissaving (−)				Net lending (+) or borrowing (−)				Net interest payments				Net lending (+) or borrowing (−) less net interest payments			
	1981	1982	1983[2]	1984[3]	1981	1982	1983[2]	1984[3]	1981	1982	1983[2]	1984[3]	1981	1982	1983[2]	1984[3]
B	−8,2	−7,6	−8,2	−7,5	−12,6	−11,9	−12,2	−11,1	7,2	8,6	9,2	10,2	−5,4	−3,3	−3,0	−0,9
DK	−3,1	−5,4	−5,6	−4,8	−7,0	−9,1	−8,8	−7,8	1,8	2,5	4,9	5,4	−5,2	−6,6	−3,9	−2,4
D	1,1	1,2	1,3	2,1	−3,9	−3,5	−3,3	−2,1	1,7	2,2	2,6	2,8	−2,2	−1,3	−0,7	−0,7
GR	−5,6	−2,8	−2,2	−1,9	−10,1	−6,4	−6,3	−6,3	:	:	:	:	:	:	:	:
F	1,4	0,6	0,1	−0,1	−1,8	−2,7	−3,1	−3,3	1,5	1,4	1,9	2,4	−0,3	−1,3	−1,2	−0,9
IRL	−7,3	−8,2	−6,6	−5,2	−15,8	−16,2	−13,4	−11,8	8,1	9,5	10,1	10,2	−7,7	−6,7	−3,3	−1,6
I	−6,8	−6,7	−6,1	−4,1	−11,7	−11,9	−11,9	−10,0	6,4	7,7	8,4	8,7	−5,3	−4,2	−3,5	−1,3
L	6,8	7,5	7,5	7,8	−2,3	−2,0	−2,9	−1,5	−2,6	−2,2	−1,9	−1,5	−4,9	−4,2	−4,8	−3,0
NL	0,5	−1,6	−1,5	−1,9	−5,2	−6,9	−6,7	−7,1	2,4	2,5	3,3	3,6	−2,8	−4,4	−3,4	−3,5
UK	−0,6	0,1	0,2	0,4	−2,9	−2,1	−2,2	−2,1	3,5	3,2	3,1	3,0	0,6	1,1	0,9	0,9
EC	−1,3	−1,4	−1,3	−0,7	−5,2	−5,2	−5,4	−4,7	3,0[4]	3,3[4]	3,8[4]	4,1[4]	−2,2[4]	−1,9[4]	−1,6[4]	−0,6[4]

1 National accounts definition, excluding loans, advances and participations.
2 Estimates.
3 Forecasts.
4 Excluding Greece.

Source: Commission services.

escape reductions. The results for 1983, moreover, show that capital expenditure has decreased or remained unchanged (in nominal terms) in five of the ten Member States (it should be noted that not all capital expenditure is 'productive', and that some categories of current expenditure, notably some items of government consumption, can be 'productive'). Further, some Member States consider that priority should be given to the development of the productive private sector. In this respect, while increasing or maintaining productive public expenditure is not seen as a priority by certain countries (in particular Denmark, the Federal Republic of Germany, the Netherlands and the United Kingdom), measures have been introduced there to support private investment by improving the fiscal and financial environment for companies. Further, a substantial public capital expenditure effort is being kept up in Greece, France, Italy and Luxembourg.

5.2 Interest charges and general government indebtedness

The strong growth of the net interest payments of general government has constituted an additional element of rigidity in budgetary management. Table 5.4 and Graph 5.1 show the development of these payments as a percentage of GDP. The increase in the Community in net interest payments was relatively modest up to 1978-79 (after, it is true, a jump in 1975), but accelerated from 1980 onwards. The year 1975 represents a turning-point for countries like Belgium and Italy whose interest charges as a percentage of GDP have grown regularly since that date. Another turning-point is constituted by the years 1979-80, since when net interest payments have grown substantially in all but one of the Member States. The notable exception is the United Kingdom, which has recently succeeded in reversing the upward trend. In 1983, the charge represented by interest payments on public debt is very heavy in three Member States, Italy (8,4% of GDP), Belgium (9,2%) and Ireland (10,1%). Moreover, the charge has practically doubled between 1982 and 1983 in Denmark, reaching 4,9%.

Table 5.4 and Graph 5.2 also show net borrowing of general government, after deduction of net interest payments, as a percentage of GDP. This presentation is justified to the extent that interest charges represent the present net financial cost of past budgetary operations via the accumulation of public debt. A calculation of net borrowing after deduction of net interest payments[1] thus gives a more precise indication of the contribution of current tax and expenditure policies to economic expansion. Thus corrected, the budget deficit of the Community, which moved from 1% of GDP in 1980 to 2,2% in 1981, dropped back to 1,9% in 1982 and 1,6% in 1983. Net borrowing after deduction of net interest payments is being reduced this year in all the Member States except Luxembourg, while the net lending of generally government in the United Kingdom is dropping slightly.

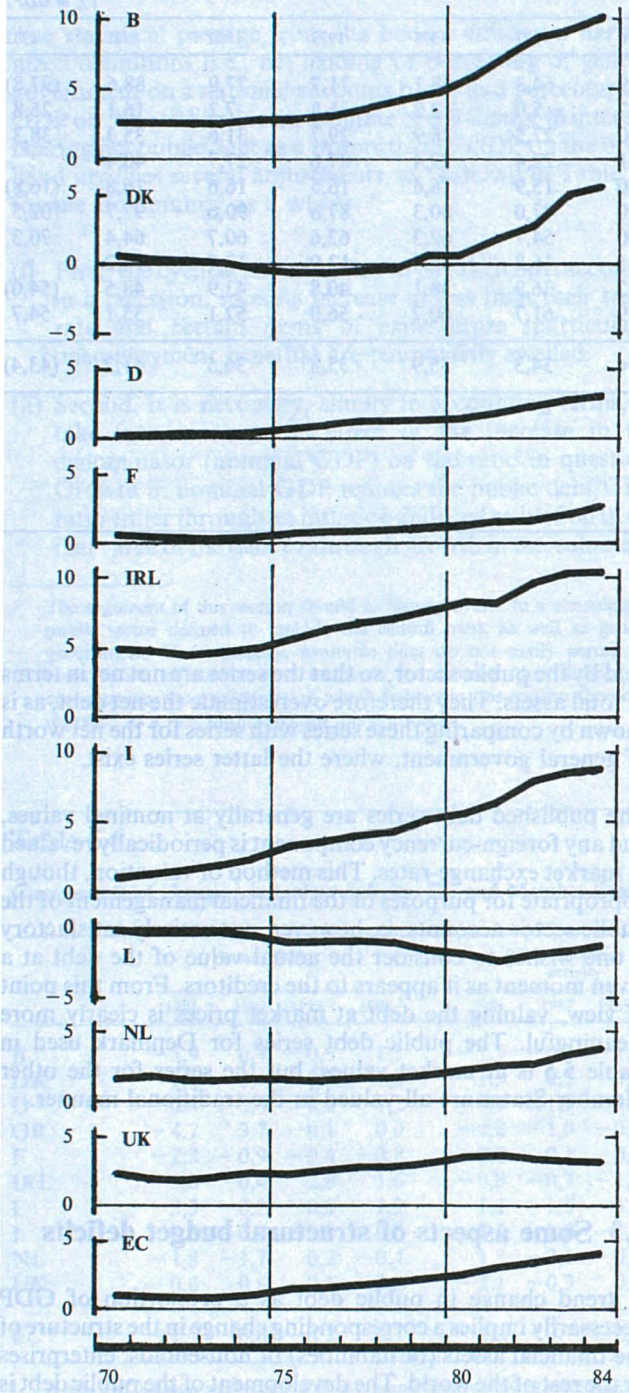
Debt interest charges depend directly on the size and development of budget deficits and on interest rates. The size of deficits explains the importance of interest payments as a percentage of GDP and, especially, the regular increase Belgium, Ireland and Italy have recorded since the beginning of the 1970s. The deterioration observable in 1980 and later years in all the Member States has been amplified by the slowdown in growth which has increased the burden of that debt contracted in a period of sustained growth.

But the cost of debt service has also been increased since 1979 by the general rise in interest rates. This increase, which took place practically simultaneously with the acceleration of inflation and the slowdown in real activity, has very rapidly created an important additional charge in government budgets. This development has proceeded at a different pace in the various Member States: where the debt is principally longterm and its average maturity distant, the repercussions of the rise in rates come through more slowly. The same is true when the authorities issue indexed securities and when public debt is exclusively, or almost exclusively, held domestically and mainly on a fixed interest rate basis. By contrast, those Member States with a substantial external debt have very rapidly felt the impact of the rise in interest rates, partly because the increase in rates began in the United States and was transmitted through the international capital markets, and partly because the greater part of loans raised in the international markets are at floating rates. Thus Belgium, Denmark, Greece and Ireland found themselves relatively more exposed than the other Member States.

A period of stagflation like that experienced by the Community in 1980 and 1981 is also likely to engender an explosion of interest charges. First, the slowdown in activity increases budget deficits; second, the persistence of strong inflation expectations pushes up interest rates. Economic agents, aware of the loss in the real value of their financial wealth, take up new government securities only at substantially increased yields. If actual inflation is higher than anticipated inflation, expectations deteriorate further and the placing of government securities becomes more difficult. Moreover, it can be seen that the influence of such expectations on market behaviour and thus on the increase in or maintenance of high interest rates has increased in recent years. The slowdown in inflation in the Community which began in 1982 was taken account of by the markets only after a delay. As a result, the fall in yields was held up and at times caused real difficulties in some Member States in securing the take-up of public sector securities.

[1] Actual interest payments minus interest receipts.

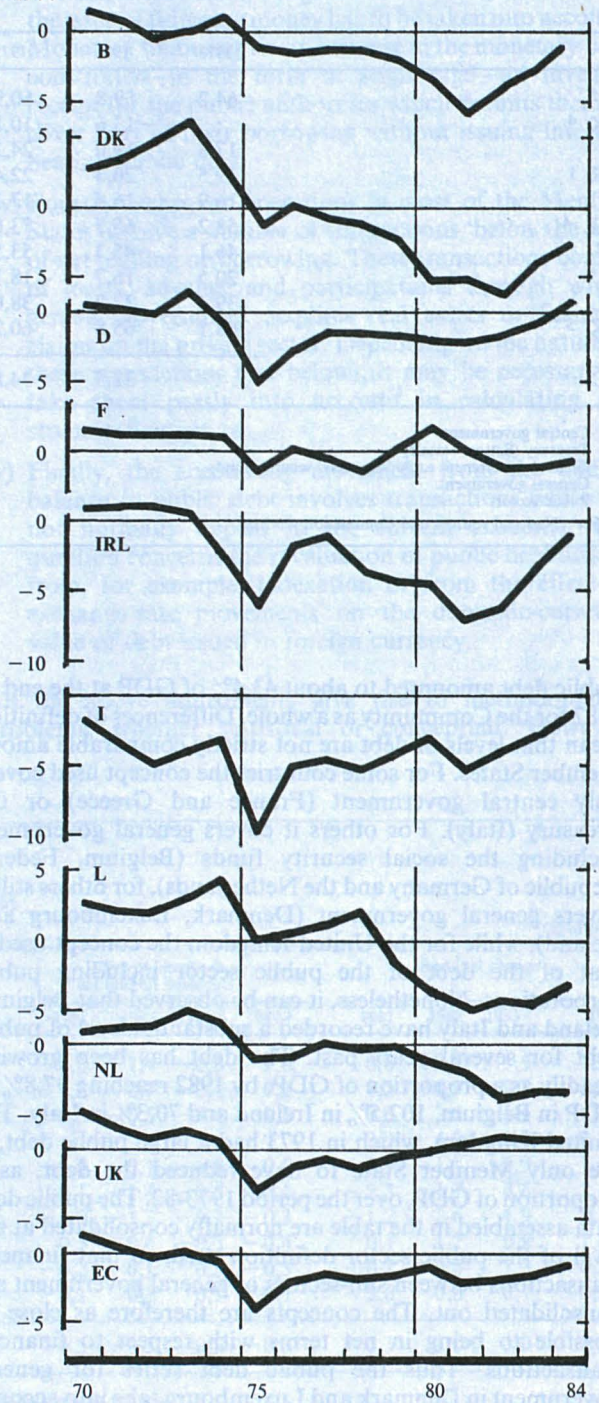
GRAPH 5.1: **Trend of general government net interest payments, as % of GDP, since 1970**



1983: estimates; 1984: forecasts.

Source: Eurostat and Commission services.

GRAPH 5.2: **Trend in general government net lending (+) or borrowing (−) less net interest payments, as % of GDP, since 1970**



Source: Eurostat and Commission services.

Table 5.5

Public debt, 1973-82

(% of GDP)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
B [3]	64,2	59,8	60,9	60,9	64,3	68,1	71,7	77,9	88,6	(97,8)
DK [4]	:	−13,6	−10,1	−7,7	−5,0	−2,2	1,8	7,2	16,1	25,8
D [3]	17,8	19,0	24,2	26,0	27,5	28,9	29,7	31,6	35,3	38,3
GR [1]	19,5	20,3	22,4	22,1	22,4	29,4	27,6	27,7	40,4	:
F [1]	16,9	16,4	17,1	16,0	15,9	16,6	16,5	16,6	16,8	(16,8)
IRL [4]	58,2	65,5	73,6	79,0	77,0	80,3	87,8	90,6	97,7	102,5
I [2]	46,1	45,3	53,5	52,0	54,7	62,3	62,6	60,7	64,4	70,3
L [4]	20,5	16,7	18,1	16,5	16,8	15,4	13,9	13,7	14,2	:
NL [3]	39,4	37,2	38,0	37,2	36,9	38,1	40,8	43,9	48,5	(54,0)
UK [5]	68,1	65,8	60,2	60,9	61,7	60,7	56,0	52,1	55,1	54,7
EC	:	32,5	34,8	34,4	34,3	35,9	35,8	36,5	41,2	(43,4)

1 Central government.
2 Treasury (Settore statale).
3 General government excluding social security funds.
4 General government.
5 Public sector.

Source: National sources and Commission services.

Public debt amounted to about 43,4% of GDP at the end of 1982 for the Community as a whole. Differences of definition mean that levels of debt are not strictly comparable among Member States. For some countries the concept used covers only central government (France and Greece) or the Treasury (Italy). For others it covers general government excluding the social security funds (Belgium, Federal Republic of Germany and the Netherlands), for others still it covers general government (Denmark, Luxembourg and Ireland), while for the United Kingdom the concept used is that of the debt of the public sector including public corporations. Nonetheless, it can be observed that Belgium, Ireland and Italy have recorded a substantial level of public debt for several years past. The debt has been growing steadily as a proportion of GDP, by 1982 reaching 97,8% of GDP in Belgium, 102,5% in Ireland and 70,3% in Italy. The United Kingdom, which in 1973 had a large public debt, is the only Member State to have reduced the debt, as a proportion of GDP, over the period 1973-82. The public debt data assembled in the table are normally consolidated at the level of the public sector definition used, so that financial transactions between sub-sectors of general government are consolidated out. The concepts are therefore as close as possible to being in net terms with respect to financial transactions. Thus the public debt series for general government in Denmark and Luxembourg take into account the considerable financial assets held by the social security funds. However, the consolidation of financial assets and liabilities does not apply to the shares and physical asssets held by the public sector, so that the series are not net in terms of total assets. They therefore overestimate the net debt, as is shown by comparing these series with series for the net worth of general government, where the latter series exist.

The published debt series are generally at nominal values, and any foreign-currency component is periodically revalued at market exchange-rates. This method of valuation, though appropriate for purposes of the financial management of the public sector accounts, is, however, not entirely satisfactory if one wishes to consider the actual value of the debt at a given moment as it appears to the creditors. From this point of view, valuing the debt at market prices is clearly more meaningful. The public debt series for Denmark used in Table 5.5 is at market values, but the series for the other Member States are all valued in the traditional manner.

5.3 Some aspects of structural budget deficits

A trend change in public debt as a proportion of GDP necessarily implies a corresponding change in the structure of the financial assets (or liabilities) of households, enterprises or the rest of the world. The development of the public debt is thus an essential element in any appreciation of the budgetary policy stance. A fall in the debt/GDP ratio may even be a target of medium-term financial strategy, for

example to reduce interest charges in the government accounts and to increase the financial resources available for private investment.

The statistical passage from the budget deficit on harmonized definitions (i.e., net lending or borrowing of general government on a national accounts basis) as a percentage of GDP on the one hand to an estimate of the change in interest-bearing net public debt as a proportion of GDP on the other hand involves several adjustments, as is shown in Table 5.7 for the Community as a whole: [1]

(i) First, the cyclical situation has to be taken into account: in a recession, receipts increase at less than their trend rate and certain items of expenditure (particularly unemployment benefits) are temporarily swelled.

(ii) Second, it is necessary, simply in accounting terms, to take into account the effect of the increase in the denominator (nominal GDP) on the ratio in question. Growth in nominal GDP reduces the public debt/GDP ratio either through an inflation-induced reduction in the real value of the debt or through growth in the volume of GDP and thus in the capacity of the economy to support a given level of public debt.

(iii) Third, the fact that a budget deficit is partly financed by the issue of fiduciary money has to be taken into account. Monetary financing via an increase in the monetary base constitutes—in the form of seignorage—an invisible receipt for the public authorities which permits them to cover part of their borrowing without issuing interest-bearing public debt.

(iv) Fourth, exchequer operations in most of the Member States involve a number of transactions 'below the line' of net lending or borrowing. These transactions consist of loans, advance and participations through which general government acquires real assets or financial claims on the private sector. Depending on the nature of these transactions (see below), it may be necessary to take them partly into account in calculating the structural deficit.

(v) Finally, the accounting movement from the budget balance to public debt involves transactions which do not normally appear in the current accounts. The question concerns the revaluation of public debt arising from, for example, indexation or from the effect of exchange-rate movements on the domestic-currency value of debt issued in foreign currency.

All the above adjustments give rise to methodological problems, whether statistical or conceptual. However,

[1] The argument of this section should in principle refer to a consolidated public sector defined to include the central bank as well as general government. Unfortunately, available data do not easily permit the construction of consolidated accounts for a sector thus defined. In consequence, the quantification which follows in this section should be regarded as a first outline within this approach.

Table 5.6

Components of change [1] in budget deficits, EC and Member States, 1981-84

(% of GDP)

	Actual change				Effect of change in activity				Effect of change in net interest payments				Residual change			
	1981	1982	1983 [2]	1984 [3]	1981	1982	1983 [2]	1984 [3]	1981	1982	1983 [2]	1984 [3]	1981	1982	1983 [2]	1984 [3]
B	−3,9	0,7	−0,3	1,1	−1,7	−0,1	−1,2	−0,4	−1,6	−1,4	−0,6	−1,0	−0,6	2,2	1,5	2,5
DK	−1,1	−2,1	0,3	1,0	−1,3	0,5	0,0	−0,7	−1,3	−0,7	−2,4	−0,5	1,5	−1,9	2,7	2,2
D	−0,4	0,4	0,2	1,2	−0,9	−1,7	−0,9	0,2	−0,3	−0,5	−0,4	−0,2	0,8	2,6	1,5	1,2
GR	−4,7	3,7	−0,1	0,0	−0,8	−1,0	−0,9	−0,2	:	:	:	:	−3,9 [4]	4,7 [4]	0,8 [4]	−0,2 [4]
F	−2,3	−0,9	−0,4	−0,2	−0,8	0,1	−0,8	−0,7	−0,4	0,1	−0,5	−0,5	−0,9	−1,1	0,9	1,0
IRL	−3,0	−0,4	2,8	1,6	−0,8	−0,7	−1,2	−0,4	0,1	−1,4	−0,6	−0,1	−2,3	1,7	4,6	2,1
I	−3,3	−0,2	0,0	1,9	−1,1	−1,5	−1,2	−0,5	−1,0	−1,3	−0,7	−0,3	−1,2	2,6	1,9	2,7
L	−0,5	0,3	−0,9	0,6	−1,1	−1,0	−1,5	−0,8	0,5	−0,4	−0,3	−0,4	0,1	1,7	0,9	1,8
NL	−1,8	−1,7	0,2	−0,4	−1,5	−2,1	−0,3	−0,3	−0,2	−0,1	−0,8	−0,3	−0,1	0,5	1,3	0,2
UK	0,6	0,8	−0,1	0,1	−2,1	−0,3	0,5	0,3	−0,1	0,3	0,1	0,1	2,8	0,8	−0,7	−0,2
EC [4]	−1,7	0,0	−0,2	−0,7	−1,3	−0,7	−0,6	−0,1	−0,5	−0,3	−0,5	−0,3	0,1	1,0	1,0	1,1

[1] A plus sign indicates a reduction in general government borrowing requirement, a minus sign indicates an increase.
[2] Estimates.
[3] Forecasts.
[4] Including the effect of net interest payments.

Source: Commission services.

despite these problems and the uncertainties which result from them, it seems indispensable to take them into account as far as possible, with a view to making a judgement on the medium-term prospects with respect to 'structural budgetary problems'. An illustration of these adjustments and of their order of magnitude is given below.

The total impact of the loss of receipts and of additional cyclical expenditure caused by the recession in 1981, 1982 and 1983 is put in Table 5.6 at 2,6% for the Community as a whole. Of this, 1,3 points may be attributable to the decline in activity in 1981 following the second oil-price shock, while 1,3 points may be attributable to the weakness of activity in 1982 and 1983. A partial correction taking account only of the impact of the weakness in activity in 1982 and 1983 would thus reduce the net borrowing of general government from 5,4% of GDP to 4,1%, while a correction also incorporating the effect of the decline in activity in 1981 would bring the deficit down to 2,8% of GDP (see Table 5.7).

Since public debt at the beginning of 1983 was 43,4% of GDP and the rate of growth of nominal GDP in 1983 is put at 6,9%, the budget deficit compatible with an unchanged debt/GDP ratio can be estimated at 3,0% (0,434 x 0,069). These figures for the EC as a whole mask, however, very divergent situations for the Member States. The budget deficit compatible with a constant debt/GDP ratio ranges from around 1,5% of GDP in Germany and France to around 10% for Greece, Ireland and Italy.

The change in the monetary base constitutes a source of implicit revenue to the government, through nominal monetary financing. Including only notes in circulation (for which statistical problems are relatively unimportant), the monetary base amounts to approximately 6% of GDP on averge for the Community. Nominal GDP growth of 6,9% should thus entail a rise in the monetary base equivalent to about 0,4% of GDP, showing that it should be considered as a source of budget financing on a par with tax receipts.

The above analysis of the budget balance is founded on the notion of the 'net borrowing of general goverment', which represents the financial saving of this sector in the framework of harmonized national accounts. This budget balance concept includes only fixed investment and capital transfers by general government and not capital transactions involving the acquisition of financial assets, such as loans, advances and participations. But to some extent these transactions involve rescue operations comparable to capital transfers with no genuine counterpart in the form of financial assets bringing an assured return. In other cases, by contrast, they involve loans (housing loans, for example) traditionally financed through the public sector, or the acquisition of real assets in the enterprise sector in pursuit of a particular industrial policy or of the enlargement of the public sector. In some cases (denationalization), the balance of these transactions can become positive, thus allowing the Treasury to cover a part of its borrowing needs by the sale of real assets. The relative importance of this category of transactions varies considerably from one Member State to another, often as a result of institutional differences in financial circuits. There is a high level in Belgium (2,4% of GDP in 1983), Italy (3,5%), Luxembourg (3,8%), the Netherlands (2,0%) and the United Kingdom (1,0%) but in Germany and Ireland the level is close to zero (data are not available for Denmark, Greece and France).

Besides the financing of the acquisition of real or financial assets by the public sector, the level of public debt can be affected by adjustments of principal through, for example, indexation or a change in the domestic-currency value of debt denominated in foreign currency. Finally, there may be a statistical difference between the net borrowing requirement of the public sector on the one hand and the change in public debt on the other if the central government borrows foreign currency abroad in order to supplement the central bank's foreign exchange reserves. The gross monetary debt of the central government increases by the amount of the loan, but the net debt of the public sector (including the

Table 5.7

Illustrative features of the structural budget balance, EC total, (1983)

(% of GDP)

	I [1]	II [2]	III [3]
Net lending or borrowing of general government	−5,4	−5,4	−5,4
Correction for effect of cyclical fluctuations	2,6	1,3	1,3
Effect of nominal GDP growth on public debt/GDP ratio	3,0	3,0	3,0
Change in monetary base (normal monetary financing)	0,4	0,4	0,4
Loans, advances and participations	—	−0,5	−1,0
Trend development of public debt as % of GDP 6 = −(1 + 2 + 3 + 4 + 5)	−0,6	+1,2	+1,7

1 Optimistic assumption about cyclical correction; no correction for loans, advances and participations.
2 Cautious assumption about cyclical correction; some correction for loans, advances and participations.
3 Cautious assumption about cyclical correction; larger correction for loans, advances and participations.

Source: Estimates of Commission services.
Note: See text for methodology.

central bank) is unaffected. The impact of these revaluation factors is not known directly.

On balance, a relatively cautious interpretation of the estimates in Table 5.7 seems to show that after two years of major efforts to compress expenditure (excluding interest payments), the Community may have been able to achieve a significant improvement in its underlying financial position; this is also shown by the reduction in net borrowing, excluding net interest payments, since 1981. On the assumption of a medium-term growth rate higher than 2% (from 1983 onwards), public debt (net of financial assets acquired through loan transactions) could rapidly stabilize as a proportion of GDP. However, within this overall situation, in a number of Member States it would be possible for the debt/GDP ratio to be kept constant only through a high rate of inflation implying a corresponding erosion of the real value of the debt. In these cases, the aim of economic policy should remain that of a parallel reduction in inflation and the budget deficit.

Main budgetary policy measures in Member States affecting the financial years 1983 and 1984

In *Belgium*, the draft central government budget for 1983 was tabled in parliament on 8 October 1982. Revenue was estimated at BFR 1 278 200 million compared with BFR 1 158 800 million in 1982, and authorized expenditure, excluding special funds financed under the budget, was set at BFR 1 701 300 million compared with BFR 1 597 700 million in 1982. The Treasury's net borrowing requirement was put at BFR 443 000 million. On 29 October, the government adopted a series of tax measures, in particular a change in the method of calculating the taxable income of households with only one source of earned income, and the introduction of a new intermediate VAT rate of 19% for most goods and services previously taxed at 17% whilst other goods and services were taxed more heavily. This last measure was expected to bring in additional revenue amounting to BFR 15 000 million in a full year. In March 1983, the government noted that, on the basis of recent developments, the budget deficit would overshoot the original estimate by BFR 52 400 million. In order to mop up this sum, the authorities decided on 12 March to reduce expenditure by BFR 39 400 million, principally by deferring payment of the end-of-year bonus to public servants, and to increase revenue by raising social security contributions, by introducing measures to discourage households with a net annual income of BFR 750 000 francs from combining unemployment benefit or income, and by increasing excise duty on certain oil products. On 22 June, the government decided to extend the reduced VAT rate of 6% on construction until the end of 1985, in order to boost this sector. According to the Commission, the net borrowing requirement of general government could amount to 14,6% of GDP in 1983, compared with 14,8% in 1982. The main features of the preliminary draft budget for 1984 were presented at the beginning of August. On 30 September the government confirmed the measures announced and on 3 October it tabled its draft budget for 1984. A number of economies, notably in the public service, were envisaged, as well as an increase in the withholding tax on interest and in social security contributions (part of which was to take effect on 1 October 1983). The increase in current receipts (in comparison with the revised 1983 budget) was put at 8% for 1984 and that in expenditure at 5,5%. The net borrowing requirement, on a cash basis, is put at BFR 507 400 million in 1984 (11,3% of GDP), against BFR 530 900 million (12,7%) in 1983.

In *Denmark*, the draft budget for 1983 prepared by the previous government in August 1982 provided for a deficit on current account, capital account and central government lending of DKR 80 200 million, or 15,4% of GDP. The new government presented its economic policy programme to parliament on 5 October. It provided for a wage freeze until 1 March 1983, a suspension of the index-linking of remuneration until January 1985 and a reduction in certain social transfer payments and subsidies. These measures, which parliament adopted with a few changes, make for an estimated deficit on current account, investment and lending of DKR 68 900 million in 1983 (13,4% of GDP). Bearing in mind the expected increase in 1983 of the public debt interest burden, the deficit, excluding those interest payments, is likely to be smaller than in 1982. In the first half of 1983, the Minister of Finance estimated that the deficit could be brought down to DKR 64 400 million (12,7% of GDP) through slower rises in prices and unemployment, lower interest rates and increased tax receipts. On Commission estimates, the net public sector borrowing requirement could amount to 10,3% of GDP in 1983, compared with 12,3% in 1982. In mid-August the government presented its draft budget for 1984. This reduced the target for the 1984 current deficit to DKR 59 300 million (10,9% of GDP, against 12,4% in 1983). Expenditure was to rise by 1,7% because of major budget cuts, and receipts were to rise by 8,5%.

In the *Federal Republic of Germany*, the new government presented its draft budget for 1983 on 27 October 1982. Total federal government expenditure was put at DM 253 400 million and the deficit at DM 41 500 million. The budget adopted by parliament in mid-December fixed expenditure at DM 253 200 million and the deficit at DM 40 900 million, and provided for certain cutbacks, particularly in the area of social expenditure, and measures to encourage investment. It was also decided to raise the VAT rate by one point with effect from 1 July 1983. Budget expenditure in 1983 was set to rise by 2,9% over 1982 and the increase in revenue was projected at 3%, while the federal government deficit was planned to stand at 2,5% of GDP, as in 1982. In March 1983, the government agreed on a four-year budget programme covering the years 1984 to 1987. Under this programme, the federal government deficit should be kept below DM 40 000 million in 1984 through budget cutbacks amounting to DM 6 500 million. The measures adopted by the government in May set limits on the annual rate of increase in public expenditure of 2% in 1984 and 3% in the following years until 1987, aim at a federal government deficit of DM 39 000 million in 1984 and its gradual reduction to DM25 000 million in 1987, cut expenditure, essentially in public consumption and social transfer payments, and reduce the tax burden on companies. On 29 June, the Government adopted its draft budget for 1984. Expenditure was set at DM 257 800 million, representing an increase of 1,8% compared with 1983, and the federal government deficit was estimated at DM 37 340 million. Budget savings mainly concerned transfers to households and public consumption. The net general government borrowing requirement was forecast by the Commission at 3,3% of GDP in 1983 compared with 3,5% in 1982. In September, a quantified plan for the federal government budget up to 1987 was presented. It envisaged a steady reduction in the deficit from DM 40 900 million in 1983 to DM 22 500 million in 1987.

In *Greece* the draft government budget for 1983 was presented to parliament on 29 November 1982. Revenue was set to rise by 34,3% and expenditure by 29,5%, with a deficit of DR 288 400 million (9,4% of GDP) compared with DR 247 100 million in 1982 (9,9% of GDP). It was decided to slash current expenditure and concentrate resources on public investment, which is to increase by 47,7%. Under the medium-term plan (1983-87) which was presented to parliament in draft form on 5 June 1983, the budgetary conditions for its success involved a reduction in the public sector borrowing requirement (in cash terms and including public enterprises) to 16% of GDP in 1983 (compared with 17% in 1981) and to 15% in 1984. Tax equity measures were also planned. Commission estimates made in October, put

general net borrowing at 6,3% of GDP in 1983 as against 6,4% in 1982.

In *France*, the 1983 draft budget was passed by parliament in November 1982. The key macroeconomic assumptions on which it was based were GDP growth of 11,1% in nominal terms and of 2% in real terms. Expenditure and revenue were forecast to rise by 11,8% and 10% respectively, i.e. much lower rates than in 1982. The central government deficit was put at FF 117 000 million and, as a result, remained within the limit of 3% of GDP set by the authorities. The intention was twofold: to impose a tight squeeze on current expenditure and to reinforce measures to promote research, industrial development, employment and low-cost housing. In addition, cuts in expenditure on unemployment benefits (FF 12 000 million) and on social security benefits were decided on by the government in late November and early December. On 25 March, the government unveiled a package of measures to back up the 21 March devaluation of the French franc. Savings were to be made in the central government budget (FF 15 000 million), in the social security budget (FF 4 000 million) and in the budget for public enterprises (FF 11 000 million), to be achieved in part through increases in public service charges. An exceptional, 1% levy on incomes and a compulsory loan corresponding to 10% of the amount of income tax paid in 1981 were introduced and the taxation of oil products raised. In autumn, the Commission estimated that the general government net borrowing requirement could be equal to 3,1% of GDP in 1983, as against 2,4% in 1982. On 14 September the Council of Ministers adopted the draft budget for 1984. It limited the rise in central government expenditure to 6,3% and also estimated the increase in receipts as 6,3%. The budget deficit target was FF 125 000 million, 3% of GDP. A shift in expenditure towards the areas given priority in the Ninth Plan (industry, research, employment, education) was implemented. The exceptional 1% income tax was reimposed for 1984, a progressive surtax was introduced, and social security contributions were increased by one point.

In *Ireland*, the 1983 budget was presented to parliament on 9 February. The prime objective in the budget was to reduce the current budget deficit and the Exchequer Borrowing Requirement to 6,5% (IRL 897 million) and 12,5% (IRL 1 722 million) of GDP respectively in 1983, compared with the figures of 8% and 16% recorded in 1982. To this end, it was decided to hold current expenditure steady in volume terms and to reduce capital expenditure slightly in real terms. Indirect taxes were raised, the measures including increases in the 18% and 30% VAT rates to 23% and 35% respectively, and no indexation of direct tax scales was allowed. In July the government, in the face of upward pressures on the planned level of expenditure, announced cuts of some IRL 50 million in current expenditure and IRL 20 million in capital expenditure. Excise duties were also raised. As a result, the current deficit for 1983 was put at around IRL 950 million and the Exchequer Borrowing Requirement at some IRL 1 750 million. Commission estimates, made in October, put general government net borrowing at 13,4% of GDP in 1983, compared with 16,2% in 1982.

In *Italy*, the 1983 budget tabled by the outgoing goverment in November 1982, provided for a Treasury deficit of some LIT 70 000 000 million (13% of GDP). The draft finance law envisaged a number of tax measures and proposed spending cuts. At the end of 1982, the new government took the view that, if no action were taken, the underlying Treasury deficit for 1983 would easily exceed the figure of LIT 70 000 000 million. For this reason, the government approved on 30 December 1982 and 7 January 1983 a set of decree-laws and draft laws designed, on the one hand, to finance part of the previous budget under provisions laid down in the finance law and, on the other, to meet new expenditure or to compensate for cuts that could not be carried through. A package of tax increases, most of them of an exceptional nature, was adopted in this context. When the quarterly report on public-sector accounts for 1983 was presented to parliament on 9 March, the government reaffirmed its determination to hold the public-sector deficit below the target of LIT 71 000 000 million (13,3% of GDP, compared with 14,9% in 1982). At the end of March, the finance law approved by Parliament fixed the Treasury deficit at LIT 75 890 000 million. Since the budget plan set in motion at the beginning of 1983 proved only partially successful in the first half of the year (reduction of LIT 15 000 000 million in the underlying deficit as against one of LIT 30 000 000 million projected in January), the underlying budget deficit was, at the end of June, put at LIT 86 300 000 million. The government formed in September 1983, following the June elections, set out its 1984 budgetary policy on 30 September. It decided to take a series of tax and expenditure-cutting measures, amounting to some LIT 50 000 000 million, in order to limit the public sector deficit to LIT 90 000 000 million, or 15% of GDP. To bring this programme into effect, the government passed a number of decree-laws and submitted the finance law. All of these measures were intended to be subsequently ratified by the parliament. This package of measures inolved receipts of LIT 23 000 000 million and expenditure economies of LIT 21 000 000 million, including a fall of LIT 6 000 000 million in interest payments as a result of the reduction in the deficit trend and in the level of interest rates. In addition to these economies, various public sector bodies were to transfer to the Treasury the sum of LIT 5 000 000 million from their bank deposits.

In *Luxembourg*, the central government budget for 1983, incorporating minor changes from the draft budget drawn up in August 1982, was adopted by parliament on 15 December. Revenue totalled LFR 60 100 million and expenditure LFR 60 000 million, giving gross borrowing of LFR 493 million. In April, the government decided, as part of its restructuring plan for the steel industry, to grant financial assistance of LFR 11 500 million spread over 1983 (LFR 7 500 million) and 1984 (LFR 4 000 million). In order to finance the plan, VAT rates and excise duties on tobacco and alcohol were increased, as were telephone charges and the solidarity tax. These measures, which took effect on 1 July, were expected to bring in LFR 4 500 million on an annual basis. In addition, the government intends to borrow LFR 2 000 million in 1983 and LFR 2 000 million in 1984. Accordingly, the Commission services estimated in October that the general government net borrowing requirement could rise from 2,2% of GDP in 1982 to 3,6% in 1983. The government on

1 August presented the draft 1984 budget: total expenditure is to be reduced by 1,5% while receipts (excluding borrowing) are to rise by 7,6%. The net borrowing requirement was estimated at LFR 1 200 million as against LFR 7 800 million in 1983. The gross budget balance is estimated to turn positive (LFR 800 million as against a deficit of LFR 5 800 million in 1983).

In the Netherlands, the outgoing government presented on 21 September 1982 a draft budget for 1983 that was characterized by only modest growth in exenditure as a result of retrenchment (amounting to HFL 12 100 million) in the social security and central government budgets. The general government cash deficit for 1983 was put at 10,8% of net national income. The new governing coalition of Christian Democrats and Liberals, which took office on 4 November, announced to parliament on 22 November the main thrust of its economic policy. For 1983, the general government net cash borrowing requirement indicated in the draft September budget, and now put at 11,9% of net national income was maintained but the planned increases in taxation (HFL 1 600 million) were jettisoned and expenditure cuts announced instead. It was also decided that, after 1983, the deficit would be reduced each year by an amount equivalent to 1,5% of net national income, bringing it down to 7,5% by 1986. In April, the updated budget notified by the government to parliament showed a deterioration in the net budgetary position of HFL 3 500 million, of which HFL 3 000 million was due to additional expenditure. The government proposed expenditure cuts totalling HFL 2 000 million (housing, national education, public servants, holiday bonus), increases in certain taxes, including petrol tax, and in social security contributions as well as reductions in social security benefits. Overall, it was estimated that the deficit would show a further increase equivalent to some 0,5% of net national income. The revised budget was adopted by parliament in June. In preparation for the 1984 budget, the government decided in July to bring in a programme to reform public finances, the changes amounting to HFL 11 000 million, with most of the proposed measures to take effect on 1 January 1984. The key points in the programme were savings in departmental expenditure, the wage and salary bill, public health spending, social security benefits and holiday bonuses payable in the event of sickness. The draft budget for 1984 was tabled on 20 September. According to it the net cash borrowing requirement for the public administration would be reduced from 12,4% of net national income in 1983 to 12,1% in 1984. With a view to limiting the growth of expenditure, the government proposed budgetary savings of HFL 11 700 million (of which 10 600 million with effect in 1984), in the fields of wages and salaries, social security, health and the spending of other ministerial departments. In the field of receipts the proposal envisages a lightening of taxes and social premiums on firms amounting to HFL 2 000 million, and an increase in other taxes (HFL 3 000 million in 1984) including an increase of 1 point in both the reduced and the normal rate of VAT.

In the United Kingdom, the Chancellor of the Exchequer announced on 8 November 1982 a number of measures and a revised public expenditure programme for 1983-84. The main points were a further reduction in the National Insurance Surcharge in 1983, to 1,5%, and increases in employers' and employees' social security contributions in April 1983. The revised level of planned public expenditure for 1983-84 was put at UKL 120 100 million, slightly lower than the figure announced in March 1982, and the public sector borrowing requirement for 1983-84 was, allowing for the introduction of further tax concessions or a UKL 1 000 million increase in expenditure, estimated at UKL 8 000 million, or 2,75% of GDP. On 1 February 1983, the government published the White Paper 'The Government's Expenditure Plans 1983-84 to 1985-86', giving revised estimates of its public exenditure for the financial year 1982-83 and plans for the next three years. For 1983-84, expenditure was planned to increase by 5,8% over the previous financial year, its level in real terms remaining virtually unchanged. On 15 March, the government presented its budget for 1983-84, along with a revised version of the medium-term financial strategy. The budget provided for a rise in expenditure in line with that indicated in the White Paper (5,8%), increases in personal tax allowances running ahead of the rate of inflation, a reduction in taxation of North Sea oil production, increases in excise duties and a further reduction in the National Insurance Surcharge. The public sector borrowing requirement remained unchanged at UKL 8 000 million (2,75% of GDP). The medium-term financial strategy set a target range for monetary growth in 1983-84 of 7%-11% for a range of aggregates and fixed the public sector borrowing requirement at UKL 8 000 million (2,5% of GDP) for 1984-85 and at UKL 7 000 million for 1985-86. It became apparent in April that the budget deficit of UKL 9 200 million in 1982-83 was running substantially higher than had been estimated in the March budget (UKL 7 500 million). As a result, a relatively more restrictive bias was imparted to budgetary policy for 1983-84. On 7 July, the Chancellor of the Exchequer announced a package of measures aimed at reducing the borrowing requirement for the current financial year by UKL 1 100 million in order to keep it on the course mapped out in March. The measures included spending cuts of UKL 500 million, the sale of public assets worth UKL 500 million and the postponement of capital expenditure totalling UKL 100 million to the next financial year.

6. Monetary policy and the European Monetary System

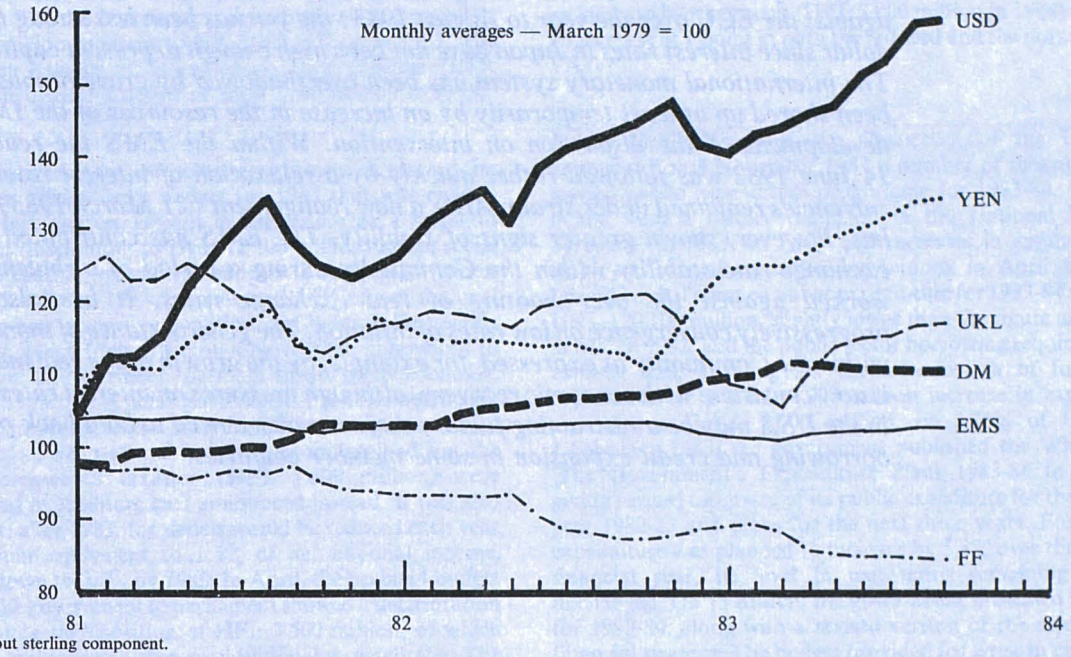
The international environment was characterized in the second half of 1982 by a marked relaxation of monetary policy in the USA, but in 1983 the unprecedented US federal budget deficit has led to a renewed tightening of conditions. The US dollar showed a rise against the ECU over the year to August 1983; the yen has been less strong than the US dollar since interest rates in Japan have not been high enough to prevent capital outflows. The international monetary system has been overshadowed by grave problems, but has been shored up at least temporarily by an increase in the resources of the IMF, and the development of the discussion on intervention. Within the EMS the realignment of 14 June 1982 was followed rather quickly by a relaxation of interest rates; however, currencies remained under strain. After a new realignment (21 March 1983) the system has, however, shown greater signs of stability. The EMS has contributed to nominal exchange rate stability within the Community during a period of turbulence, and has worked against the over-shooting of real exchange rates. It has also promoted progressively convergence on low rates of inflation. The general stance of monetary policy within the Community as expressed, for example, by the growth of the real money supply, is now consistent with economic recovery, although pressures on interest rates originating in the USA may be a restraining factor; there remains a need to hold back public sector borrowing and credit expansion in some member countries.

6.1. The international context

The broad international environment within which Community monetary policies have to take their place has been characterized by a succession of important changes during the period under review. From July 1982 onwards the meetings of the Open Market Committee of the US Federal Reserve System began to signal a shift in the stance of US monetary policy. Innovation by US financial institutions following the lifting of certain regulatory constraints made the interpretation of the monetary data, particularly that relating to M1, difficult, but the Open Market Committee was also influenced to some extent by a deterioration in business sentiment, by the rising number of bankruptcies and by a general perception of an increased demand for liquidity. The outcome was that over the year ending in the fourth quarter of 1982, M2 grew by 9,3% in the US (just above the upper limit of its target range), and thus considerably more rapidly than did nominal GDP, whereas in the previous year the reverse had been the case. In parallel with this process interest rates fell in New York and the 13-week Treasury bill yield was virtually halved between the middle of February 1982 and a low of just over 7% in the second half of September; and the USD was temporarily weak on the exchanges.

Since the turn of the year, however, the emergence of an unprecedented federal budget deficit, which virtually doubled in one year to reach 6,5% of GDP in the fiscal year ending in September 1983, has prevented any further easing of monetary conditions in the USA and tended to put the process into reverse. M2 rose by an annualized 16% over the six months to May 1983 and a large part of that rise was accounted for by banks' acquisition of Treasury securities. Notwithstanding persistent difficulties of interpretation, the development could not be ignored by the Federal Reserve. The discount rate, which had been progressively cut by 3,5 points in the second half of 1982 was held at 8,5% and official operations were conducted in a way which tended to push the 13-week Treasury bill yield towards 9,5%; the first rise in the prime rate for 18 months—to 11%—came in early August 1983. Whereas nominal interest rates thus remained much below earlier levels, the rapid deceleration of inflation meant that the improvement in real interest rates was much less; in July 1983 the long term government bond yield was 8,5 points above the 12-month rise in consumer prices, an unprecedented margin. The availability of high yields led, in a process which came to feed on itself, to renewed upward pressure on the exchange rate of the US dollar—see Graph 6.1. The Federal authorities persisted for a long time in their determination not to intervene on the foreign exchange market and the USD, having gained 21% against

GRAPH 6.1: **Movement of major currencies and the EMS [1] against the ECU**



[1] ECU without sterling component.

the ECU in 1981, rose a further 13% in the first half of last year; although the process moderated in the second half of 1982, the impact of the Federal government's borrowing requirement reignited the process. A particularly sharp rise in the middle of August 1983 was countered by concerted intervention by the major authorities (other than those of the UK), but even at the end of that month the USD/ECU rate stood 12% above its levels of a year previously. The rise of the USD has damaged the price competitiveness of US products and contributed to the record current account deficit of 1983.

The Japanese yen rose more slowly in the period under review, gaining 5% against the ECU in the course of 1982. The relative performances of the yen and the USD are the more remarkable for the fact that Japan is running a balance of payments current account surplus. The weakness of the yen against the USD is in fact explained by the very large net outflow of private capital from Japan last year, following the relaxation of exchange control in December 1980, and this in its turn suggests that interest rates in Japan may not be sufficiently high; the discount rate has remained at 5,5% since the end of 1981 and the cost of bank loans in Japan came down about half a point during 1982, to about 7%, whereas the US prime rate came down only to 10,5% in February 1983. The public sector borrowing requirement [1] in Japan was below 3% of GNP in 1973 but subsequently rose sharply and was equal to 7,1% of GNP in 1982. M2 [2] rose by 7,9% in Japan in 1982, while M3, [2] which is particularly influenced by public sector borrowing, rose by 9,2%. Both these rates of monetary expansion were well above the rate of growth of nominal GNP. Although the liquidity ratio has shown a long-run upward trend in Japan these figures nevertheless suggest that interest rates may not have been high enough in that country to prevent an inappropriate degree of monetary financing of the public sector.

The international monetary system has been overshadowed for the past year by the problems of certain highly-indebted countries. A number of measures have however been taken to strengthen it, mainly by way of increasing the resources available to assist the adjustment process. The Community played its full part in the rapid and timely procedure by which the Interim Committee of the International Monetary Fund acted to bring forward the eighth quota increase of the

[1] Consolidated financial deficit of central government, local authorities and public corporations.

[2] Including certificates of deposit.

Fund and agreed to raise quotas by approximately 47%, in parallel with a substantial extension of both the resources and the role of the General Arrangements to Borrow. The IMF should be enabled to continue the conditional lending which helps to maintain confidence generally and acts as a catalyst to promote important private capital flows.

In pursuance of their commitment to promote a stable system of exchange rates as developed in the Joint Statement on Monetary Undertakings made at the Versailles Summit in June 1982, the eight summit participants have jointly reviewed the role of official intervention in the foreign exchange markets, drawing on the report of their working group. There is now general agreement that intervention can be useful not only to counter disorderly market conditions but also to reduce short-term volatility; and that intervention is more likely to be effective if it is not sterilized (see box). It might also be argued from recent experience that exchange rates can diverge over long periods from the path that would be indicated by economic fundamentals; on the other hand, intervention cannot resolve the problems which arise when a country's domestic policies are inconsistent with its exchange rate objectives. The participants at the Williamsburg Summit at the end of May renewed their commitment to a consultation process 'to promote convergence of economic performance in our countries and greater stability of exchange rates' and declared their willingness 'to undertake coordinated intervention in exchange markets in instances where it is agreed that such intervention would be helpful'. The 'Group of Ten' in September 1983 decided to follow up this work with a study by the Deputies of the group of ways to improve the functioning of the international monetary system.

6.2 Developments in EMS countries in the second half of 1982

The easing of monetary conditions in the USA after the middle of 1982 was paralleled to some extent in the Federal Republic of Germany, although interest rates in the Community have generally followed a smoother course than have US rates. On 1 July 1982 the Deutsche Bundesbank reaffirmed, in view of the improved balance of payments position, its intention of keeping the growth of the central bank money stock in the upper half of its target range. This policy was supported by cuts in the discount rate in August, October and December totalling two and a half points, and by a one-tenth cut in reserve ratios taking effect on 1 October. In the outturn the target variable rose over 6% over the 1982 target period, a considerable acceleration from 3,5% in 1981—see Graph 6.5. In December it was decided to continue with a target range of 4-7% in 1983. The French authorities had buttressed the realignment of their currency on 12 June 1982 by a five-month wages and prices freeze and by de-indexing arrangements which could subsequently link pay to targeted and not actual price increases; and by other measures including action designed to keep the general government borrowing requirement to 3% of GDP. The way thus seemed open for Paris money rates to fall and the intervention rate of the Bank of France was progressively cut by two and a half points in the second half of the year to stand at 12,75% at the year end, the process being supported by a cut in compulsory reserves on 1 July 1982 and 10 January 1983 which had the effect of cutting these ratios by more than half (to 2,5% for sight deposits). In a broadly parallel policy the Belgian authorities, who had moved economic policy to a more rigorous stance in the early months of 1982,

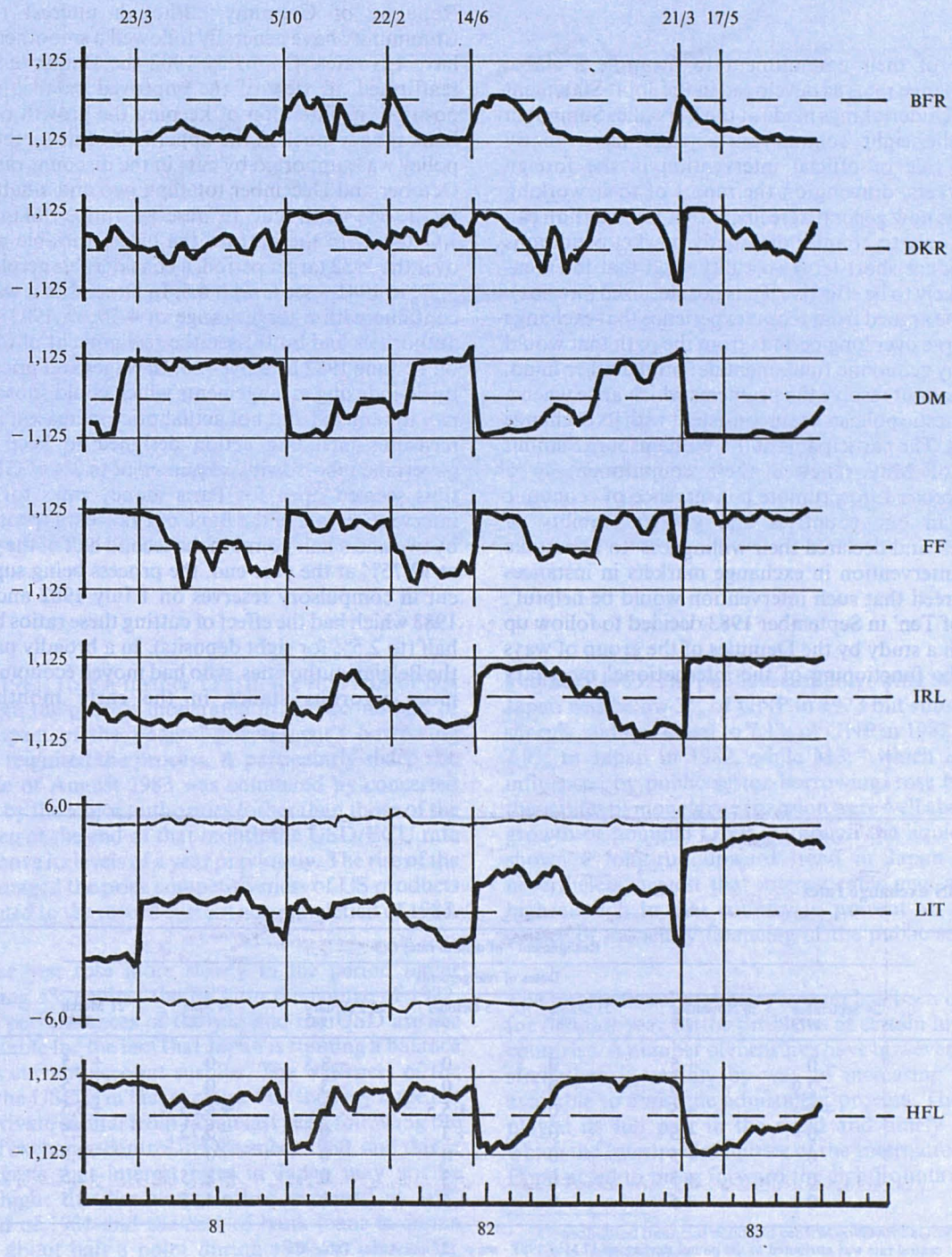
Table 6.1

Changes in EMS exchange rates

	Realignment [1] of central rates (%)							Cumulative change in central rates to 21.3.83
	Dates of realignments							
	24 September 1979	30 November 1979	23 March 1981	5 October 1981	22 February 1982	14 June 1982	21 March 1983	
BFR/LFR	0	+5	0	0	−8,5	0	+1,5	−11,06
DKR	−2,9	0	0	0	−3	0	+2,5	−11,91
DM	+2	+5	0	+5,5	0	+4,25	+5,5	+13,34
FF	0	+5	0	−3	0	−5,75	−2,5	−14,64
IRL	0	+5	0	0	0	0	−3,5	−7,59
LIT	0	+5	−6	−3	0	−2,75	−2,5	−17,21
HFL	0	+5	0	+5,5	0	+4,25	+3,5	+9,01

[1] A new notional central rate was attributed to the pound sterling on 17 May 1983 - see p. 121 and Annex Table 42.

GRAPH 6.2: **Bilateral spreads in the EMS**



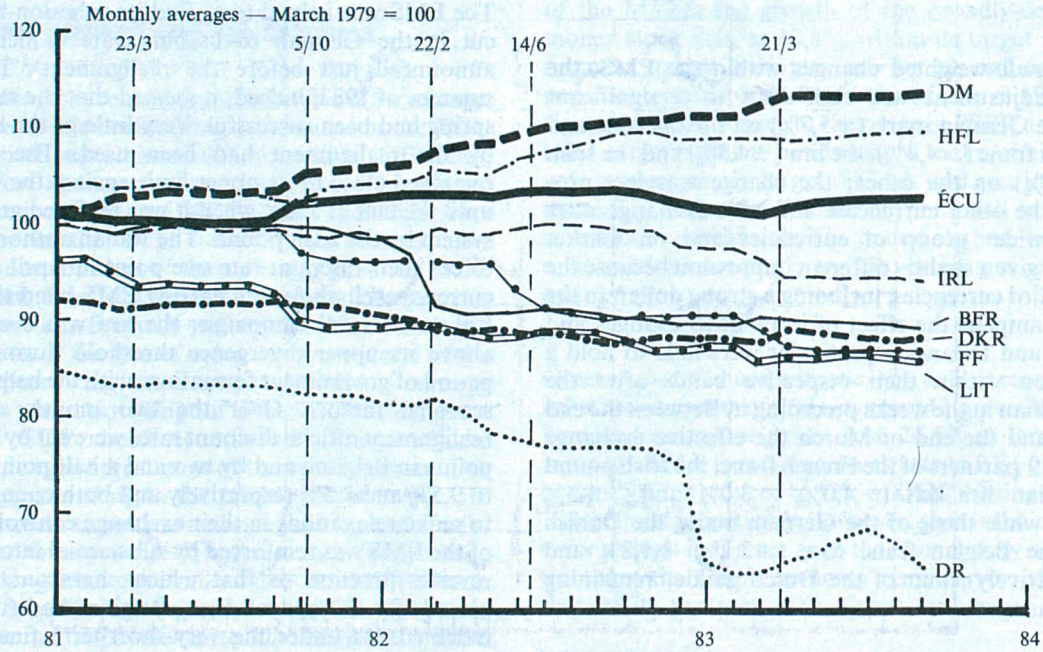
progressively reduced their discount rate from 14% at the beginning of July to 11,5% on 13 November.

The Italian authorities signalled, by a one point cut in their discount rate in late August, a willingness to see a fall in interest rates but the public finances deteriorated in the second half of 1982 and prevented such an outcome. In order to regain control over bank liquidity— which had been boosted by treasury operations—and in response to events in the foreign exchange market, the Banca d'Italia had to push up market interest rates in November and eventually raised marginal reserve requirements on the banks from 20 to 25% at the year end. The Government experienced increasing difficulty in placing Treasury bills throughout the autumn and took credit from the Banca d'Italia in an amount which eventually required special approval from parliament. In the outcome total domestic credit grew by 20,8% in 1982 (and thus considerably faster than GDP), whereas the target had been for 15,5%; the over-run was entirely due to credit taken by the State sector which amounted to LIT 67 900 000 million instead of a planned LIT 43 000 000 million. The target for total domestic credit in 1983 is 18,2% and thus rather less ambitious than that set for 1982. Until the middle of October 1982 the Italian authorities were able to keep their currency above the narrow band which constrains other EMS currencies; over the next six weeks severe pressures in the foreign exchange market were countered by substantial intervention—the official reserves fell by LIT 4 500 000 million in two months—but the lira nevertheless fell temporarily to the middle of the system, subsequently rising above the narrow band towards the end of the year.

6.3 The realignment of 21 March 1983 and its aftermath

In the early weeks of 1983 the Belgian franc and the Irish pound remained under pressure close to the bottom of the system. The Belgian authorities, indeed, had recourse in February to the very-short-term financing facility for the third successive month; the relative success of their strategy was, however, shown by the discount of their currency on the non-regulated market, which opened briefly to 7% in the middle of January, but was quickly reduced to 3,5%. The Irish pound was stronger after the introduction of a budget on 9 February which aimed to reduce the Exchequer deficit by about three points to some 12,5% of GDP and implied a reduction of the public sector borrowing requirement to 17% of GDP. The accompanying sharp fall in private consumption and investment led the authorities to reduce the credit

GRAPH 6.3: **Movement of EMS currencies and the drachma against the EMS** [1]



[1] ECU without sterling component.

expansion target—for bank lending to persons and corporations—from 14% in 1982 to 11% in 1983.

These were in fact the weeks in which it became clear that conditions across the Atlantic would not permit a further reduction of interest rates generally, although the Deutsche Bundesbank showed its flexibility by raising rediscount quotas at the beginning of February and the Dutch authorities also acted to ease strains in the EMS by a half point discount rate cut at the beginning of March. Pressure nevertheless built up relentlessly on the French franc, reflecting both the need to finance a substantial current account deficit (USD 4 000 million in the first quarter) and private capital flows. The French authorities made intra-marginal interventions, in both US dollars and EMS currencies, which became heavy in February. Their strategy was to keep their currency glued to the DM, and in this they were successful until the beginning of March, reinforcing their action in that month by a renewed squeeze on the Euro-FF market, where rates for short-term money rose to 300% per annum at one point. After the federal German elections of 6 March, however, the strains within the EMS became more severe. The French franc and the Italian lira had fallen substantially—the latter passing below the narrow EMS band—while the Belgo-Luxembourg authorities protected their position by a tightening of exchange control and a two and a half point rise in the Belgian discount rate. Finally, at the completion of the municipal election process in France, the Council Presidency called a meeting to consider the situation in the foreign exchange markets and this led to the ECU-parity changes announced on Monday 21 March (see Table 6.1).

In terms of trade-weighted changes within the EMS, the central rate adjustment was equivalent to a significant change for the German mark (+5,7%) on the one side and for the French franc (−4,4%), the lira (−4,3%) and the Irish pound (−5,0%) on the other; the change was less pronounced for the other currencies. Effective exchange rates based on a wider group of currencies and on market developments give a slightly different impression because the inclusion of third currencies, including a strong dollar, in the comparison dampens the effect of intra-EMS changes and because Italy and Ireland in particular were able to hold a higher position within their respective bands after the realignments than in the weeks preceding it. Between the end of February and the end of March the effective exchange rates against 19 partners of the French franc, the Irish pound and the Italian lira fell (−4,0%, −3,0% and −1,3% respectively), while those of the German mark, the Danish krone and the Belgian franc rose (+2,2%, +1,8% and +1,3% respectively), that of the Dutch guilder remaining virtually unchanged.

The origins of the weakness of the French franc are complex: France's large external trade deficit (USD 14 200 million in 1982) is partly due to the strong growth of domestic demand while major partners have fallen into recession; but it is also partly attributable to the continuance of high rates of inflation in France. The pressures on the franc came not only from the current account but also from private capital outflows, and these in turn were related to very rapid domestic credit expansion in 1982, supported to a significant degree by external borrowing undertaken by the banking sector. On March 25, the French Government introduced a comprehensive set of measures designed to correct the situation and make a success of the realignment. With the declared intention of halving the external trade deficit by the end of 1983 and eliminating it by the end of 1984, and in order to respect a target for the budget deficit equal to 3% of GDP, extended to both years, internal demand was cut by an amount equal to 2% of GDP, principally by tax and public expenditure changes. In line with a more modest expectation of GDP growth, the money supply target for 1983 was reduced by one point to 9%. In comparison with both the target (12,5-13,5%) and the outcome (11,5%) in 1982 this represents a considerably stricter stance, the more so since the improvement in the balance of payments will put upward pressure on the money supply, so that the deceleration of domestic credit will be even more notable than that of the money supply. The authorities have in fact reduced the indices limiting the growth of credit substantially below those applied in 1982. The French Government's measures were completed by a request for a Community loan of 4 000 million ECU for balance of payments financing, which was agreed to by the Council of Ministers on 16 May.

The EMS was helped to re-find its cohesion by a one-point cut in the German re-discount rate (which was in fact announced just before the realignment). In the middle summer of 1983, indeed, it seemed that the measures of the spring had been successful. Very little of the leeway opened by the realignment had been used. The French franc remained close to its upper limit against the German mark until the end of June, when it was replaced at the top of the system by the Irish pound. The Italian authorities were able to cut their discount rate one point in April and kept their currency well above the narrow EMS band throughout the Italian electoral campaign; the lira was even held briefly above its upper divergence threshold during the difficult period of government formation, with the help of favourable seasonal factors. Over the two months following the realignment official discount rates were cut by four and a half points in Belgium and by two and a half points in Denmark to 9,5% and 7,5% respectively and both countries were able to make relaxations in their exchange controls. The solidity of the EMS was reinforced by substantial intervention in the reverse direction to that which characterized the earlier period. By the end of June, Belgium had fully cleared its indebtedness under the very-short-term financing facility, while being able to cut its discount rate by a further half point, and both Italy and France were purchasing foreign

exchange on a large scale. The reversal of the flow of speculative funds was, indeed, so strong that the Netherlands had to raise its discount rate by one point early in May and by a further half point, to 5%, in September 1983. The Italian authorities felt sufficiently sure of their position to introduce a certain liberalization of their regulatory system by allowing their formal credit ceiling arrangements to lapse at the beginning of July 1983. As the summer progressed, however, it was by no means clear that the general relaxation would continue. Money market interest rates began to creep upwards in Frankfurt in May and the Deutsche Bundesbank had to assess the implications of the growth of its target variable; on the basis of quarterly averages this grew at an annual rate of 10,6% in the first quarter, partly for non-recurring reasons, and even in the second quarter the annualized rate was 8,6%. The first rise in official German rates since February 1981 came into effect on 9 September 1983 with a rise of half a point in the Lombard rate.

In the realignment of 21 March the notional ECU central rate of the UK pound was reduced by 11,02% on the basis of the preceding market exchange rate of that currency. On 17 May 1983 a new notional central rate based on market exchange rates of 13 May was attributed to the UK pound, 7,3% higher than that attributed on 21 March, and new ECU central rates for all EMS currencies were derived. The bilateral central rates and the upper and lower intervention limits between the currencies participating in the EMS exchange rate mechanism remained unchanged.

6.4 The pound sterling and the drachma

The pound sterling has remained outside the EMS exchange rate mechanism, while constituting an element in the ECU basket; as has been seen, this has raised practical difficulties, particularly for agro-monetary decisions. The Greek drachma is represented neither in the exchange rate mechanism nor in the ECU basket. Two themes have dominated the development of the monetary situation in the United Kingdom. First, at the centre of official concern has been the medium-term financial strategy (MTFS), based on a gradual reduction of the rate of monetary growth and of the public sector borrowing requirement (PSBR: a concept which includes the borrowing of State industries) as a percentage of GDP; but, secondly, the markets have produced a prolonged adjustment of the exchange rate. For most of 1982 bank lending to the private sector in the UK was expanding at an unprecedented rate, but the authorities did not counter this by a rise in interest rates; they chose instead to sell long-term government debt to the non-bank private sector in sufficient quantity to enable the public sector to make net repayments to the banking system. Technical measures were also taken to facilitate bond issues by private companies.

The authorities were able to conduct these operations while encouraging a fall of four points in market interest rates over the first 10 months of 1982 (to 10,5% for bank loans to first class borrowers). They also advanced yet further in the liberalization of their regulatory system by abolishing controls on hire purchase finance on 27 July 1982. In November, however, pressure built up on sterling in the foreign exchange market, related to the dwindling of the UK current account surplus in the presence of continuing capital exports. The fall in the price of oil, reducing the relative weakness of other countries' current accounts, was also thought by some to be a factor. Interest rates were pushed up three-quarters of a point at the end of November and again, by the same amount, in January. By the end of March sterling had lost 14% in effective terms over five months and from some points of view this adjustment was welcome. A number of calculations show that the long rise of the pound sterling after 1976 and domestic inflation had left UK industry in 1981 with a severe cost disadvantage, but the exchange rate adjustment of September 1981 and 1982/83 has, alongside the substantial drop in inflation [1] which has been a conspicuous achievement of recent UK policy, greatly reduced this problem—on the basis of GDP prices, the estimate of Commission staff is that UK price competitiveness in 1983 is ten points worse than that of 1970.

The UK Government achieved its financial objectives in 1981-82: the PSBR was a little below target at UKL 9 000 million (3,3% of GDP), albeit somewhat bunched in the early months of 1983, and, for the first time since the introduction of the MTFS, the growth of the broadly-defined sterling money stock was, at 10,8%, within its target range. All the financial target variables are to be reduced slightly in nominal terms in 1983-84. In the middle of 1983 there were signs that a persistence of the bulge in PSBR and a fall-off in sales of government bonds would make attainment of the new money supply target difficult and put in question the durability of the one-and-a-half point fall in interest rates which started in March. The pound sterling, however, made a substantial recovery on the exchanges in the second quarter.

Greece has continued with the long task of recovery from the inflationary burst of 1981, when M3 grew 34,7% over the year and consumer prices rose 24,5% in terms of annual averages. M3 is forecast to decelerate to 23% growth in 1983 as the PSBR is reduced to 12% of GDP, having been 15,2% in 1981. The implication is, however, that inflation will still be twice as high in Greece as in the Community as a whole and thus that the Greek economy remains very different from that of its partners. The Greek authorities succeeded in

[1] In terms of changes over 12 months, UK consumer price inflation was 21,9% in May 1980 and 4,2% in July 1983.

keeping the ECU value of their currency stable for the greater part of last year, but became increasingly preoccupied with their balance of payments position: while the current account benefited from increased net transfers from the Community and an officially arranged de-stocking of oil, the balances of both non-oil trade and tourism deteriorated while the support from private capital flows diminished. On 9 January 1983 the Greek authorities decided unilaterally to devalue the drachma by 15,5% against all currencies. For some months official policy was to maintain the newly established drachma/USD rate and this entailed a rise of the drachma against other currencies and notably the ECU. By the beginning of August it was recognized that the consequent rise of the drachma effective exchange rate had been excessive and it was announced that the link with the dollar would be weakened. The drachma/ECU rate has since come back to the levels recorded immediately after the devaluation.

6.5 Assessment—the development of the EMS

The EMS has now undergone seven realignments of central rates in its history of rather more than four years, which has coincided with an epoque of extreme exchange rate instability in the wider system. By the end of June 1983 the market rates of both the French franc and the Italian lira had fallen 23% from their initial DM central rates of 13 March 1979; this may be compared with the experience of the previous four and a quarter years, that is from the end of 1974 to 13 March 1979, during which the French franc fell 20% but the Italian lira had fallen 41% against the DM. Thus even on the basis of long-term nominal exchange rates before and after the introduction of the EMS there has been a certain gain in stability, at least as far as the Italian lira is concerned. A fairer comparison would, however, be with the behaviour of non-EMS currencies over the recent turbulent period. To take just one conspicous example, the exchange rate between the US dollar and the pound sterling changed by 34% over the four years to the end of October 1980 but then underwent an even larger change, in the reverse direction, over the next 33 months, i.e. to the end of July 1983. In contrast to developments in the wider system, nominal changes within EMS have been more modest, and consistent in their direction.

Developments in real exchange rates are perhaps rather more illuminating (see Table 6.2, based on GDP prices). By 1978 the pre-EMS arrangements had permitted large discrepancies to emerge between members of the new system: Italy's nominal exchange rate had more than compensated for its inflation differential and its real exchange rate had fallen a long way, exacerbating its inflationary problem and adding to the resource cost of balancing its external account, while Denmark, the FR of Germany and the Netherlands tended to be pushed into an uncompetitive position. Since 1978, however, exchange rate relationships within the EMS have ceased to over-compensate for inflation differentials. In the cases of Ireland and Italy, in particular, the real exchange rate rose to a level which, while no means unsustainable, corrected earlier distortions and gave a clear warning of the problems posed by inflationary developments in those countries. Thus, although convergence of inflation rates has still not been achieved (12-month consumer-price inflation rates varied from 15,2% in Italy to 2,5% in Germany in July 1983), the EMS has not fully accommodated this, and has exerted a systematic, although not extreme, pressure for greater price stability. Conversely, the lower-inflation countries have not been subjected to upward distortions of their (intra-EMS) real exchange rates, although the figures for the Netherlands are difficult to evaluate because of the impact of that country's energy exports.

The EMS has, however, worked less rapidly to produce monetary stability than it might have done because some participating countries have had recourse to large external official and quasi-official market borrowing to deal with balance of payments problems and thus avoided or delayed recourse to the conditional facilities associated with the system. Attention has been given at Community level to the growing recourse among member countries to external public sector market borrowing to an extent greater than would have been necessary to finance transitory current account deficits; such borrowing seems in fact in some cases to have financed private capital outflows which should have been a signal for policy adjustments. Meanwhile the arrangements for short-term monetary support and medium-term financial assistance have never been used in the history of the EMS and the Community loan facility for balance of payments purposes had not featured in the EMS context until the French request of May 1983.

In addition to market borrowing, some member countries have also sought in certain periods to alleviate their position by tightening exchange controls on intra-Community flows; a conspicuous example was the restriction introduced after the realignment of 21 March 1983 on French residents' tourist expenditure outside the franc zone. It must also be noted that no progress has been made in reducing the wider fluctuation margin enjoyed by the Italian lira. Thus a number of factors have retarded or prevented recourse to the conditional finance which might have led to earlier convergence of inflation rates; they may also have impeded the development of consultation and policy coordination which might have permitted an earlier reaction to policies which were insufficiently convergent.

These factors have not in the end prevented the EMS from being effective, and their identification may enable certain lessons to be learned. It remains, however, a substantial defect of the exchange rate mechanism of EMS that it

Table 6.2

Real effective exchange rate [1] based on GDP prices

(annua averages, 1970 = 100)

	1975	1976	1977	1978	1979	1980	1981	1982	1983 [2]
				Against EMS partners only					
B	101,8	104,0	108,5	107,7	104,9	100,8	97,8	88,0	87,0
DK	108,9	112,5	111,3	111,0	108,7	101,5	104,5	101,4	101,6
D	103,3	105,7	107,8	109,3	107,8	102,0	98,4	100,4	101,3
F	100,0	99,3	93,6	94,0	96,1	99,3	101,1	97,0	93,3
IRL	86,3	84,4	82,9	84,8	88,9	93,4	101,0	108,2	107,7
I	83,1	76,0	77,0	76,1	78,7	85,9	89,6	92,3	98,1
NL	114,3	119,7	123,7	123,5	120,5	117,9	115,9	120,1	116,8
				Against 19 partners					
GR	88,1	89,3	90,4	86,6	90,5	83,9	83,7	89,7	83,4
UK	93,7	84,7	85,0	87,9	100,1	120,9	125,5	119,9	110,2
USA	72,1	73,3	71,5	65,1	63,1	62,2	71,7	78,8	84,4

[1] Calculated using double export weights, variable from year to year until 1980.
[2] Forecasts by Commission services.
Note: The EMS started on 13 March 1979.

excludes the pound sterling. Quite apart from the technical difficulties which this has produced for the management of the system, the participation of the pound sterling would greatly increase the value of the system as a central reference point in the development of Community economic policy and as an expression of the monetary identity of Europe in its relations with the rest of the world. The recent substantial improvement in the UK's price and cost competitiveness suggests that it may now be time to reconsider the question of the relation of the pound sterling to the EMS exchange rate mechanism.

6.6 Assessment—the stance of monetary policy

In 1982 the broadly defined Community money stock resumed the deceleration which had characterized it over the period 1978-80 (in terms of annual averages—see Table 6.4) and its rate of growth is expected to fall again in 1983. The performance of individual countries varied—in the UK the deceleration did not begin until 1982, whereas in Germany monetary growth was allowed to accelerate again from the middle of 1982; the rate of monetary growth remains dangerously high in Italy and Greece—but in broad terms the contrast with the early 1970s is evident and reveals in the period 1978-82 a fairly cautious approach to monetary policy which has had its reward in the slowdown of inflation in some countries.

The assessment of the present stance of monetary policy is more difficult. It is, however, helpful to review the money supply data in the light of a number of supplementary indicators, and one of these is the liquidity of economy (the ratio of money to nominal GDP, which can also be understood as the inverse of the velocity of circulation—see Table 6.5 (a)). The reasons for expecting a stable relationship between money and nominal GDP are not entirely clear-cut. First, money is held not only to conduct the transactions which underlie GDP, but also, particularly in the EC, although to an extent which varies between member countries, as a savings medium. The search for a 'transactions balances' definition of money, which has been made difficult in the USA by recent institutional changes, has always been in vain on this side of the Atlantic. Secondly, nominal GDP (final output) does not coincide with the total of transactions in an economy, which includes intermediate output and financial transactions. Nevertheless, in a long-term perspective and over two decades the growth of the broadly defined money stock was very similar in the Community as a whole to the growth of nominal GDP, showing a slight tendency to rise in Germany, France and Italy, and to fall in the UK in line with the development of alternative savings media.

Over the last three years, however, liquidity has increased significantly in the Community. In the absence of fully tested models a considerable element of judgment is involved in assessing this development. The demand for money has

probably risen as economic agents seek to build up precautionary balances in response both to the recession and to the difficulty of making long-term investment decisions in a period of rapidly changing inflation rates: but it is also possible to argue that the available evidence points to a disequilibrium situation in which there is now a certain overhang of liquidity which could lead to additional spending over the coming year. It is even possible that such a development will be reinforced by a reversal of precautionary saving as the recovery gathers pace. The built-up of liquidity appears recently to have been even more rapid in the USA than in Europe.

This situation represents the working out of a medium term policy based on quantitative targets: such targets represent nominal quantities and as inflation falls they place less of a constraint on the economy and open up possibilities of growth. This can also be shown by a calculation of the growth of the 'real money supply', or money deflated by GDP prices—see part(b) of Table 6.5. Real money growth has been positive and significant in the Community for three years, but not as large as the average result over two decades; to some extent this corresponds to a more modest growth of potential output, but it also reflects a cautious attitude, particularly where inflation remains a serious problem. It is

GRAPH 6.4: **Divergence indicator**

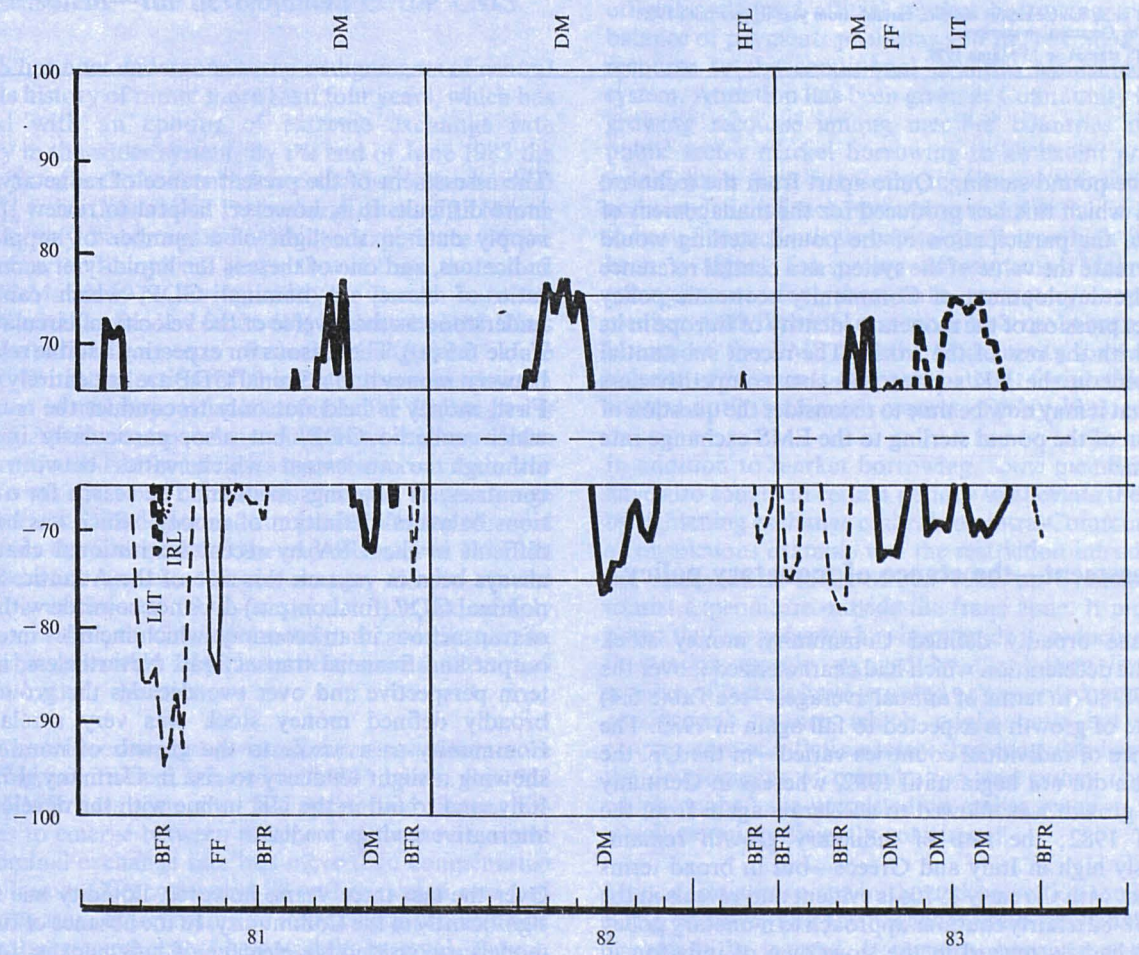


Table 6.3

Intermediate objectives and outturns

Country	Key variable [3]	1981		1982		1983		
		Objective	Outturn	Objective	Outturn	Objective	Outturn over 12 months to:	
D	MZ	4-7	3,5	4-7	6,0	4-7	7,9	August
GR [1]	PSCE	19,3	25,6	23,0	24,0	23,0	19,5	July
F	M2	10,0	11,4	12,5-13,5	11,5	9,0 [2]	9,4	June
IRL	PSCE	15,0 [3]	15,6	14,0 [3]	10,4	11,0	13,5	August
I	TDCE	16,0	18,2	15,5	20,8	18,2	20,7	June
UK [4]	LM3	6-10	13,8	8-12	10,8	7-11	11,0	August

1 The Greek monetary authorities also fix a target for the rate of growth of the note circulation.
2 Change between Nov. / Dec. 1982 / Jan. 1983 and Nov. / Dec. 1983 / Jan. 1984.
3 Financial year February to February.
4 At an annual rate for the period from February of the current year to April of the following year. Targets have also been fixed for M1 and PSL2 (private sector liquidity).

Note: TDCE: total credit expansion of domestic origin; MZ: central bank money; PSCE: domestic credit extended to the private sector; LM3: sterling M3. For further details, see technical annex.

Source: Central banks.

entirely appropriate that planned real monetary growth should be low or negative in France and Italy, where progress in the struggle against inflation has been slow, and one may, indeed, ask whether the monetary growth in prospect for Greece is appropriate in view of the inflationary problems of that country.

Two other supplementary indicators of the stance of monetary policy are interest rates and exchange rates. While nominal interest rates in themselves are not without a certain direct effect on the profitability of firms, real interest rates generally give a better indication of the impact of monetary policy. The calculation of real interest rates depends on the

Table 6.4

Growth of money stock

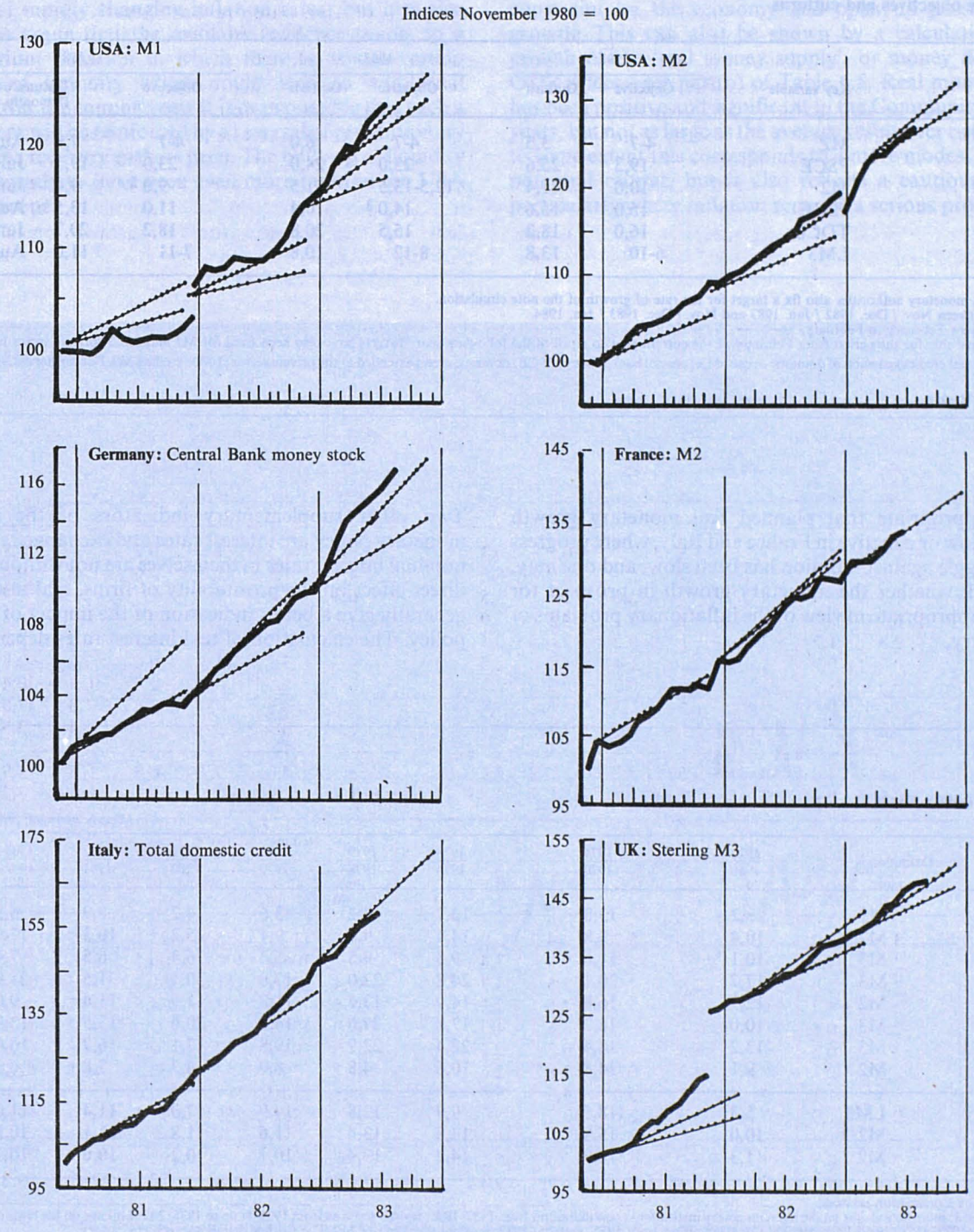
(Yearly averages, annual % change)

Country	Definition [2]	1970/1960	1974/1970	1978/1974	1979/1978	1980/1979	1981/1980	1982/1981	1983/1982 [1]	1984/1983 [1]
B	M2	8,2	13,8	12,7	8,2	3,6	4,7	8,9	6,5	6,0
DK	M2	10,4	9,8	14,4	9,8	9,4	5,2	10,3	17,0	9,5
D	M3	10,1	11,6	9,3	9,5	5,3	6,3	6,5	7,4	5,7
GR	M3	17,7	20,1	24,8	22,0	17,0	30,4	31,5	21,9	22,9
F	M2	12,7	16,8	14,9	13,5	11,8	11,9	11,4	9,0	7,9
IRL	M3	10,0	16,3	17,8	29,0	14,5	20,6	13,5	13,9	14,4
I	M3	13,2	18,4	22,4	22,9	19,8	17,1	16,7	16,6	12,8
NL	M2	9,1	14,8	10,6	4,8	8,0	4,3	7,8	6,3	5,6
UK	LM3	5,3	18,5	9,9	12,8	14,9	17,0	11,4	11,0	9,5
EC 10 [3]	M2/3	10,0	15,8	13,5	13,4	11,6	11,8	11,1	10,5	8,7
EMS [3]	M2/3	11,3	14,9	14,2	13,4	10,7	10,2	10,6	10,1	8,1

1 Forecasts by Commission services.
2 B: up to 1964: monetary claims on the main monetary institutions; new definition from 1982. IRL: revised series as from 1971. I: up to 1975: M2. Linkage on the basis of growth rates. NL: 1976, 1977, 1978: break in series. DK: new definition from 1975. F: from 1982, resident's holding of M2. For further details see technical annex.
3 Rate of growth of the geometric average, weighted by GDP at current prices and purchasing power parities, of the money stock indices of the countries concerned (1975 = 100). The weight of Luxembourg has been added to the weight of Belgium.

Source: Up to 1982, central banks.

GRAPH 6.5: **Monetary targets and outcomes, 1981-83** [1]



[1] The USA also has targets for M3 and credit; the UK also has targets for M1 and private sector liquidity.

expected rate of inflation and is likely to differ from one economic agent to another but a simple calculation (part(c) of Table 6.5) indicates that real long term interest rates are now high in the Community by historic standards. The results for the decade 1971-80 are influenced by prolonged periods of negative real interest rates in some countries which corresponded to periods of excessively slack monetary policy, but real interest rates are now in general well above their levels of the 1960s, which would appear to indicate that monetary policy is now rather tight for a recessionary phase. On the other hand the evidence of nominal effective exchange rates (Table 6.5 part (d)) might seem to point in the opposite direction. The medium-term divergence of currencies within the Community has already been noted, but the effective exchange rate of the Community as a whole has been falling for several years and is now well below its level of 1970. In fact the signals given by real interest rates and by the nominal effective exchange rate are both greatly influenced in the third quarter of 1983 by the deficit of the US Federal Government which is forcing up real interest rates in New York and thus putting pressure on the foreign exchange market. The resulting interest rate/exchange rate combination in Europe cannot be interpreted as directly revealing the objectives of Community monetary authorities, but rather as representing the best compromise which the situation permits, albeit one which on balance dims somewhat the prospect for real growth opened up by quantitative monetary policy.

Table 6.5

Subordinate indicators of the stance of monetary policy

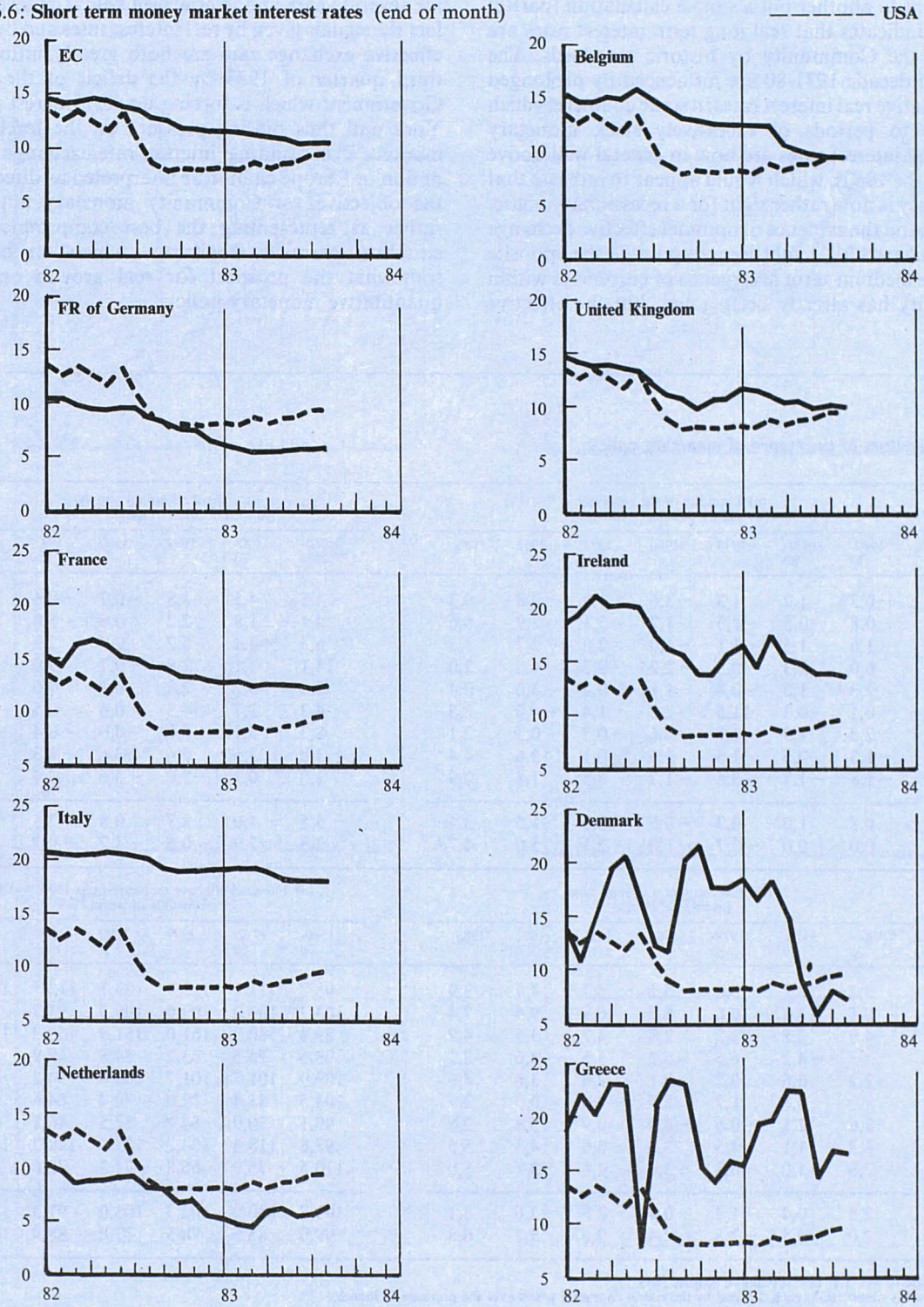
	(a) Liquidity of the economy (M: GDP) *(annual % changes)*							(b) Real money supply (M: GDP prices) *(annual % changes)*						
	1960-70	1970-80	1979	1980	1981	1982	1983	1960-70	1970-80	1979	1980	1981	1982	1983
B	−0,3	1,2	1,3	−3,6	1,2	0,8	0,3	4,5	4,5	3,8	−0,7	−0,6	1,8	−0,6
DK	−0,8	−0,5	−1,5	1,7	−5,1	−2,9	6,6	4,1	1,8	2,2	0,6	−5,0	0,4	8,9
D	1,6	1,5	1,1	−1,0	2,0	2,7	3,5	6,3	4,4	5,2	0,9	2,2	1,7	4,2
GR	6,0	2,3	−0,8	−2,2	9,7	4,8	2,0	14,1	7,1	2,8	−0,7	9,0	4,8	1,8
F	2,3	1,5	−0,4	−1,1	−0,2	−3,0	−0,4	8,0	5,2	2,8	0,2	0,0	−1,2	−0,7
IRL	0,1	−0,3	11,5	−2,2	1,4	−4,0	2,5	4,3	3,7	14,3	0,6	2,5	−2,8	3,0
I	2,5	1,9	1,1	−4,5	−0,2	−0,3	2,1	8,3	5,1	6,0	−0,8	−0,4	−0,4	0,2
NL	−1,3	0,5	−1,5	1,6	−0,1	3,6	4,4	3,8	3,5	0,6	2,6	−1,3	2,0	4,6
UK	−1,8	−1,7	−3,6	−1,7	6,5	1,8	2,9	1,0	0,1	−2,0	−3,6	4,4	3,3	5,8
EC	0,8	1,0	0,3	−0,5	3,0	1,5	3,4	5,5	4,0	3,7	0,8	2,5	1,9	4,0
USA	0,0	0,0	−2,7	−1,0	−2,1	5,0	4,7 [1]	3,8	2,9	−0,5	−1,2	−0,1	3,2	8,3 [1]

	(c) Real long-term interest rate (averages) % p.a. [2]							(d) Nominal effective exchange rates 1970 = 100, against rest of world [3]						
	1960-70	1970-80	1979	1980	1981	1982	1983	1960-70	1970-80	1979	1980	1981	1982	1983
B	3,2	1,2	5,0	5,2	5,7	4,4	3,9	98,7	111,1	122,9	123,1	116,7	105,8	103,7
DK	2,1	4,3	6,6	5,7	6,8	9,4	7,4	103,7	106,0	109,6	100,5	93,8	89,8	89,8
D	4,0	2,8	3,2	2,8	4,2	3,5	4,9	89,4	130,9	161,0	161,9	153,3	161,0	168,2
GR	:	−4,2	−6,5	−6,2	−5,5	−4,6	−2,1	98,5	75,5	63,2	54,8	49,9	46,2	38,2
F	2,2	0,6	0,2	0,1	2,6	3,6	4,6	109,9	101,7	101,7	103,0	94,2	86,5	81,0
IRL	:	−0,8	1,7	−2,5	−2,4	−0,3	2,7	104,5	81,4	72,0	70,4	64,6	63,9	61,8
I	2,6	−2,1	−0,6	−4,3	0,9	3,8	2,6	99,1	70,9	54,2	52,5	46,1	42,9	41,5
NL	1,3	1,1	4,5	3,5	5,0	4,3	5,5	98,8	118,3	134,2	135,0	128,2	135,0	138,2
UK	2,8	−1,0	−0,3	−3,5	2,6	3,7	5,0	110,5	75,9	65,8	72,2	72,6	69,6	64,8
EC	2,8	0,4	1,2	−0,4	2,8	3,6	5,1	101,8	100,9	102,3	103,0	97,3	89,4	85,2
USA	2,0	−0,5	−2,3	−2,4	2,3	5,7	6,8	99,0	85,5	78,5	77,8	88,9	99,8	107,9

1 Based on increase of M2 over nine months to August 1983.
2 Average of monthly observations each deflated by the rise in consumer prices over the previous 12 months.
3 Calculated using double export weights variable from year to year.

Note: Except as indicated, 1983 figures represent forecasts by Commission services; money definitions and aggregation method as for Table 6.4.

GRAPH 6.6: **Short term money market interest rates** (end of month)



Note: For definitions see notes to statistical annex, Table 38.

Monetary policy must also be evaluated in the light of the structure of the counterparts of the money stock (Table 6.6). There are at present substantial difficulties in the way of aggregating these figures at Community level, but the contrasts at the level of member countries are revealing. The data shows, first, the extent to which public sectors have dominated the money creation process. A useful rule of thumb might be to concentrate attention on those countries in which bank credit to the public sector is greater than bank credit to the private sector (parts 6 and 7 of Table 6.6). In 1983 this is particularly true of Belgium, Italy and Ireland; in Greece a certain balance has been restored (regrettably in the context of high inflation), and in Denmark a remarkable adjustment appears to be occurring. The tables also reveal the differing roles of external counterparts. While special considerations may apply in particular cases, there must be a *prima facie* assumption that a persistent, significant negative figure under this heading indicates that the extension of bank credit has gone beyond the willingness of residents to acquire claims on the domestic banking system at existing interest rates and that domestic monetary conditions are therefore ill-adapted to the needs of the domestic economy. The improving position of Belgium and Denmark is reflected in a progressive reduction of their external counterparts. Greece is a special case in that its negative figure partly reflects a traditional form of capital inflow. The UK position largely reflects the problem of managing the transition to complete freedom of capital movements. The programmes of the French authorities implicitly recognize the need to eliminate the negative external counterpart and they intend to effect a major adjustment by reducing the expansion of bank credit. Success in achieving this adjustment will be an indispensable sign that their policies to correct their balance of payments and defeat inflation are working.

Table 6.6

Counterparts of money creation [1]

(as % of money stock at the end of the preceding period)

Country	1 Money creation = rate of growth of M2/3 (1 = 2 + 3 + 4)			2 Domestic money creation (2 = 5 = 6 + 7 − 8)			3 External creation (+) and destruction (−) of liquidity			4 Other		
	1982	1983	1984	1982	1983	1984	1982	1983	1984	1982	1983	1984
B	5,7	5,0	6,7	16,2	13,8	12,0	−9,8	−7,9	−4,8	−0,7	−0,9	−0,5
DK	11,7	12,5	7,5	25,3	18,3	9,9	−13,6	−5,8	−2,4	−0,0	0,0	0,0
D	7,1	7,5	5,5	7,2	6,7	6,2	0,4	−0,2	0,4	−0,5	1,0	−1,1
GR	29,1	22,6	20,2	33,8	24,8	23,3	−4,7	−2,2	−3,1	0,0	0,0	0,0
F	10,8	8,8	6,5	14,1	10,6	7,5	−3,6	−1,8	−1,0	0,3	0,0	0,0
IRL	13,0	14,4	14,4	14,8	11,8	12,2	−1,8	2,6	2,2	0,0	0,0	0,0
I	17,2	16,0	11,0	20,6	17,7	15,2	−0,6	1,1	0,0	−2,8	−2,8	−4,2
NL	7,6	5,5	6,0	5,5	4,8	4,5	2,8	3,2	3,6	−0,7	−2,5	−2,1
UK	9,3	10,6	8,6	10,8	10,6	9,6	−2,3	−1,1	−1,9	0,8	1,1	0,9

	5 = 2 Domestic money creation (5 = 2 = 6 + 7 − 8)			6 Lending to the public sector			7 Lending to the private sector			8 Non-monetary liabilities		
	1982	1983	1984	1982	1983	1984	1982	1983	1984	1982	1983	1984
B	16,2	13,8	12,0	20,9	19,7	18,0	2,7	3,7	4,2	7,4	9,6	10,2
DK	25,3	18,3	9,9	18,1	13,2	6,2	10,6	6,9	5,6	3,4	1,8	1,9
D	7,2	6,7	6,2	4,9	4,3	2,5	8,5	9,8	11,0	6,2	7,4	7,3
GR	33,8	24,8	23,3	20,3	14,6	13,6	17,6	13,5	12,3	4,1	3,3	2,6
F	14,1	10,6	7,5	2,2	3,4	3,3	16,0	11,4	9,2	4,1	4,2	5,0
IRL	14,8	11,8	12,2	8,2	9,9	10,2	6,4	3,8	3,9	−0,2	1,9	1,9
I	20,6	17,7	15,2	16,8	18,2	15,9	8,1	8,0	9,4	4,3	8,5	10,1
NL	5,5	4,8	4,5	4,0	5,1	5,6	5,1	5,6	5,6	3,6	5,9	6,7
UK	10,8	10,6	9,6	−6,1	0,0	0,5	20,3	14,3	12,4	3,4	3,7	3,3

[1] Money stock broadly defined (same definition as Table 6.4 except that the change of definition in Belgium in 1982 does not apply). The figures for the counterparts are generally difficult to compare between one country and another.

Source: 1982: Central banks; 1983-84: Forecasts by Commission services.

In section 6.5 on the EMS it was noted how recent policy developments in particular countries favour convergence within the Community on a low rate of inflation. This conclusion can now be extended by noting that at the level of the Community as a whole quantitative monetary policy seems to be consistent with non-inflationary recovery from the recession. This situation is emerging because certain countries, notably the United Kingdom and the Federal Republic of Germany, have persisted in the pursuit of moderate quantitative monetary targets which have held back inflation and now in consequence open up some room for recovery. A similar degree of success has been achieved by the Netherlands. The recovery will however be impeded by the persistence of high real interest rates having their origin on the other side of the Atlantic. The monetary authorities of the UK and Germany are faced, in the third quarter of 1983, with signs of overshooting of their monetary targets. It would be consistent with past policy declarations in both countries if reactions to the present situation were designed not with a view to eliminating month-to-month variations but with a view to securing a steady and reasonable growth of the aggregate over the medium term while avoiding, for example, the kind of sustained departure from target seen in Germany in 1978. The adjustment programmes of Belgium, Denmark and France have begun to bear fruit but do not yet allow of any relaxation. In Greece, Italy and, to some extent, Ireland the persistence of inflation rates well above the Community average suggests that the struggle against inflation must be at the centre of policy, and that targets for aggregate credit expansion in 1984 should be set well below the rate of growth of nominal GDP in 1983, in parallel with a reduction of public sector borrowing requirements.

Sterilization of foreign exchange intervention in the EMS

1. The distinction between 'sterilized' and 'unsterilized' interventions has played an important role in the discussion of central bank interventions following the 1982 Versailles Summit. This note recalls, in a highly simplified manner, the theoretical issues and describes the current practice of EMS monetary authorities.

2. An intervention operation, i.e. a purchase or sale of foreign exchange by the central bank against the domestic currency, raises or reduces the monetary authorities' net foreign assets. Intervention is sterilized when the increase (decrease) in the net foreign assets is matched by a decrease (increase) in the monetary authorities' net domestic assets. In consequence, the liability side of the monetary authorities' balance sheet is not affected by a sterilized intervention operation. This implies that sterilized intervention has no impact on the monetary base, defined as currency in circulation plus deposits of the banking sector at the central bank.

3. A purely hypothetical example may serve to illustrate the definition. Suppose the central bank of an EMS country wants to purchase its own currency against DM on its foreign exchange market in an attempt to prevent it from depreciating to its bilateral fluctuation limit. Upon agreement of the Bundesbank to the desired intervention operation, the central bank obtains the required DM from the Bundesbank against transfer of a corresponding amount of US dollars taken from its reserves. It then buys the domestic currency from domestic commercial banks and pays for it from the newly acquired DM deposit at the Bundesbank. This produces an increase in German commercial bank reserve accounts at the Bundesbank as well as in their demand deposit liabilities to commercial banks of the weak currency country.

In turn, demand deposits held by commercial banks of the weak currency country at German commercial banks increase; and their reserve accounts at their central bank decline.

Since bank reserves have fallen in the weak currency country, the monetary base decreases as a result of this foreign exchange market operation. On the other hand, since German commercial banks' reserves have risen, the German monetary base increases.

If the central banks concerned do not want the foreign exchange intervention to affect their monetary base, they may sterilize its impact with an offsetting sale or purchase of domestic assets, injecting reserves into the commercial banking system in the case of the weak currency country and draining off newly created reserves in the case of the strong currency country.

4. From a technical point of view, the foreign exchange operation described above gives rise to unsterilized intervention in the first place since foreign exchange holdings and bank reserves are affected simultaneously. A subsequent action of monetary policy (e.g. an open market operation) is necessary to restore the latter to their original level. A sterilized intervention operation is thus made up of unsterilized intervention and a monetary policy operation that offsets the implied change in the monetary liabilities of the central bank. For analytical purposes, however, it is convenient to change perspective and view unsterilized intervention as a joint decision on sterlized intervention on the one hand, and on monetary policy on the other. In studies on the effects of intervention on exchange rates, it then becomes possible to separate the impact of sterilized intervention from that of monetary policy, and to analyse whether monetary authorities can operate simultaneously a monetary policy and an exchange rate policy.

5. Two conditions must be met to allow both an exchange rate target and a monetary aggregate target to be pursued independently.

First, the size of intervention operations must not exceed the central banks' ability to absorb the liquidity effect in their domestic markets, i.e. their capability to sterilize.

Secondly, for sterilized interventions to exert an impact on exchange rates, assets denominated in different currencies must be imperfectly substitutable. [1] If, in the example above, investors regard securities denominated in DM and in the weak EMS currency as perfectly equivalent, they will be indifferent as to which of the two they hold. The change in the relative size of net asset stocks denominated in the two currencies brought about by the intervention operation then will have no direct effect on the exchange rate. If, however, these securities are not perfect substitutes, investors will be unwilling to hold the new portfolio at the original exchange rate and/or interest rates. A change in one or all of these variables is required to incite investors to accept the new relative amounts outstanding. [2]

6. In monetary theory, the monetary base is sometimes regarded as an efficient instrument for the control of money supply [3] i.e. currency plus deposit assets held by the public. Intervention, that—in theory—is sterilized instantaneously, does not affect the monetary base nor in consequence the monetary conditions in the countries concerned. Its impact on exchange rate behaviour is therefore thought to be more pronounced in the short run than in the long run, since imperfect asset substitutability is likely to vanish in the long run. Investigations undertaken in the framework of the Report of the Working Group on Exchange Market Intervention [4] set up at the Versailles Summit confirm that sterilized intervention generally has been effective in influencing the exchange rate in the short run.

7. In practice, however, it is often felt that the link between the monetary base and money supply is less tight. Monetary

[1] Sterilized intervention may also affect the exchange rate by influencing expectations with respect to future monetary and exchange rate policies by the central bank. Strictly speaking, it is not independent of monetary policy in this case.

[2] It has been shown that imperfect substitutability is not a sufficient condition for sterilized interventions to affect exchange rates. For a survey of the theory and the literature, see *Solomon* (1983).

[3] See e.g. *Mussa* (1981), *Batten and Kamphoefner* (1982).

[4] *Jurgensen* (1983).

aggregates other than the monetary base may be affected by sterilized intervention, depending on the type and maturity of deposits preferred by the public, and the domestic interest rate structure may change accordingly. Therefore, the concept of sterilization as defined above is too narrow for the assessment of the monetary effects of interventions by EMS central banks which do not express their monetary targets in terms of the monetary base. For the remainder of the note, intervention effects will also be considered as sterilized if they do not hamper monetary management oriented at the achievement of quantitative intermediate monetary objectives.

8. The relationship of intervention to monetary policy in Germany is as follows:

The Bundesbank undertakes smoothing operations in the DM/US dollar market when exchange rate fluctuations are deemed excessively large or erratic. Within the EMS, it intervenes in partner currencies at the obligatory intervention points, and may also do so before the limit rates have been reached. Moreover, the function of the DM within the EMS to a certain extent is similar to that of the US dollar in the wider international monetary system, in that the DM is used as the preferred EMS currency for interventions by other EMS central banks within the fluctuation margins. [1]

As to monetary policy, the intermediate target variable adopted by the Bundesbank is a weighted monetary aggregate: the central bank money stock. It comprises currency in circulation and minimum reserve requirements on domestic liabilities, calculated at constant 1974 reserve ratios.

The Bundesbank conceives the way it exerts monetary control as a multi-stage procedure. [2] At the money market level, the Bundesbank accepts foreign exchange purchases as one means of providing liquidity to the banking sector, when this fits in with the evolution of other market influences and does not upset its short-term operational instruments (in particular money market interest rates). However, interventions are sterilized when they are likely to have a disruptive effect on domestic money market conditions. At the level of the intermediate target variable, the Bundesbank closely monitors the development of the central bank money stock. Short-term (one to three months) and possibly reversible deviations of the central bank money stock from the target path are not corrected by an immediate change of monetary policy. The Bundesbank neutralizes, however, the secondary effects of interventions as well as those of other determinants of money stock growth, if the achievement of the annual growth target is believed to be endangered.

The flexible use of EMS financing and intervention arrangements has, in many cases, facilitated the neutralization of unwarranted liquidity effects in Germany. [3] EMS central banks often were able to purchase DM sold either at the intervention points or intra-marginally after foreign exchange flows had reversed. Since the proceeds of such recouping operations mostly were deposited at the Bundesbank or used for the advance settlement of debtor balances under the EMS very-short-term financing facility, the preceding liquidity expansion tended to be offset.

9. In France, the quantitative target of monetary policy is expressed in terms of M2 money supply. The target aggregate is not, however, pursued through the influence of money market conditions on bank liquidity, but mainly through the regulation of credit ceilings. [4] The liquidity needs of commercial banks being determined by a number of automomous factors, *inter alia* changes in foreign reserves, and by reserve requirements, they are not directly related to credit expansion as the means of implementing the monetary policy objective.

Since commercial banks hold a large stock of highly liquid securities, they can usually even out intervention induced liquidity swings. From a quantitative point of view the scope for systematic non-sterilization is restricted in France. However, the French monetary authorities use discretionary changes in the money market intervention rate to enhance the effectiveness of interventions.

10. The order of monetary objectives in France—a monetary aggregate at the policy level and a credit target at the operational level—is reversed in Italy. The Italian target of monetary policy is total domestic credit expansion and the monetary base is the short-run operational target adopted by the Banca d'Italia.

At the setting of the credit expansion target, the Banca d'Italia makes a decision as to the extent to which the forecast foreign sector impact on base money creation should be sterilized. At the operational level, the Banca d'Italia is flexible in the pursuit of the monetary base target through operations in the Treasury bills market. Deviations from the target path may lead to adjustments of money market interest rates, and the sterilization of the impact on monetary base creation from the foreign channel is by no means automatic. [5]

11. Ireland's monetary policy target is formulated with respect to bank lending to the private sector. Deviations from the target are penalized through a system of supplementary deposits which licensed banks are obliged to hold at the central bank in case of excessive lending activity.

In its short-term management of liquidity, the Central Bank of Ireland smoothes irregular liquidity flows. [6] In general,

[1] On the intervention policy of the Bundesbank, see *Gleske* (1982 a), *Gleske* (1982 b), and *Scholl* (1982). On the role of the DM, see also *Baer* (1982).

[2] See *Dudler* (1982), *Schlesninger* (1982) and *Deutsche Bundesbank* (1982).

[3] More detail, also on the period of DM weakness in the EMS 1980/81, is given in *Scholl* (1981).

[4] See *Raymond* (1982).

[5] For an example, see *Banca d'Italia* (1983), pp. 232 and 233.

[6] See *Barry* (1983).

therefore, interventions in Ireland can be considered as sterilized, although on occasion, the Bank has allowed interest rates to reflect tension in the foreign exchange market.

12. Similarly as in Ireland, monetary policy in Denmark operates on bank lending to the private sector. It is guided through liquidity policy and by way of a target for credit expansion by banks.

Repercussions of exchange rate strains are allowed to feed through into domestic money markets. A system of borrowing and deposit limits, under which banks can smooth over liquidity swings, is used flexibly in response to the foreign exchange situation. Measures range from increases in the interest rate at which the central bank supplies additional liquidity to the banking system to the suspension altogether of the borrowing limits. [1] Non-sterilization is not automatic, bur rather more a consequence of a deliberate liquidity and interest rate policy pursued by Danmarks Nationalbank.

13. No quantitative money supply or credit objective guides the conduct of monetary policy in Belgium. Nevertheless, the tightening of domestic liquidity caused by the National Bank's interventions in the foreign exchange market is regularly counterbalanced to a great extent by the creation of base money. [2]

The policy constraint under which interventions are sterilized is the financing requirement of the Treasury which the central bank in its function as lender of last resort is obliged to fulfil. The need to replenish the supply of Treasury funds imposes limits on the Bank's ability to avoid offsetting liquidity shortages in the money market. To a certain extent, however, the Bank allows money market interest rates to reflect pressure on the exchange rate.

14. In the Netherlands, monetary policy aims at the control of the liquidity ratio, i.e. the money supply in relation to national income. A credit target—the domestic counterpart of money—is used for operational purposes, being the easiest to control in view of the openness of financial markets and the exchange rate constraints of the EMS.

Foreign exchange interventions in the Netherlands have a double function. [3] On the one hand, they are an instrument of monetary policy used for the regulation of the money market which is essentially an interbank market. On the other hand, they are effected for the purposes of an exchange rate target. In case of conflict, external factors dominate the evolution of the domestic money market as interventions are left unsterilized.

15. In the United Kingdom, which does not participate in the EMS exchange rate mechanism, the stated monetary objectives cover three different monetary aggregates, one narrow (M1) and two broad (sterling M3 and private sector liquidity broadly defined). [4] On the operational level, debt management is considered to have the 'most immediate and direct quantitative linkage' [5] with M3.

The quantity of base money in the UK serves neither a target nor an operational function. Foreign exchange interventions carried out through the Exchange Equalization Account are automatically sterilized by sales or purchases of Treasury bills to the banking system. [6]

16. The narrow theoretical concept of sterilization which is related to the monetary base is of no great significance for the practice of EMS monetary policies which are expressed and operated in a variety of other monetary variables. In the EMS context, it is therefore more appropriate to consider foreign exchange interventions as sterilized when they do not affect the conduct of monetary policy.

At the level of the money market, the effects of interventions on liquidity volumes are more or less automatically sterilized in all EMS countries (with the exception of the Netherlands and, in a way, Denmark), given various institutional factors and practices. But EMS central banks do have recourse—although to varying degrees—to money market interest rates as a policy instrument when strains on foreign exchange markets call for a reaction of monetary policy.

When drawing up monetary policy, EMS monetary authorities tend to take a view on the probable influence of their economics' external position on their policy objectives—however different these may be at both the policy and the operational level. Intermediate targets are generally set in the light of such considerations, and this implies a certain neutralization of the liquidity effects of anticipated changes in foreign reserve holdings.

When strains on foreign exchange markets occur, they generally are not allowed to cause substantial or longer-term deviations of intermediate objective variables from their target path, although persistent interventions to support a weak currency will usually be interpreted as requiring some tightening of domestic monetary management.

17. In conclusion, repercussions of intervention on monetary policy in EMS countries generally remain limited. Therefore, the situation in these countries is different from but not diametrically opposed to that in the US, where intervention is sterilized automatically and immediately and hence deemed independent of domestic monetary policy.

1 See *Danmarks Nationalbank* (1983).
2 See *National Bank of Belgium* (1983).
3 See *Timmerman* (1981).
4 See *Fforde* (1982).
5 *Coleby* (1982).
6 See *Bootle* (1983).

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Private use of the ECU

In last year's *Review*, the private ECU market was described, with a list of the transactions carried out and a summary of the ECU's status in the light of national rules. It is worthwhile returning to the subject this year in order to present further information on this fast-developing market. We begin by highlighting some of the significant aspects of the market's development, and go on to mention initiatives on the part of private operators and the Commission of the European Communities to facilitate the use of the ECU as a foreign currency. We then consider some of the features that make this new currency unit attractive.

The development of the market

The ECU market has now achieved a recognized place on the European monetary scene, as was expected in view of its activities during 1982. A few facts will illustrate its rapid development:

— *Public issues:* Twenty-eight public issues, totalling 1 545 million ECU, were launched on the Euro-market in the first nine months of 1983; this compares with 17 issues totalling 722 million ECU in the whole of 1982. The ECU is now the third-ranked issuing currency on the market, after the US dollar and the German mark, with a share of 4,5%. If all international issues are considered (Euro-issues and foreign issues launched on domestic markets), the ECU was the sixth most important currency in the first half of 1983, after the dollar, the mark, the Swiss franc, the yen and the guilder. Outstanding issues, amounting to 2 012 million ECU, break down as follows: 1981: 190 million ECU, five issues; 1982: 722 million ECU, 17 issues; 1983 (seven months): 1 100 million ECU, 19 issues.

— The Community institutions are increasingly resorting to the ECU; if the sum of 150 million ECU raised under arrangements for balance of payments support for the Member States is included, these institutions now rank second among issuers, with 627 million ECU in 10 operations, behind French operators, the leading issuers with 805 million ECU in 14 operations. Other major issuers are the Italians, the North Americans, the Swedes and two Japanese banks; the Council of Europe's Resttlement Fund has floated three issues.

— *Bank loans:* By the end of the first half of 1983, bank loans outstanding totalled over 1 000 million ECU in amounts ranging from 2 million ECU to 200 million ECU. Among the borrowers are important names such as Saint-Gobain, the Crédit National, Fiat, Air France, the Kingdom of Denmark, the Cassa per il Mezzogiorno and the IRI.

— *Short-term loans:* Importers and exporters in need of short-term foreign currency loans are showing a growing preference for ECU loans, which cost less, on balance, than loans in other currencies. This type of loan is particularly popular in Italy (where 1 628 million ECU had been borrowed by the end of 1982), but is also developing rapidly in other countries, and notably in France.

— *Commercial transactions:* By reason of its stability, the ECU is particularly suitable for denominating transactions and keeping accounts between firms and subsidiaries operating Europe-wide. Applications of the ECU in the commercial world are fairly recent, and not many details are available; but the field is interesting, for the ECU will graduate beyond the level of just another Euro-currency only if it is actually used by economic agents. Already, some European multinationals are tending to prefer the ECU to Community currencies and to the dollar for invoicing and even settling transactions with their subsidiaries; by so-doing they reduce their exchange risk and simplify their cash management.

New departures

— *The operators:* Much the most promising initiative by operators is the organization of a multilateral ECU clearing by the banking profession. The working party set up in 1982 by a few banks interested in the ECU's development has since welcomed a number of new members, and is now embarking on the practical application of its work. This group could be the hard core of a future association of banks that will manage the clearing of ECU transfers, expected to become operative in 1984.

— *The Commission of the European Communities:* To date, the ECU has developed on the spontaneous initiative of the private sector, without any commitment or responsibility being undertaken by Community or national authorities. The Commission feels that the time has now come for the Member States to take their share of responsibility in the development of the private use of the ECU, which is now emerging more and more as an efficient instrument to reinforce European monetary identity both inside and outside the Community; it has therefore exercised its prerogative to draw the Council's attention to the matter in two communications, on financial integration (18 April 1983) and on the international promotion of the ECU (24 May 1983) (see annexes).

In the first of these communications, the use of the ECU is considered one of the most important means of reviving the financial integration process, which has come to a standstill. The aim is to create a Community financial area which would contribute to the economic development of Europe. This area should be as homogenous as possible; its relations with the outside world would be orderly, and it would have available a set of efficient instruments to tap savings; the idea is to improve opportunities for raising resources to contribute to financing investment in the Community.

In the Commission's view, one of the means of setting up an integrated financial market would be to give Community

residents access to the ECU, for example by enabling them to subscribe to ECU loans issued by Community institutions on the basis of official exchange rates; at present, such operations are either prohibited or made difficult in some of the Member States.

Besides contributing to financial integration within the Community, the ECU could also act as a buffer between the dollar and certain Community currencies. This would make it possible to spread the effects of movements that often disturb inter-EMS relations over all the ECU component currencies. The second communication therefore deals specifically with promoting the international role of the ECU. To this end, the Commission suggests that the ECU should be treated as a foreign currency by all the Member States, and that its use should be facilitated. For its own part, the Commission is prepared to draw up, in due course, a document that would serve as the single reference text on the ECU, setting out the provisions to be respected by all users of the currency instrument.

On 16 May 1983, the Council instructed the Monetary Committee to examine these proposals.

Attractiveness of the ECU

Despite the irregular behaviour of short-term interest rates on the occasion of some realignments, the ECU's essential advantage is that it is more stable than other currencies whether one looks at it from an exchange rate or an interest rate point of view. This double advantage, which has been demonstrated by work done in several quarters,[1] is extremely valuable to commercial and financial operators. Past experience shows that the ECU has provided one of the cheapest means of foreign currency financing from the point of view of the real average cost (interest charges plus exchange rate gains or losses against national currency); moreover, for borrowers in practically all countries, the ECU has been the least risky currency. It is also the most predictable currency in the short term, as a comparison of actual short-term rates with three-month forecasts has shown. In brief, the ECU is attractive mainly because it is stable and little risk is involved in its use as a foreign currency.

[1] In particular, work on this point has been done at three conferences held in 1983: one in London on 27 April on financing, accounting and invoicing in composite currencies, organized by the Fondation pour l'étude du droit et des usages du commerce international (FEDUCI); one in Paris on 10 June on the ECU as a currency for the bank and the firm, organized by the Groupement pour la coopération monétaire européenne; and one in Luxembourg from 13 to 15 September on the future of the ECU organized by Euromoney Publications

Public international bond issues [1]

(million Ecu)

	1981	1982		1983	
	Whole year	1st half	2st half	1st half	3rd quarter
USD	20 445	26 654	19 293	21 850	7 328
DM	1 896	2 294	2 461	4 006	1 304
FF	581	156	76	208	—
UKL	1 162	715	1 283	858	717
HFL	792	394	606	997	303
SFR	3 570	2 398	2 676	2 702	1 144
ECU	190	185	525	900	460
Other units of account	420	17	—	—	—
Yen	2 346	1 863	1 331	1 948	670
CDN	541	1 002	285	505	346
Other currencies	379	185	229	219	159
Total	32 322	35 863	28 765	34 193	12 431

[1] Euro-issues and foreign issues on domestic markets.
Source: EIB.

7. Balance of payments

The world economy has continued to adjust to the changes in the terms of trade between major country groups that were set off by the sharp increase in oil prices in 1979. However during 1982-83, in contrast to the preceding two years, the most striking adjustment, particularly in real terms, has been made by the non-oil developing countries, while in the industrial countries progress towards external balance, which had been especially rapid in 1980-81, has slowed down. The experience of the European Community has conformed closely to that of industrial countries generally in this respect, while that of the United States has been noticeably worse and that of Japan somewhat better than the industrial countries' average. During the last five years industrial countries have experienced significant changes in the structure of their exports and imports. As a general rule they have increased their traditional surplus on trade in manufactured goods to offset the larger deficit on trade in primary products which has resulted from the rise in oil prices. There have, however, been considerable variations in the degree of success with which individual countries have met his challenge. Much of this variation can probably be explained by real exchange rate movements, which have exerted a powerful influence on trade in flows in manufactured goods. The Community's current deficit has now been almost eliminated, but the deficits accumulated in recent years have been aggravated by a heavy net outflow of autonomous capital. The resulting basic deficit has been financed by large-scale official borrowing and an inflow of short-term banking capital. In some Member States this has produced a situation in which debt service now constitutes a serious and persistent drain on resources. Several member countries have also had to draw upon their official reserves and the ratio of reserves to imports has fallen to a level that is decidedly low by historical standards.

7.1 International payments adjustment

The process of international payments adjustment that was set in motion following the eruption of the second 'oil crisis' in 1979 has continued during 1982-83. The current surplus of the oil exporting countries has, at least according to the recorded figures, been transformed into a deficit. The deficit of the industrial countries, taken as a whole, has been virtually eliminated, while that of the non-oil developing countries has been substantially reduced. When allowance is made for statistical errors, mainly in the recording of service and investment income receipts of residents of the oil exporting and industrial countries, it is probable that these two groups have both had a small current surplus this year roughly offsetting the USD 50-60 000 million deficit of the non-oil developing nations.

In nominal terms the current balance of the oil exporting countries has oscillated wildly over the last five years the huge improvement during 1979-80 being followed by a rapid deterioration over the following three years. In real terms the adjustment of this group of countries to the changes in their terms of trade has proceeded more steadily. Between 1978 and 1982 the terms of trade improved by almost 100% and real net imports of goods and services (excluding investment income) increased by USD 85 000 million at 1975 prices, an amount roughly equal to 25% of GDP. This process has now been reversed. The oil exporting countries are estimated to have experienced a deterioration of 14% in their terms of trade this year and this has obliged them to cut back the volume of their imports sharply. As a result the balance of trade on goods and services is expected to show some improvement in real terms this year, although this will not be enough to offset the effect of the adverse movement of the terms of trade, so that in nominal terms both the trade and current balances will continue to deteriorate.

The counterpart to these developments is to be found in the changes that have occurred in the current balances of the industrial and non-oil developing countries. However the adjustment process in these two groups has not been closely synchronized. The industrial countries achieved the greater part of their external adjustment between 1980 and 1981, their current deficit being reduced by two thirds or USD 42 000 million in the space of a single year. Progress since then has been much slower. The non-oil developing

countries, by contrast, did not begin to reduce their current deficit in nominal terms until 1982, but progress in the last two years, despite an unfavourable international economic environment and the unremitting burden of debt service, has been impressive (see Table 7.1).

The pattern of nominal adjustment followed by the European Community has conformed closely to that of the industrial group as a whole—a very strong improvement in 1981, but rather slow progress in the following two years.

The United States achieved a sharp improvement (+ USD 20 000 million) between 1978 and 1981 but the deterioration of USD 35 000 million that has occurred during 1982-83, as a result of more buoyant economic activity in the US than elsewhere in the world economy and a serious loss of competitiveness brought about by the appreciation of the dollar on the foreign exchange markets, has left the US with a significantly weaker position than in 1978. The current deficit this year is expected to be twice as large in absolute terms and about 50% larger in relation to

Table 7.1

Nominal and real external adjustment by major country groups

(USD '000 million)

	1978	1979	1980	1981	1982	1983	Change 1978/83
Oil exporting countries							
(i) *At current prices:*							
Balance of trade in goods & services	+9	+74	+118	+67	−2	−20	−29
Investment income & transfers (net)	−8	−8	−7	−6	−2	−1	+7
Current balance	+1	+66	+111	+61	−4	−21	−22
(ii) *At constant 1975 prices:*							
Balance of trade in goods & services	+13	+22	−10	−48	−72	−62	−75
(iii) *Terms of trade*							
(index: 1975 = 100)	96	123	175	194	191	164	+71 [1]
Industrial countries							
(i) *At current prices:*							
Balance of trade in goods & services	+20	−28	−57	−11	−9	+3	−17
Investment income & transfers (net)	−4	+3	−6	−10	−16	−18	−14
Current balance	+16	−25	−63	−21	−25	−15	−31
(ii) *At constant 1975 prices:*							
Balance of trade in goods & services	+7	−6	+36	+72	+50	+55	+48
(iii) *Terms of trade*							
(index: 1975 = 100)	102	99	93	92	94	95	−7 [1]
Non-oil developing countries							
(i) *At current prices:*							
Balance of trade in goods & services	−30	−41	−59	−60	−28	−11	+19
Investment income (net)	−27	−39	−53	−70	−79	−79	−52
Unilateral transfers (net)	+24	+31	+36	+36	+33	+35	+11
Current balance	−33	−49	−76	−94	−74	−55	−22
(i) *At constant 1975 prices:*							
Balance of trade in goods & services	−41	−47	−35	−24	−1	+7	+48
(iii) *Terms of trade*							
(index: 1975 = 100)	108	108	101	97	94	95	−12 [1]

[1] In percent.

Source: IMF, Commission estimates.

GDP than it was five years ago. Japan has registered a steady improvement in its current account in each of the last four years and the surplus this year is expected to be close in dollar terms to the record figure of 1978 (see Table 7.2).

The oil importing countries were quick to adapt their policies to the events of 1979 and the process of real adjustment to the deterioration in their terms of trade—i.e. of improvement in the balance of trade in goods and services in volume terms—had already begun in 1980. So far as the industrial countries are concerned this process was completed in the two years 1980-81, in the course of which USD 78 000 million worth of goods and services or 1,6% of GDP at 1975 prices was shifted into net exports. Since 1981, however, the real trade balance has deteriorated; exports have fallen while imports have remained frozen at their 1980-81 level. The continuing improvement in the current balance in nominal terms during 1982-83 has been due to more favourable terms of trade (see Table 7.1).

The record of the Community in the field of real, as of nominal, adjustment, has mirrored that of industrial countries generally, with a sharp improvement of the real trade balance during 1980-81 followed by some deterioration

Table 7.2

Nominal and real adjustment in the European Community, the United States and Japan

(USD '000 million)

	1978	1979	1980	1981	1982	1983	Change 1978/83
EC							
(i) *At current prices:*							
Balance of trade in goods & services	+32	+6	−17	+10	+13	+25	−7
Investment income & transfers (net)	−13	−17	−20	−24	−29	−30	−17
Current balance	+19	−9	−37	−14	−16	−5	−24
(ii) *At constant 1975 prices:*							
Balance of trade in goods & services	+22	+8	+16	+49	+39	+34	+12
(iii) *Terms of trade*							
(index: 1975 = 100)	101	99	95	92	95	96	−5 [1]
USA							
(i) *At current prices:*							
Balance of trade in goods & services	−31	−26	−22	−22	−30	−47	−16
Investment income & transfers (net)	+16	+25	+22	+27	+19	+17	+1
Current balance	−15	−1	0	+5	−11	−30	−15
(ii) *At constant 1975 prices:*							
Balance of trade in goods & services	−19	−1	+20	+15	+3	−16	+3
(iii) *Terms of trade*							
(index: 1975 = 100)	96	90	82	85	88	94	−2 [1]
Japan							
(i) *At current prices:*							
Balance of trade in goods & services	+17	−10	−10	+7	+7	+18	+1
Investment income & transfers (net)	0	+1	−1	−2	0	0	0
Current balance	+17	−9	−11	−5	+7	+18	+1
(i) *At constant 1975 prices:*							
Balance of trade in goods & services	+4	−4	+18	+26	+25	+30	+26
(iii) *Terms of trade*	113	96	77	79	80	81	−28 [1]

[1] In percent.

Source: Eurostat and Commission estimates.

during the last two years. The United States has suffered a much more severe deterioration in its real trade balance (USD 36 000 million at 1975 prices between 1980 and 1983) while Japan, having registered a strong improvement (+ USD 30 000 million between 1979 and 1981) has maintained its trade surplus at a roughly constant level in real terms over the last three years (see Table 7.2).

In last year's annual report it was observed that the process of real adjustment in the non-oil developing countries had not really got under way until 1982. In the light of the more complete data now available it is clear that in fact the non-oil developing countries had already begun to shift resources into real net exports on a substantial scale as early as 1980 and the process has continued unabated throughout the last four years. On the basis of present estimates the real trade balance of this group of countries will have improved between 1979 and 1983 by USD 54 000 million or approximately 6% of GDP at 1975 prices. Thus net exports have absorbed half the total increase in real output in this group of countries during the last four years. In fact, at 1975 prices, these countries are now running a small surplus on goods and services (excluding investment income flows). Even at current prices their trade deficit is smaller in relation to output and exports than at any time during the 1970s. The fact that this remarkable real adjustment effort has not been more fully reflected in the current balance of these countries is due to the ever growing transfer burden entailed by debt service which has offset a large part of the improvement in the resource balance. The deficit on investment income account, most of it accounted for by debt service, has increased threefold, or by more than USD 50 000 million since 1978 (see Table 7.1).

7.2 External adjustment and changes in the structure of trade and payments, 1978-82

The second oil crisis produced a deterioration of nearly 10% in the terms of trade of industrial countries between 1978 and 1980, only a small part of which was reversed in the two following years. As a general rule the effects of this terms of trade deterioration were concentrated on trade in primary products (a term which, throughout this chapter, is used to include all goods within categories 0 to 4 of the Standard International Trade Classification). Industrial countries have traditionally run a deficit on their trade in primary products with the rest of the world, but in the two years from 1978 to 1980 this increased from USD 172 000 million to USD 314 000 million on a fob/cif basis (see Table 7.3).

This increase in net imports of primary products has been by far and away the most important single factor contributing to the deterioration in the combined current account of industrial countries since 1978, although others, in particular the growing burden of debt service, have exerted a significant influence upon the performance of individual countries.

Adjustment by the industrial countries has taken two main forms. In the first place they have endeavoured with some success to cut back on the volume of primary product imports, in particular, energy imports. As a result of their efforts their deficit on trade in primary products narrowed from USD 314 000 million in 1980 to USD 250 000 million in 1982. Some of this improvement was due to energy saving and the substitution of internally produced for imported sources of energy and where this is the case it should endure. A large part, however, is simply the result of the recession and may therefore be expected to be reversed once economic activity in the industrialized world recovers to a more normal level.

The second form of adjustment and the one on which the main emphasis must be placed in the medium term since it is the only one that will enable industrial countries to reconcile external with internal equilibrium, consists of increasing the traditional surplus on trade in manufactured goods. Industrial countries as a whole have achieved some progress in the pursuit of this objective, increasing their trade surplus on manufactured goods from USD 135 000 million in 1978 to USD 165 000 million by 1982.

There have, however, been considerable variations in the performance of individual countries. Starting out from a position of current account deficit, the United States suffered a deterioration in its trade balance in primary products of rather modest dimensions (USD 22 000 million or less than 1% of GDP) between 1978 and 1982. Over the same period, despite a short-lived improvement during 1978-80, the balance of trade in manufactured goods showed no change and the United States external adjustment, such as it was, took the form of an improvement in the balance on services and investment income. This was sufficient to produce an outturn for the current account in 1982 that was marginally better in current dollar terms than in 1978.

Japan, by contrast, suffered a deterioration in its balance of trade in primary products during 1978-82 that was much more severe—equivalent to USD 40 000 million or 4% of GDP. However, aided by an exchange rate at which Japanese traded goods were—and still are—extremely competitive, Japanese exporters succeeded in offsetting most of the adverse movement on trade in primary products by an increase in net exports of manufactures. Despite a modest deterioration in the balance on services and transfers, this was enough to restore the current account by 1982 to a surplus of USD 7 000 million, which, in relation to GDP, was roughly equivalent to the average of the years 1975-78 between the two oil shocks. Thus already by 1982 Japan may be considered to have successfully completed the process of

Table 7.3

Contributions to changes in current balances of industrial countries, 1978-82

(USD '000 million)

	1978	1980	1982	Change 1978-82
1. *All industrial countries*				
Trade balance on primary products (fob/cif)	−172	−314	−250	−78
Trade balance on manufactures (fob/cif)	+135	+172	+165	+30
Total merchandise trade balance (fob/cif)	−37	−142	−85	−48
Total merchandise trade balance (BOP basis)	+5	−75	−25	−30
Services, investment income and transfers	+5	+5	−9	−14
Current balance	+10	−70	−34	−44
2. *United States*				
Trade balance on primary products (fob/cif)	−26	−48	−32	−6
Trade balance on manufactures (fob/cif)	−5	+20	−5	0
Total merchandise trade balance (fob/cif)	−31	−28	−37	−6
Total merchandise trade balance (BOP basis)	−34	−25	−36	−2
Services and investment income	+24	+34	+33	+9
Unilateral transfers	−5	−7	−8	−3
Current balance	−15	+2	−11	+4
3. *Japan*				
Trade balance on primary products (fob/cif)	−56	−105	−96	−40
Trade balance on manufactures (fob/cif)	+74	+94	+103	+29
Total merchandise trade balance (fob/cif)	+18	−11	+7	−11
Total merchandise trade balance (BOP basis)	+25	+2	+18	−7
Services and investment income	−7	−11	−10	−3
Unilateral transfers	−1	−1	−1	0
Current balance	+17	−11	+7	−10
4. *European Community*				
Trade balance on primary products (fob/cif)	−88	−152	−119	−31
Trade balance on manufactures (fob/cif)	+84	+87	+93	+9
Total merchandise trade balance (fob/cif)	−4	−65	−26	−22
Total merchandise trade balance (BOP basis)	+13	−35	−3	−16
Services and investment income	+21	+19	+7	−14
Unilateral transfers	−15	−21	−20	−5
Current balance	+19	−37	−16	−35

Source: Eurostat; OECD.

external adjustment to the higher level of real energy costs which have prevailed since 1980.

The European Community, like Japan, experienced a very severe deterioration in its balance of trade in primary products—USD 64 000 million or 4% of GDP in the two years 1978-80 above. Since 1980 it has been somewhat more successful than Japan in reducing its net primary product imports in current price terms and approximately half of the increase in the trade deficit on such goods that had occurred during 1978 to 1980 was eliminated over the next two years. On the other hand it has been much less successful than Japan—although rather more so than the United States—in expanding its net exports of manufactured goods. The Community's surplus on trade in manufactures increased by a modest USD 9 000 million between 1978 and 1980, an improvement equivalent to less than 0,5% of 1978 GDP.

In addition to the deterioration in its visible trade balance, the Community as a whole has experienced an adverse swing on invisible transactions. Much of this has been due to the swing from surplus to deficit on investment income account, as a result of borrowing to finance current deficits in the past. There has also been a steady increase in official transfers to developing countries. The net result of all this has been that, despite a significant improvement since 1980, the Community's current account in 1982 was still USD 35 000 million worse than it had been four years earlier. In 1978 the Community had a current surplus equal to 1% of GDP; in 1982 it had a deficit equal to 0,5% of GDP. Clearly the adjustment process for this group of countries, taken as a whole, still has quite a long way to go before it can be considered to have been completed.

Within the Community there have been significant differences between the Member States in the extent to which they have adjusted and the manner in which that adjustment has been achieved (see Table 7.4).

The most remarkable adjustment was achieved by the Netherlands which, through a combination of restrictive internal economic policy and a sharp improvement in cost and price competitiveness managed both to increase its net exports of primary products and to reduce its net imports of manufactures, thereby improving the current balance by nearly 5 000 million ECU or 5% of GDP. This is much more than was necessary to achieve a satisfactory outturn on current account and it may be thought that external adjustment in the Netherlands has been pushed rather too far.

The pattern of adjustment followed by the FR of Germany has been very similar to that in Japan, with the worsening of the trade balance on primary products continuing throughout the whole four years from 1978 to 1982, but being somewhat more than fully compensated for by a massive increase in net exports of manufactures. Consequently despite a deterioration in services, investment income and transfers, the current account again registered a surplus in 1982, albeit a slightly smaller one than in 1978. Thus Germany, like Japan, may be thought to have successfully completed its external adjustment.

The second oil shock coincided with the transition of the United Kingdom from the status of a net importer of energy products to that of a small net exporter. This, combined with a continuing reduction in dependence on imported foodstuffs completely transformed the country's balance of trade on primary products. In 1978 net imports of primary products still amounted to 12 000 million ECU or 5% of GDP. By 1982 they had fallen to 3 800 million ECU or less than 1% of GDP. However, in sharp contrast to the Netherlands, whose situation is in some respects rather similar, by reason of its status as an energy-sufficient economy, the United Kingdom has not combined an improving trade balance on primary products with an improving trade balance on manufactures. On the contrary, despite restrictive economic policies leading to stagnation of domestic demand, net exports of manufactures declined from 6 600 million ECU in 1978 to 1 100 million ECU or 0,2% of GDP in 1982. This appears to have been the consequence of the steep appreciation of sterling in real terms, which has severely damaged the competitiveness of British manuacturing industry. Over the period under review, however, this worsening of the United Kingdom's manufacturing trade performance has not been sufficient to offset the improvement on trade in primary products, so that both the merchandise trade balance as a whole and the current account improved substantially and registered comfortable surpluses in 1982. This year, however, the United Kingdom, for the first time since statistics on the composition of its foreign trade have been compiled, is expected to record a deficit on its trade in manufactured goods and the surplus on current account is likely to be almost, if not completely, eliminated.

In other Community countries adjustment proceeded more slowly and in some cases there was no adjustment at all in the period under consideration. Italy, Belgium-Luxembourg and Denmark have all made some progress in offsetting the increase in their net imports of primary products by improving their balance of trade in manufactured goods. But in all three countries the effect of this on the current balance has been to some extent offset by an adverse swing on investment income account—the result of the need to service, in a period of high interest rates, the debts that were incurred to finance current deficits in previous years. The growing burden of debt service has proved a particularly serious obstacle to adjustment in Denmark, where the deficit on goods and services (excluding investment income flows) was virtually eliminated between 1978 and 1982, but in spite of this the current deficit more than doubled over the same period.

Table 7.4

Contributions to changes in current balances of Community countries, 1978-82

('000 million ECU)

	1978	1980	1982	Change 1978-82
1. *Belgium-Luxembourg*				
Trade balance in primary products (fob/cif)	−5,4	−8,7	−9,4	−4,0
Trade balance in manufactures (fob/cif)	+3,6	+3,7	+6,2	+2,6
Total merchandise trade balance (fob/cif)	−1,8	−5,0	−3,2	−1,4
Total merchandise trade balance (BOP basis)	−2,3	−4,1	−4,0	−1,7
Services	+1,7	+1,4	+2,5	+0,8
Investment income	+0,5	0,0	−0,5	−1,0
Unilateral transfers	−0,6	−1,0	−1,3	−0,7
Current balance	−0,8	−3,8	−3,3	−2,5
2. *Denmark*				
Trade balance in primary products (fob/cif)	+0,3	−0,4	−0,2	−0,5
Trade balance in manufactures (fob/cif)	−2,5	−1,5	−1,6	+0,9
Total merchandise trade balance (fob/cif)	−2,2	−1,9	−1,8	+0,4
Total merchandise trade balance (BOP basis)	−1,8	−1,5	−1,1	+0,7
Services	+0,9	+0,9	+0,9	0,0
Investment income	−0,7	−1,3	−2,3	−1,6
Unilateral transfers	+0,4	0,0	−0,2	−0,6
Current balance	−1,2	−1,8	−2,6	−1,4
3. *Federal Republic of Germany*				
Trade balance in primary products (fob/cif)	−25,2	−40,3	−46,6	−21,4
Trade balance in manufactures (fob/cif)	+42,1	+44,5	+68,4	+26,3
Total merchandise trade balance (fob/cif)	+16,9	+4,2	+21,8	+4,9
Total merchandise trade balance (BOP basis)	+18,7	+5,8	+24,8	+6,1
Services	−6,6	−9,1	−8,6	−2,0
Investment income	+2,0	+1,7	−1,0	−3,0
Unilateral transfers	−7,0	−9,7	−11,8	−4,8
Current balance	+7,1	−11,3	+3,5	−3,6
4. *Greece*				
Trade balance in primary products (fob/cif)	−0,7	−1,1	−1,8	−1,1
Trade balance in manufactures (fob/cif)	−2,6	−2,8	−3,7	−1,1
Total merchandise trade balance (fob/cif)	−3,3	−3,9	−5,5	−2,2
Total merchandise trade balance (BOP basis)	−2,8	−4,0	−4,6	−1,8
Services	+1,3	+1,8	+2,2	+0,9
Investment income	−0,1	−0,2	−0,6	−0,5
Unilateral transfers	+0,8	+0,8	+1,5	+0,7
Current balance	−0,8	−1,6	−1,5	−0,7
5. *France*				
Trade balance in primary products (fob/cif)	−12,0	−22,0	−27,4	−15,4
Trade balance in manufactures (fob/cif)	+8,0	+5,1	+3,5	−4,5
Total merchandise trade balance (fob/cif)	−4,0	−16,9	−23,9	−19,9
Total merchandise trade balance (BOP basis)	+0,6	−9,4	−16,2	−16,8
Services	+6,7	+7,7	+5,1	−1,6
Investment income	+0,8	+1,6	−0,2	−1,0
Unilateral transfers	−2,6	−3,0	−4,7	−2,1
Current balance	+5,5	−3,0	−16,0	−21,5

Table 7.4 *(continued)*

Contributions to changes in current balances of Community countries 1978-82

('000 million ECU)

	1978	1980	1982	Change 1978-82
6. *Ireland*				
Trade balance in primary products (fob/cif)	+0,6	+0,2	0,0	−0,6
Trade balance in manufactures (fob/cif)	−1,7	−2,1	−1,6	+0,1
Total merchandise trade balance (fob/cif)	−1,1	−1,9	−1,6	−0,5
Total merchandise trade balance (BOP basis)	−0,8	−1,5	−1,6	−0,8
Services	0,0	−0,1	+0,3	+0,3
Investment income	−0,3	−0,5	−0,9	−0,6
Unilateral transfers	+0,7	+0,9	+0,7	0,0
Current balance	−0,4	−1,2	−1,5	−1,1
7. *Italy*				
Trade balance in primary products (fob/cif)	−16,5	−28,0	−35,5	−19,0
Trade balance in manufactures (fob/cif)	+16,3	+12,4	+22,0	+5,7
Total merchandise trade balance (fob/cif)	−0,2	−15,6	−13,5	−13,3
Total merchandise trade balance (BOP basis)	+2,3	−11,8	−8,1	−10,4
Services	+3,8	+4,3	+5,6	+1,8
Investment income	−0,9	−0,5	−4,0	−3,1
Unilateral transfers	−0,3	+0,9	+0,9	+1,2
Current balance	+4,9	−7,1	−5,6	−10,5
8. *Netherlands*				
Trade balance in primary products (fob/cif)	+1,9	+0,9	+3,7	+1,8
Trade balance in manufactures (fob/cif)	−4,1	−2,9	0,0	+4,1
Total merchandise trade balance (fob/cif)	−2,2	−2,0	+3,7	+5,9
Total merchandise trade balance (BOP basis)	−1,2	−1,0	+3,9	+5,1
Services	+0,8	+0,1	+1,0	+0,2
Investment income	0,0	−0,2	−0,1	−0,1
Unilateral transfers	−0,8	−0,9	−1,3	−0,5
Current balance	−1,2	−2,0	+3,5	+4,7
9. *United Kingdom*				
Trade balance in primary products (fob/cif)	−12,0	−9,6	−3,8	+8,2
Trade balance in manufactures (fob/cif)	+6,6	+6,2	+1,1	−5,5
Total merchandise trade balance (fob/cif)	−5,4	−3,4	−2,7	+2,7
Total merchandise trade balance (BOP basis)	−2,4	+2,3	+4,0	+6,4
Services	+5,6	+6,9	+6,4	+0,8
Investment income	+0,9	−0,5	+0,6	−0,3
Unilateral transfers	−2,7	−3,5	−3,7	−1,0
Current balance	+1,5	+5,2	+7,3	+5,8

Source: Eurostat.

France achieved no external adjustment during the four years 1978-82. The balance of trade on primary products grew steadily worse throughout the whole period, while at the same time the surplus on manufactures, which in 1978 had largely offset the deficit on primary products, was reduced by more than half so that a massive deficit on total merchandise trade emerged. The deterioration of the trade balance may be attributed to the fact that economic policy in France during this period was less restrictive than in most of the country's major trading partners as well as to the appreciation of the franc in real terms up till 1981 which somewhat eroded the competitiveness of French manu-

facturing industry. With the surplus on services and transfers also declining, the current account registered an adverse swing of 21 000 million ECU or 5% of 1978 GDP. Ireland and Greece also failed to make significant progress towards adjustment during the years up to and including 1982. In both countries the deterioration in primary product trade continued unabated and little success was achieved in offsetting this by reducing net imports of manufactures. This year Ireland's trade balance, both in primary products and manufactured goods has registered a marked improvement, but in Greece external performance remains a cause for serious concern. In particular the deterioration of the balance of trade in manufactures which appears to have resulted from the opening up of the Greek market to exporters from other Member States following Greek accession to the Community in 1981 has yet to be halted. The problems of both Ireland and Greece, like those of other persistent deficit countries, have been seriously aggravated by the rising cost of debt service.

7.3 Competitiveness and international trade

The second oil shock, like the first, exacerbated existing inflation differentials and triggered off substantial movements in exchange rates. As a result of these two factors, which have sometimes tended to offset and at other times to reinforce each other there have been some rather large swings in international cost competitiveness and these in turn have exerted a significant influence on trade flows. In the short run at least price elasticities of demand tend to be very low for most primary products and probably also for the majority of service transactions, with the notable exception of tourism. As a result the effect of changes in relative costs and prices tends to be felt mainly in trade in manufactured goods. However, manufactured goods account for approximately 75% of total merchandise exports and 60% of merchandise imports of industrial countries, so that relative price changes in this sector, provided that they are accompanied by appropriate internal economic policies, can have a significant impact upon the sum of current transactions.

Changes in competitiveness tend to be spread over a period of several years and their effects sometimes only occur with a lag and then last for several years. Consequently some of the changes in trade in manufactured goods which have occurred during the last few years have their origin in changes in cost and price competitiveness which occurred in the middle 1970s. Some of the more recent changes in competitiveness have yet to produce their full effect on trade flows. Indeed in some cases the effects have not yet even begun to show through.

The basic data concerning the international competitiveness of the European Community, the United States and Japan are set out in Table 7.5. The table compares the performance

Table 7.5

Inflation, exchange rate movements and competitiveness in the European Community, the United States and Japan

(Indices: 1970-75 = 100)

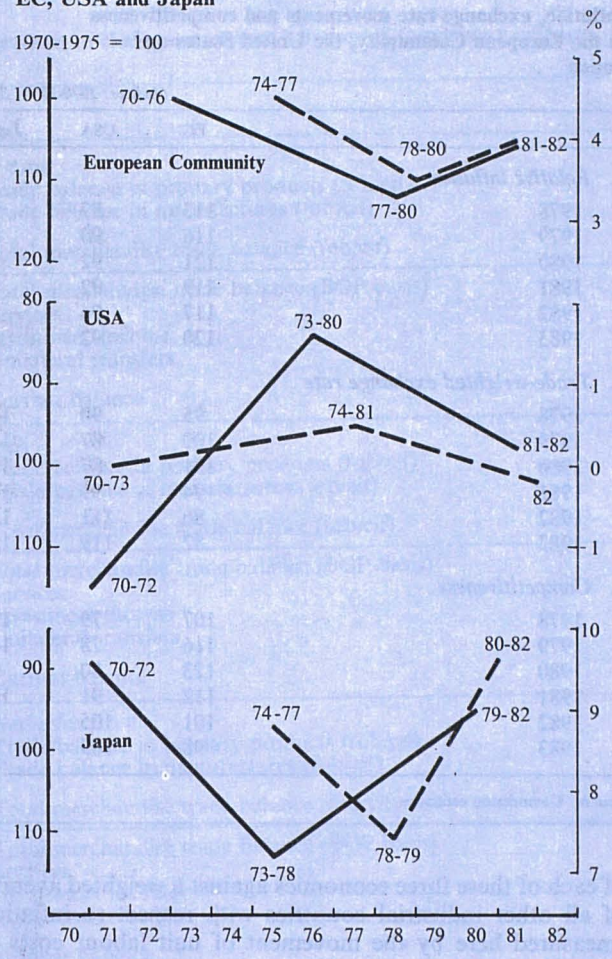
	EC	USA	Japan
1. *Relative inflation*			
1978	113	87	90
1979	116	90	82
1980	121	92	72
1981	119	92	70
1982	117	94	66
1983	120	92	65
2. *Trade-weighted exchange rate*			
1978	95	90	141
1979	100	87	132
1980	101	87	127
1981	94	99	144
1982	86	111	137
1983	82	119	151
3. *Competitiveness*			
1978	107	79	127
1979	116	78	108
1980	123	80	92
1981	112	91	101
1982	101	105	90
1983	98	109	98

Source: Commission estimates.

of each of these three economies against a weighted average of all other industrial countries with respect to inflation (measured here by the movement of unit labour costs in manufacturing), nominal exchange rates and competitiveness. Graph 7.1 shows movements in cost competitiveness and trade performance (measured here by the balance of trade in manufactured goods as a percentage of GDP) and it can be seen fairly clearly from the graph that changes in competitiveness have been followed, with a variable lag of anything up to three years, by changes in trade performance in the direction that both common sense and economic theory would suggest.

During the 1970s inflation in the European Community as a whole was well above the international average, but this was not fully reflected in exchange rate movements. In particular, during the second half of the decade Community currencies appreciated on average against the currencies of competitor countries and this, together with the adverse inflation differential, produced a very substantial loss of competitiveness during 1977-80. This in due course affected the Community's trading performance in the manufactured goods sector, which deteriorated sharply during 1978-80.

GRAPH 7.1: **Competitiveness and trade performance in the EC, USA and Japan**



Note: A fall in either of the two curves denotes a deterioration (i.e. a loss of competitiveness or a fall in the trade balance in relation to GDP). A rise denotes an improvement.

Since 1980 labour costs in the Community have risen at about the same rate as in the rest of the world, but the Community's average exchange rate has depreciated by nearly 20%. As a result the competitive loss experienced during the previous years has been recouped. Already by 1982 the fruits of this healthier competitive position were beginning to show in the Community's trade performance and this trend seems to be persisting during 1983.

The United States' experience has been the mirror of the Community's. During the 1970s inflation in the USA was in fact slightly lower than in competitor countries, but during the latter half of the decade the dollar depreciated, so that by 1980 US competitiveness was about 20% stronger than in 1970-75. This produced a sharp improvement in US manufacturing trade performance during the second half of the decade. Since 1980, however, the position has been dramatically reversed. US labour costs have risen at about the same rate as labour costs in competitor countries but the dollar appreciated by 28% between 1980 and 1982 (and by a further 7% this year). As a result US competitiveness has deteriorated by about one third. This had already produced a very sharp deterioration in US manufacturing trade performance by 1982 and there are clear indications that the decline has continued this year.

During the 1970s Japan had the lowest rate of manufacturing labour cost inflation of any industrial country. In the long term the exchange rate has tended to appreciate and thus more or less to offset the favourable inflation differential, but these exchange rate movements have been very irregular, with the result that the competitive position has shown marked variations in the short and medium term.

Thus appreciation of the exchange rate caused a deterioration of competitiveness during the mid-1970s and this had begun to have some effect on trade performance by 1977-78. However the second oil shock precipitated a steep fall in the yen's exchange rate (since the Japanese economy was thought at the time to be especially vulnerable to higher oil prices) and the recovery since then has been insufficient to offset Japan's below average rate of labour cost inflation. Japan's competitive position is thus still substantially stronger that it was in the late 1970s and this has undoubtedly contributed to the striking improvement in Japanese trade performance since 1980.

Inside the Community too there have been some quite large nominal and real exchange rate movements and these have also, in most cases, produced changes in trade performance in the direction, if not always on the scale, that would have been expected (see Table 7.6 and Graph. 7.2).

Thus in Germany, competitiveness was eroded during the 1970 as a result of the continuous appreciation of the German mark and this produced a deterioration in German trade performance during 1978-80. During 1980-83 competitiveness has improved significantly the result of a continued below-average rate of inflation combined with a fairly stable exchange rate, and this has been followed by a revival of manufacturing trade performance which began in 1982 and seems to have been maintained during 1983.

France experienced a rate of inflation above that of its competitors during 1979-80 but this was not reflected in the behaviour of the exchange rate which was held fairly stable during this period. As a result there was a loss of competitiveness which, with the normal lag of one to two

years, produced a marked falling-off in French manufacturing trade performance during 1980-82. Inflation in France has continued to run above the international average, but exchange rate adjustments within the EMS, combined with the strength of other major third currencies, have by now produced a trade-weighted depreciation of the franc of over 20% since 1980. This has been more than enough to offset the adverse inflation differential and competitiveness has improved substantially. This did not at first produce any positive effect on trade performance, probably because, as mentioned earlier, the pressure of demand in France was maintained at a somewhat higher level than in the country's principal trading partners, but there is some evidence that an improvement is now getting under way.

In Italy inflation has been persistently well above the international average. In recent years, however, the exchange rate has been managed so as to offset this adverse inflation differential. The relative cost position improved markedly in the mid-1970s and has been maintained at a satisfactorily competitive level since then. There has been a considerable improvement in trade performance in response.

In the United Kingdom the combination of a higher than average rate of inflation and a strongly appreciating exchange rate has produced a massive loss of competitiveness since 1978 and this has predictably been accompanied by a very serious deterioration in the UK's trading performance in manufactured goods. The sharp deceleration of inflation together with the fall in the exchange rate during 1982-83 has repaired some of the damage done to UK competitiveness and may arrest the decline in the UK's manufacturing trade performance but it is unlikely that these developments will be sufficient to recover the ground lost over the last four years. At today's exchange rate UK manufacturing costs are about the same, in relation to those of competitors, as they were before the sterling devaluation in 1967.

Among the smaller member countries the Netherlands, Belgium-Luxembourg and Denmark, have all substantially improved their competitiveness during the last three to four years. In the Netherlands this result has been achieved by a lower than average rate of inflation which has been less than fully offset by exchange rate appreciation. In Belgium and

Table 7.6

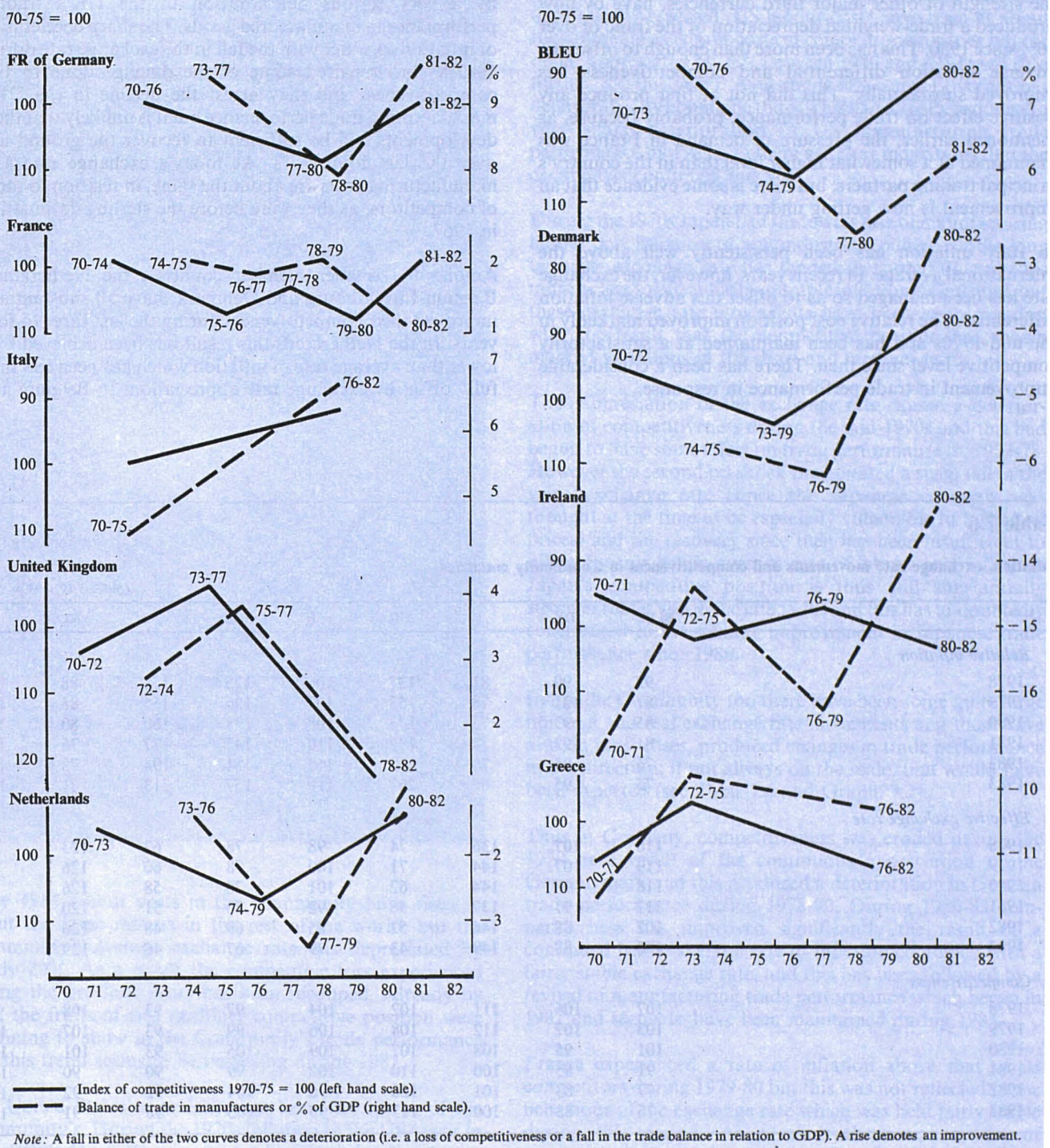
Inflation, exchange rate movements and competitiveness in Community countries

(Indices: 1970-75 = 100)

	BLEU	DK	D	GR	F	IRL	I	NL	UK
1. *Relative inflation*									
1978	92	99	81	137	106	125	151	88	138
1979	87	101	78	153	107	126	155	85	150
1980	85	97	75	173	108	138	160	80	169
1981	81	93	73	197	110	142	177	75	171
1982	76	95	70	233	113	151	194	73	168
1983	75	95	67	262	119	157	213	71	165
2. *Effective exchange rate*									
1978	116	107	136	74	98	78	62	123	69
1979	119	107	144	71	100	78	60	126	74
1980	118	98	144	62	101	76	58	126	81
1981	112	91	137	56	92	70	51	120	81
1982	102	88	144	52	85	69	48	126	78
1983	100	88	149	43	79	67	46	129	73
3. *Competitiveness*									
1978	107	106	111	102	104	97	93	108	95
1979	103	107	112	108	106	99	93	107	110
1980	101	95	108	107	109	105	93	101	137
1981	91	85	100	110	102	99	90	90	140
1982	77	83	101	120	96	104	92	92	131
1983	75	83	100	113	95	105	98	91	120

Source: Commission estimates.

GRAPH 7.2: **Competitiveness and trade performance in EC countries**



Note: A fall in either of the two curves denotes a deterioration (i.e. a loss of competitiveness or a fall in the trade balance in relation to GDP). A rise denotes an improvement.

Denmark, not only has inflation been below the international average, but the franc and the krone have depreciated on a trade-weighted basis, thus producing very large improvements in competitiveness, of the order of 20-30% since 1978. The effects of these changes on trade performance have been particularly striking in the Netherlands, but they have been impressive in Belgium and Denmark too.

The position of the Irish pound is exceptional in that the EMS countries, to whose currencies it is pegged, account for only about 25% of Irish foreign trade. Ireland's principal trading partner, the United Kingdom, which accounts for about 45% of Irish foreign trade, remains outside the EMS. There have been sizeable exchange rate fluctuations between sterling and the Irish pound since the parity between them was broken in 1979 with the result that the movement of the Irish pound on a trade-weighted basis over the last four years has, to a large extent, escaped the Irish authorities' control. Despite this Ireland has over the years managed—sometimes more by accident than design—to offset a persistently higher than average rate of inflation by a generally downward movement of the exchange rate on a trade-weighted basis. Variations in competitiveness have been fairly moderate and changes in relative pressure of demand appear to have exerted a more important influence on trade performance, which has fluctuated considerably over the medium term. Greece, on the other hand, has failed to offset its higher than average rate of inflation by exchange rate adjustment and its competitiveness appears to have been quite seriously eroded during recent years, although so far the effect on trade performance has not been as damaging as might have been expected. The devaluation of the drachma at the beginning of this year has recouped less than half of the competitive loss suffered during 1979-82.

7.4 Financing the Community's deficit

As mentioned earlier, progress towards the elimination of the Community's current deficit which had been substantial in 1981 has slowed down considerably since then. Nevertheless, according to present forecasts the Community as a whole will have almost eliminated its current deficit this year. As usual performance has varied considerably from one member country to another. The Federal Republic of Germany, Italy, the Netherlands, the BLEU and Ireland have continued the process begun in 1981 (or in some cases in 1982) and have either moved back into comfortable surplus or considerably reduced their deficits. The United Kingdom and France on the other hand have both suffered a serious deterioration, the surplus of the former having almost disappeared, while the deficit of the latter has substantially increased. In Denmark and Greece there has been little change in an already unsatisfactory situation (see Table 7.7).

Table 7.7

Current balances of Community countries

('000 million ECU)

	1980	1981	1982	1983 [1]	1984 [1]
BLEU	−3,6	−3,6	−3,3	−2,1	−1,4
DK	−1,8	−1,7	−2,6	−1,3	−0,7
D	−11,3	−5,6	+3,5	+6,0	+6,1
GR	−1,6	−2,1	−1,5	−1,9	−2,1
F	−3,0	−4,3	−16,0	−8,6	−4,8
IRL	−1,2	−2,0	−1,5	−0,4	−0,1
I	−7,1	−7,4	−5,6	−2,8	+0,3
NL	−2,1	+2,6	+3,5	+4,6	+5,7
UK	+5,2	+11,0	+7,3	+1,2	−0,4
EC	−26,4	−13,1	−16,2	−5,3	+2,6

[1] Forecast.

Source: Eurostat and Commission estimates.

The Community has now been in deficit on current account for five consecutive years (1979-83). This is by far the longest uninterrupted period of deficit in its history. Over the four years 1979-82 for which reasonably reliable and comprehensive data are available the Community as a whole recorded a cumulative current account deficit of 62 000 million ECU. To this was added a net outflow of private non-bank capital of 65 000 million ECU, making a total 'basic' deficit to be financed of 127 000 million ECU.

Over this four year period every single Member State has recorded a substantial deficit on its basic balance of payments. In Germany, France and the BLEU the current deficit was aggravated by a net outflow of private non-bank capital. In Italy, Denmark and Ireland only a small part of the current deficit was covered by a net capital inflow. Greece alone managed to finance more than half its current deficit through a net inflow of private non-bank capital. In the only two members to record a current surplus over the period as a whole, the United Kingdom (where developments have clearly been influenced by the removal of exchange controls) and the Netherlands, the net capital outflow greatly exceeded the current surplus (see Table 7.8).

There have been considerable variations between Member States in the manner in which these basic deficits have been financed. The Federal Republic of Germany, Italy, the BLEU, Denmark and Greece have had recourse mainly to official borrowing, with use of reserves playing a significant, although secondary, role in the German case. France, the United Kingdom and the Netherlands have financed their deficits almost entirely by means of short-term borrowing by

Table 7.8

Balance of payments financing in the Community, 1979-82

('000 million ECU)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1. Cumulative current account deficit	−12,6	−8,3	−17,9	−7,0	−19,4	−5,4	−16,1	+2,4	+22,2	−62,1
2. Private non-bank capital (net)	−4,9	+2,5	−8,0	+4,1	−12,1	+1,4	+2,3	−6,9	−43,2	−64,8
3. Total to be financed (= 1 + 2)	−17,5	−5,8	−25,9	−2,9	−31,5	−4,0	−13,8	−4,5	−21,0	−126,9
Financed by:										
4. Banks + errors and omissions	+5,9	−0,6	−4,5	+1,0	+28,9	+2,2	+2,6	+6,8	+18,2	+60,4
5. Official long and short-term capital (net)	+9,8	+5,6	+21,1	+1,5	+0,5	+2,1	+9,6	−0,7	−1,2	+48,2
6. Change in reserves (− denotes increase)	+1,8	+0,8	+9,3	+0,4	+2,1	−0,3	+1,6	−1,6	+4,0	+18,3

Source: Eurostat and Commission estimates.

banks. [1] In the Netherlands' case such borrowing exceeded the basic deficit and thus allowed a small addition to reserves.

During the period under review the five smallest Member States—the BLEU, Denmark, Greece and Ireland—all registered cumulative current deficits equal to between 15% and 30% of 1982 GDP. Except in the case of Greece, where, as already mentioned, inflows of private non-bank capital covered a substantial proportion of the deficit, financing has been achieved almost entirely by a combination of official borrowing and short-term borrowing by banks. Thus debts have been incurred which are decidedly large in relation to the economies of the countries concerned, while there must be considerable doubt whether the funds have been used productively in the sense of generating additional tradeable output in the future. With high rates of interest at present being applied to such large amounts of outstanding debt, debt service has become a serious burden for some of these countries. The annual net outflow on investment income account, most of it debt service, is now estimated to amount to 5% of GDP in Denmark and 6% in Ireland.

Notwithstanding that most of the Community's deficit during 1979-82 was financed by borrowing, the net effect of transactions over this period was to reduce gross reserves by the equivalent of 18 000 million ECU. The fact that over the same period the level of gross reserves (excluding the 80% of gold reserves that have not been swapped against ECU), expressed in terms of ECU, has risen by 27 000 million ECU is to be explained entirely by valuation changes. Over this period the ECU value of the Community's foreign currency and SDR denominated holdings has been considerably

[1] Including 'errors and omissions'.

Table 7.9

Gross reserves in the European Community

('000 million ECU)[1]

	1978	1980	1982	1983
	end of year			June
B/L	3,4 (7,5)	6,0 (8,7)	3,7 (4,3)	6,0 (6,5)
DK	2,3 (15,3)	2,6 (13,5)	2,3 (9,5)	3,4 (13,0)
D	39,5 (32,2)	36,2 (21,0)	47,2 (22,6)	50,4 (24,0)
GR	0,8 (13,0)	1,2 (14,2)	1,2 (8,8)	1,2 (8,8)
F	9,6 (10,5)	22,3 (16,0)	16,2 (8,9)	20,1 (10,3)
IRL	1,9 (29,2)	2,1 (21,9)	2,7 (24,0)	2,4 (21,8)
I	10,4 (20,0)	17,6 (21,1)	14,5 (13,5)	20,8 (19,3)
NL	5,0 (10,0)	8,8 (12,6)	10,4 (12,3)	11,2 (13,2)
UK	11,3 (15,0)	15,7 (14,1)	12,7 (9,3)	13,2 (9,1)
EC	84,2	112,5	110,9	128,5
USD 000 million	116,0 (18,1)	145,5 (16,5)	107,5 (12,9)	114,2 (14,5)

[1] Figures in brackets indicate the ratio of reserves to imports of goods and services.
Souce: Commission.

inflated by the appreciation of the dollar against the ECU, while the value of ECU holdings has been inflated both by the appreciation of the dollar and by the increase in the price of gold.

Despite the rise in the level of reserves, the ratio of reserves to imports declined by nearly one third between 1978 and 1982, an experience which the Community has shared with industrial countries generally. Reserve to import ratios had sunk to particularly low levels in France, the United Kingdom, the BLEU, Denmark and Greece. During the first half of 1983 some of these countries, and indeed the Community as a whole, were able to replenish their reserves to a limited extent, although in most Member States reserves are still on the low side in relation to imports when viewed in the light of historical experience (see Table 7.9). Only in the Netherlands is the ratio of reserves to imports higher today than it was five years ago. Moreover, since in almost all Member States the present level of gross reserves has only been achieved by heavy foreign borrowing in one form or another, the gross figures conceal the considerable absolute decline in net reserves that has occurred since 1978.

8. Some properties of the European economies in the light of econometric models

The Commission services are at present using two econometric models for macroeconomic forecasts and analyses. The earlier of these models, Comet, was used especially in the studies associated with the fifth medium-term programme. The second model, Eurolink, groups four large national models (those for Germany, France, Italy and the United Kingdom), which are linked with each other and with the rest of the world via bilateral international trade flows. In 1983, Eurolink was used to construct a set of economic policy multipliers for a number of budgetary and monetary measures, and to analyse the reaction of the countries covered to certain external shocks and to changes in exchange rates. One may, of course, question and discuss how faithfully economic systems can be represented by means of models, however complex they may be. The lessons drawn from the analyses presented here should therefore be treated with caution. Yet they illustrate the impact of certain economic policy measures depending on whether they are taken in isolation or coordinated, on whether the budgetary measures are taken against an accommodating or a restrictive monetary background, and on whether their environment is one of controlled or freely floating exchange rates.

8.1 The economic policy scenarios

This chapter presents a systematic analysis of the Eurolink model's responses to a normalized series of shocks involving public expenditure and revenue, interest rates, changes in nominal wages, the influence of the import price of oil (or export price in the United Kingdom's case), and deliberate devaluations and revaluations of national currencies. The opportunity was also taken of comparing the impact of each measure according to whether the shock is given in isolation in one country or jointly by all the European countries at once. Also, the presence in each national model of a monetary and financial sector was used to compare the effect of the budgetary measures taken against an accommodating monetary background (in the sense that interest rates are held constant) with the effect against a non-accommodating monetary background. Whenever the model permits, each shock is applied first with an unchanging exchange rate, and then with a freely floating exchange rate, except, of course, for the shocks to the exchange rates themselves, where the variant is a comparison of the effect of a 10% devaluation against the dollar with that of a 10% revaluation. Lastly, we tested the impact of a reaction to the rise in raw material prices under an expansionary budgetary policy (via public investment).

8.2 Summary of the main results: general comments

Several million numerical data and well over a thousand pages of detailed commentaries would be needed for an exhaustive presentation of the variations observed in all the models' variables in response to the shocks in all their variants; the picture would be too complex to be grasped and there would be a good chance of not being able to see the wood for the trees.

Therefore, all that we can do here is to present an overall macroeconomic summary of the results obtained, putting the emphasis on a comparison of changes rather than absolute levels.

The analysis will be made in two stages: the first will examine the comparative effectiveness of the measures tested in terms of the fundamental objectives of economic policy: growth, inflation, employment, external equilibrium and general government borrowing requirement. Since the Eurolink models are basically geared to short-term or short medium-term forecasting, the period considered was deliberately limited to 16 quarters.

This section will confine itself to examining the measures in the most usual simulation of the national models, i.e. action in isolation, fixed exchange rate and non-accommodating monetary policy. [1] These assumptions will be relaxed in the following sections.

Table 1 of the annex summarizes the results obtained for growth and prices.

With regard to growth, the magnitude of the multipliers may vary substantially from one shock to another but broadly

[1] A situation where interest rates are free to fluctuate in response to shocks to the other variables.

speaking, one might say that a 1% variation in public income or expenditure is equivalent to a 6 to 8% variation in the exchange rate.

It is more difficult to compare the shocks to the main items of revenue (direct and indirect taxes, social security contributions) and expenditures (public consumption and investment, social transfer payments) in that the results are clearly affected by the level of disaggregation of the public sector, which can vary from one model to another. Nevertheless, the results clearly show that measures in the form of direct injections of spending into the economy (public consumption and investment) have greater immediate effects than shocks acting on the components of disposable income (direct taxes, social security contributions and social transfer payments) or on the price elasticity of demand (indirect taxes), this of course reflecting the leakage into saving.

Also, on the revenue side, the negative effects of putting up direct taxes are appreciably weaker than the effects of an initial increase of the same amount in indirect taxes or social security contributions. For, in all the models, the general fall in domestic demand resulting from the increase in direct taxation is reflected in a downward pressure on prices which improves the external competitiveness of the country in question, whereas the two other shocks are characteristically reflected in 'stagflation', with falling GDP, rising unemployment and accelerating inflation.

Lastly, the simulation of a 20% fall in the price of oil has comparable initial effects for France and Germany (an increase of 0.5 points of GDP), with Italy reacting much more sharply (an increase of 1.2 points). The Treasury model's reaction is very interesting in that although the United Kingdom exports more oil than it imports, the net overall effect on growth is slightly positive because of the fall in the inflation rate.

If we now consider the dynamic profile, the comments on the instantaneous impacts change a little. With regard to budgetary measures, the initial substantial impact of increases in public consumption and investment diminishes very rapidly over the period, and by the end of the fourth year is down to under half the starting level, whereas the weakening is far less marked for measures acting on incomes or prices. There are, nevertheless, two notable exceptions to this rule; France, where the impacts remain virtually at their starting level throughout the period and Italy, where public investment also maintains its initial impact. Table 8.1 gives the initial and final ranking of economic policy instruments in decreasing order of power of impact (in absolute value).

With regard to the inflation rate, the results clearly reflect the structural differences that have been observed amongst the EC countries. Whatever the measure, the induced inflationary or deflationary mechanisms are generally weaker in Germany than in the other three countries, except for the impact of a 2% reduction in the growth rate of nominal wages. However, this is partly for technical reasons: given the growth rate of nominal wages in Germany, a 2% reduction is a modification in the trend far more substantial in relative terms than it is in the high-inflation countries.

When one compares the dynamic profiles (with fixed exchange rates), however, substantial divergences appear between Germany and the United Kingdom on one side and France and Italy on the other side. In the former group, the impacts on prices do not fall over time, although the real impacts of the shocks are decreasing (see Graphs 8.1 and 8.3). For France and Italy, on the other hand, the price profile duplicates the output profiles. However, since large divergences exist between the models in the modelization of the wage-price block (notably in the inclusion of demand-pull versus cost-push factors), further investigations are clearly needed in this field before making any structural conclusions about inflation dynamics in the four Eurolink countries.

Table 8.1

Ranking by decreasing initial and final impact (in absolute value) of budgetary policy instruments. Effects on real GDP

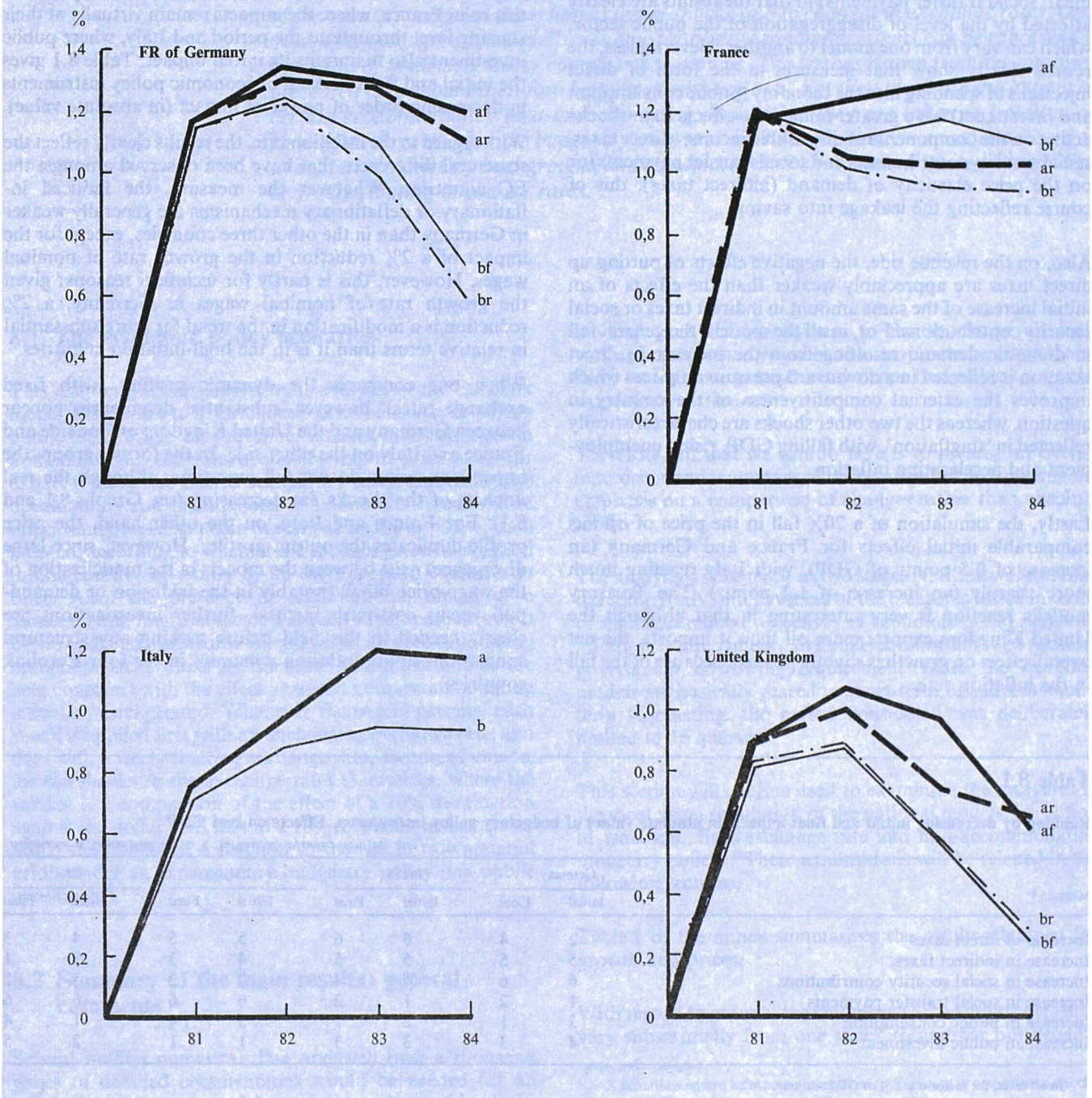
(1 = the most powerful instrument; 6 = the least powerful instrument)

Measure [1]	Germany		France		Italy		UK	
	Initial	Final	Initial	Final	Initial	Final	Initial	Final
Increase in direct taxes	2	4	6	6	5	5	4	3
Increase in indirect taxes	5	5	5	5	4	3	3	1
Increase in social security contributions	6	6	4	4	2	2	5	2
Increase in social transfer payments	1	2	1	2	6	6	6	6
Increase in public consumption	3	1	2	1	3	4	1	4
Increase in public investment	4	3	3	3	1	1	2	5

[1] In all cases, the increase is 1 % of GDP, *ex ante*.

GRAPH 8.1: **Comparative dynamic profile of the multipliers linked to an increase in public investment equal to 1% of 1981 real GDP — Impact on GDP**

(a = accommodating monetary policy; b = non-accommodating monetary policy; r = fixed exchange rate; f = flexible exchange)



Two shocks stand somewhat apart: first, the reduction in the price of oil has positive effects on the growth of real GDP and negative effects on the inflation rate, both of which increase over time in all countries.

Second, the change in the trend rate of growth of nominal wages differs markedly from the other measures. In all the countries, the negative effects on prices are very sharp (ranging from $-1{,}5\%$ initially to -3% or even -4% at the end of the period).

The real effects of the wage compression, by contrast, differ appreciably depending on whether or not its negative effects on private consumption are offset by positive effects on investment and exports; whether or not this happens also depends on the net effect on imports of the variations in the above three aggregates. In France, the 'private consumption' effect is much larger, producing an appreciable reduction (over one half of a percentage point) in GDP. In Germany, positive and negative effects virtually cancel each other out, the net negative effect on GDP being very close to zero. In Italy and the United Kingdom, on the other hand, the net overall effect is positive on GDP and growing over time (ranging from $+0{,}15$ to $0{,}5\%$ in Italy, and from $+0{,}17$ to $+1{,}0\%$ in the United Kingdom).

With regard to employment and unemployment, our analysis confirms the results obtained in all the similar exercises undertaken elsewhere: the induced employment effect of shocks bearing initially on aggregate demand fluctuates with the variations in GDP and in prices and wages but remains relatively marginal. More specifically, none of the measures studied here produces a variation in the unemployment rate of more, in absolute value, than half a percentage point relative to the starting level, with the most powerful measures (if we can use this term) for bringing down the unemployment rate being an increase in public consumption and a 2% reduction in the growth of wages. In the other direction, indirect taxes and the increase in social security contributions have effects which are virtually similar (ranging from $+0{,}2$ to $+0{,}3$ percentage points) and greater than the effect of direct taxes and a revaluation. Lastly, the increase in interest rates produces no more than a negligible variation in employment and unemployment. These results confirm the great inertia of demand for labour observed in Europe since 1962.

With regard to the external equilibria, the changes in current account balances stem from the combination of two effects which can either reinforce each other or cancel each other out. The first effect is the result of the variation in aggregate demand. As a general rule, and all things being equal, the current account balance will deteriorate if domestic demand expands, and will improve in times of recession. Added to this demand effect is a price effect since every acceleration (deceleration) in inflation tends to worsen (improve) the current account balance. As a general rule, however, the 'volume' effects outweigh the 'price' effects.

The current balance effect of increases in public revenue is consistently positive, with indirect taxes this time having a markedly greater effect due to the working of value-added tax (VAT), which is charged on imports but not on exports. In this case, therefore, both the volume effect and the price effect depress imports.

The current balance effects of public expenditure increases are consistently negative. But we note a smaller deterioration with shocks to public consumption and investment (which have a low import content and which affect the other components of demand only indirectly) than with shocks to social transfer payments, which act directly on private consumption.

The effects of the reduction in wage growth are consistently positive for France and Germany. For Italy and the United Kingdom, however, the effects change from positive to negative from the third year on as a result of the deterioration in the terms of trade. The two percentage point rise in the short-term interest rate has favourable effects for France, Germany and Italy. For the United Kingdom, however, the positive effect on the balance of goods is accompanied by a negative effect, greater in absolute value, on the balance of services and transfers. The net overall effect is therefore a slight deterioration in the current account balance.

The contrast between the United Kingdom and the other countries recurs, as had to be expected, for the oil price shock (-20%): in the United Kingdom, the drop in export revenue produces a deterioration in the balance of trade which grows from $0{,}1\%$ of GDP in the first year to $0{,}6\%$ at the end of the period, relative to the base solution, whereas for the other countries, there is an improvement of over 1% of GDP.

Lastly the devaluations and revaluations have the expected effects, but with a J-curve phenomenon in the first year in all the countries. We also note marked differences in the lags with which imports and exports adjust to the new prices, these lags being longest in Germany.

The general government borrowing requirement also reacts to the combination of a volume effect on real income and transaction and a price effect, which can either come on top of each other or can cancel each other out, in addition, of course, to the possible initial shock. So we find that for the same *ex ante* increase, the increases in social security contributions produce an *ex post* reduction in net borrowing greater than that deriving from direct and indirect taxes. However, on the public expenditure side, the effects in increasing the deficit are the same once the slight differences in impact on the nominal taxable bases have been eliminated. Lastly, we find that from a dynamic point of view, the final *ex*

post effect is always smaller than the initial effect and represents only 60-70% of the shock defined *ex ante*.

The effect of the reduction in the growth rate of wages is strongly affected by the differences in the way in which public revenue and expenditure are incorporated into the models, and in particular by the divergent role played by the private sector nominal wage rate in the determination of public sector wages and social transfer payments: thus we find that for France and the United Kingdom, the fall in tax revenue caused by the reduction in the wage bill is virtually offset by a drop in current public expenditure. By contrast, for Germany and Italy, the revenue reduction effect markedly outweighs the induced variation of expenditure.

The effects on the general government borrowing requirement of raising the short-term interest rate also vary considerably from one model to another, depending partly on institutional differences. The direct effect depends on the interactions first, between the various interest rates (controlled/not controlled, short-term/long-term, private/public) and second, on the repercussions which these interactions have on the servicing of the public debt broadly defined. Added to this there is, of course, the induced effect of the fall in transactions and incomes. Conclusions on the economies concerned rather than on the way they are represented in the model would therefore be risky. In any event, the public finance effects measured by Eurolink in this area are everywhere very small.

The effects of the external measures (oil price, devaluation, revaluation) do not call for any special comments, since the borrowing requirement varies relatively little, except for the United Kingdom, where the public sector borrowing requirement increases by half a percentage point of GDP as a result of the drop in oil revenue.

8.3 Analysis of the variants

As stated in section 8.2, the multiplier effects described apply to the models used in isolation, assuming a fixed exchange rate and a non-accommodating monetary policy in the sense that interest rates will react to fluctuations in the transactions level and the inflation rate.

This section will analyse the implications for the multipliers of relaxing these assumptions in succession.

A priori, the linkage of the models might seem to be merely a technical problem since, to simplify the point, in Eurolink the only difference between a 'linked' model and its 'non-linked' equivalent is that the global export function to the world is replaced by five export functions to the three European partners, the United States and the rest of the world.

Further, the disaggregated functions may be so calibrated that the introduction of disaggregated growth and price assumptions compatible with the former aggregated one will produce the same result, the sum of the five partial 'linked' flows being equal to the global 'non-linked' export flow. This can actually be achieved for the purposes of forecasting. [1] However, when policy simulations are carried out, a non-linked model will necessarily supply multipliers which are underestimated in relation to its linked equivalent. For, in a non-linked national model, exports are virtually exogenous, and the only element under the model's control is the export price. The explanatory factors, movements in export demand and competitors' prices are, by their nature, exogenous and hence unchanging in relation to the shocks which do not affect them directly. In the same way, where imports are concerned, although domestic demand and prices are controlled by the model, the import price itself is also unchanging in relation to economic policy shocks.

Once the model is linked, any expansionary shock (for example) will increase imports as before, but this increase will necessarily be reflected in an increase in the partner countries' exports; this in turn will increase their import demand, which will create additional export possibilities for the country to which the initial shock is applied. In other words, the effect of the leakage into imports is partly offset by an increase in exports to the partner countries, which boosts the multipliers. Conversely, if a measure is deflationary, the transmission of the fall in demand to the other countries will reinforce the negative domestic effects of the measure by an induced reduction in export demand. The same will occur for prices once the import price ceases to be an exogenous datum to become the average of the other countries' export prices.

Eurolink clearly illustrates the phenomenon described above: the mere linkage of the models is sufficient to increase the absolute value of the multipliers by 10-15% with all the measures. The exceptions are the fall in the oil price which, by its nature, applies to all the countries at once and will therefore be analysed below, and the changes in exchange rates, where the effect of the linkage is to reduce the value of the non-linked model's multipliers, since the non-linked changes in the exchange rate are made at the expense (or to the advantage) of the partner countries, the reduction in imports which accompanies a devaluation produces, *ceteris paribus*, a reduction in demand from those same countries *vis-à-vis* the devaluing country. Conversely, the negative

[1] This implies also linkages in the monetary and financial part of the model where consistency of interest rates and exchange rates must be ensured. In Eurolink, this is obtained through *ad hoc* linkage equations ensuring the unicity of bilateral parities once the US dollar-national currency parity is defined, the dollar being the 'numéraire' (or in more technical terms, the nth country money).

effect of a revaluation will be smaller in the linked than in the non-linked version.

If we now examine the effect of joint measures, taken by all the countries together, as compared with measures taken in isolation, the effects described above will be further reinforced, with the multipliers being increased in value by between 10% and 25% as compared with the non-linked version. Of course, this operates at all levels. Consequently, the stimulatory effects of a joint expansionary policy will be distinctly greater than the effects of isolated efforts, but so will the induced inflationary pressures.

The oil price simulation is particularly interesting here. As said before, by its very nature it applies to all countries at the same time just as a concerted action on domestic policy instruments. Therefore, linked and non-linked multipliers are quite similar except for the single net exporter in the group, the United Kingdom. In this country,the decrease in export revenue due to the fall in the price of oil becomes less important in the linked version, where the induced expansion of the partner countries' demand is explicitly taken into account.

Also here too parity changes differ from the other shocks in that joint devaluation by the four European Eurolink countries does not greatly change their relative positions and improves their competitiveness only in relation to the rest of the world, i.e. in respect of some 50% of their trade instead of total trade as in the non-linked simulations. The value of the joint multipliers will therefore be 10-30% lower than with isolated measures.

The action of monetary policy also deserves some attention. The simulations can be carried out using either free interest rates (non-accommodating monetary policy) or constant interest rates, with money supply adjusting as a result. The section 8.2 exercises reveal a Keynesian (or Hicks' effect) of the shocks to interest rates which clearly respond to the variations in transactions demand and thus act on the interest-rate-sensitive components of real demand. Added to this effect are, of course, the portfolio effects with regard to the equilibria between assets, with the implications of such effects for the interest rate being a *priori* indeterminate. It is nevertheless clear that the role of portfolio or wealth effects is only a minor one in the Eurolink models as compared with the effects of the transactions demand for money balances.

The models left to themselves therefore point to private expenditure being crowded out by public expenditure via the induced interest rate variations. This crowding-out effect can be measured by fixing interest rates within an 'accommodating' monetary policy, with money supply adjusting immediately so as to hold interest rates constant.

Examination of the results shows that an accommodating policy has a greater effect on the dynamic profile of the public expenditure multipliers than on their initial level: given the response lag of transactions demand to the public expenditure shock, the adjustment lag between that response and the change in interest rates and lastly the response lag of the components of final demand to the variations in the interest rate, the immediate impacts are almost identical under the two monetary policy assumptions.

By contrast the multipliers which are characteristic of the simulations for a stimulus to public consumption or investment no longer taper off here; they stabilize at a level close to the maximum generally reached at the end of the second period. The shift observed for GDP for example reached relative values ranging from −25% (Germany) to −60% (United Kingdom) in the 'non-accommodating' multipliers as compared with the 'accommodating' multiplier. The exception to the rule is France, where the differences between the two sets of multipliers are surprisingly small: this seems to be due to the fact that interest rates almost completely fail to react to the shocks affecting the real part of the model.

The crowding out of private expenditure by public expenditure is therefore apparent in the models (other than Metric) but its short-term effect is weak. It is possible, however, that the present models (for the most part estimated before the large rise in interest rates in 1981-82) slightly underestimate both the possible reaction of interest rates to restrictive monetary policies and the economy's speed of response to such changes in rates. In addition, because the present linkage system operates only in respect of goods and services, it disregards the international transmission effects of interest rate movements and is therefore liable to underestimate the effects of restrictive monetary policies, especially in the event of joint policies.

With the exception of Prometeia, all the Eurolink models contain a set of equations for the endogenous determination of exchange rates, which varies in specification from one model to another, but which takes direct or indirect account of the inflation differentials and of the degree of disequilibrium of the balance of payments on current account. The United Kingdom model additionally takes account of the interest differential and of capital movements.

The single country simulation results thus show marked differences in the country changes. If we consider France, the current balance effect is clearly predominant in determining the exchange rate. Consequently, the measures which improve the balance (shocks to public revenue, the growth rate of wages, the rise in the interest rate, the oil price) produce an induced exchange rate appreciation which is small to begin with but which reaches 2% at the end of the period. The appreciation thus modifies the dynamic profile

of the multipliers by increasing the medium-term depressive effect of the deflationary measures (or by reducing the favourable impact of the fall in the oil price), the absolute value of the final multiplier being 15-20% higher than that of the multiplier obtained under a fixed exchange rate, all other things being equal. Converse effects can be observed with measures which cause the current balance to deteriorate.

For Germany, the greater weight attached to the inflation differential reduces the net effects of the exchange rate shocks: thus the shock to VAT improves the current balance and therefore tends to cause appreciation of the exchange rate but it also widens the inflation differential, which tends to cause depreciation of the exchange rate. As a general rule, however, the balance of payments effect is dominant and the exchange rate appreciates but far less sharply than in France. The effect on the multipliers is therefore very small.

Lastly, for the United Kingdom, we find that the induced interest rate variations and their effects on the balance of services, transfers and foreign capital tend to outweigh the balance of trade effects. We thus find marked differences in the effects of floating rates on the multipliers depending on whether monetary policy is accommodating or not. In the former case, we observe that an increase in public expenditure (for example) will initially produce an appreciation of the exchange rate which will not be transformed into a depreciation (as in the other models) until after the second year of the simulation period. Where budgetary policies are concerned, the distortions in the dynamic profile of the multipliers are therefore a good deal more complex than in the other models, making any generalization difficult.

By contrast, the simulation of a restrictive monetary policy in the shape of a deliberate increase in interest rates is far clearer: in all cases, a restrictive monetary policy tends to cause exchange rate appreciation, which reinforces the policy's depressive effect by destroying with varying rapidity the current balance gain observed in a fixed rate situation. The effect of these policies is therefore both more pronounced and longer lasting. This would therefore tend to confirm the theoretical findings of Mundell and Fleming on the comparative effectiveness of monetary policies under fixed and floating exchange rates. However, the simulations do not confirm the other part of the Mundell-Fleming propositions, namely that budgetary policies have no permanent effect in a floating rate situation. On the contrary, and as indicated above, in a floating rate situation, the expansionary or contractionary effect of budgetary measures tends to strengthen in the medium-term.

However, the simulation of joint policies under floating exchange rates produces a different picture. For, once the exchange rates vary in the same direction for everyone, the relative changes in competitiveness diminish, which reduces the impact of variations in rates.

Graph 8.1 summarizes all these results for the shock to public investment.

Lastly, the simulation of a shock public investment was used to test the effects of a rise in raw material prices in response to joint expansionary action in the four European Eurolink countries and in the United States, making the assumption that this action would result in a 10% increase in the price of raw materials with respect to the base case. As shown in Table 2 of the annex this price rise practically cancels the impact of the participation of the US to the European concerted action.

More precisely, these effects are obtained with a 10% rise in the price of raw materials (oil and non-oil) in the first year, with prices thereafter stabilizing in nominal terms to return to their baseline level at the end of the simulation period.

The effects of this rise are shown in Table 2 and in Graph 8.2 where we note an appreciable decline in growth accompanied by an equally appreciable acceleration in inflation, with the impact of imported inflation much greater than the deflationary effect of the fall in the activity level.

8.4 Conclusion

Although the Eurolink results should be treated with some caution in that certain differences in impact clearly have more to do with 'technical' differences between the models than with the structural differences between the economies concerned, it is evident from the multipliers that the actual structural differences are indeed taken into account: examples are the weaker response of the inflation rate in Germany, the United Kingdom's position as an oil exporter, the fact that indirect taxes contribute a larger proportion of French budget revenue than direct taxes, etc.

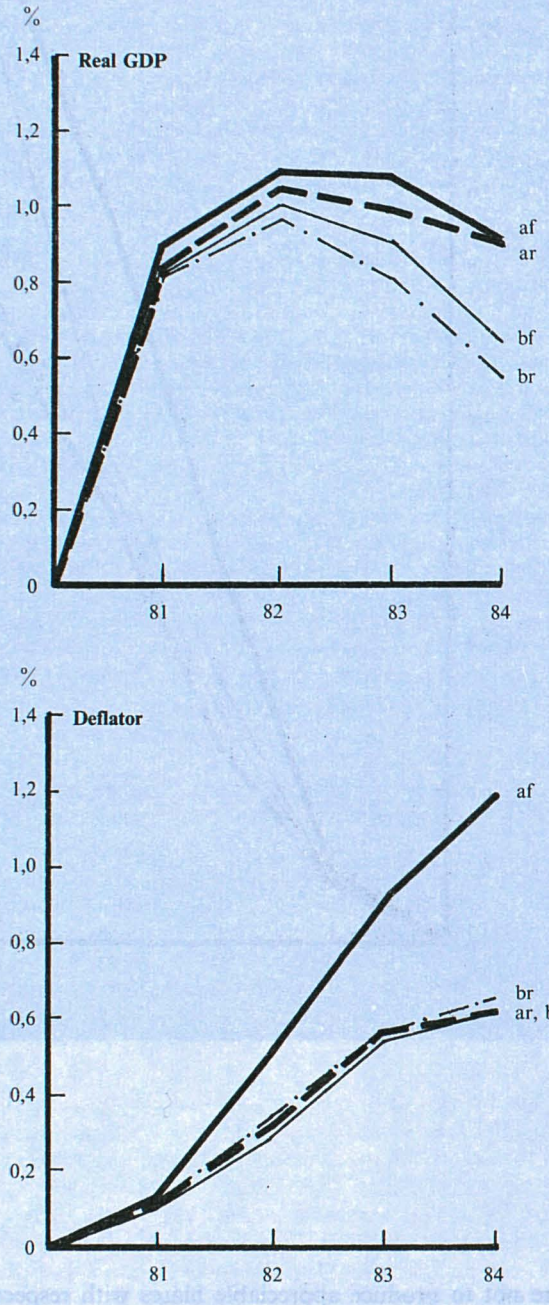
The variables also throw light on the fundamental implications of the environments in which the shocks take place. For instance, in the case of expansionary measures, the most favourable results are obtained with concerted action under an accommodating monetary policy and a fixed exchange rate, provided that the pressures on prices are kept under control, which may, however, be more difficult to realize.

More generally, we find that empirical models often do not completely reflect the theoretical reasoning based on the so-called Hicks-Hansen-Mundell generalized IS-LM diagrams on the crowding-out effect of public expenditure or the comparative effectiveness of budgetary and monetary policies in situations of fixed and floating exchange rates.

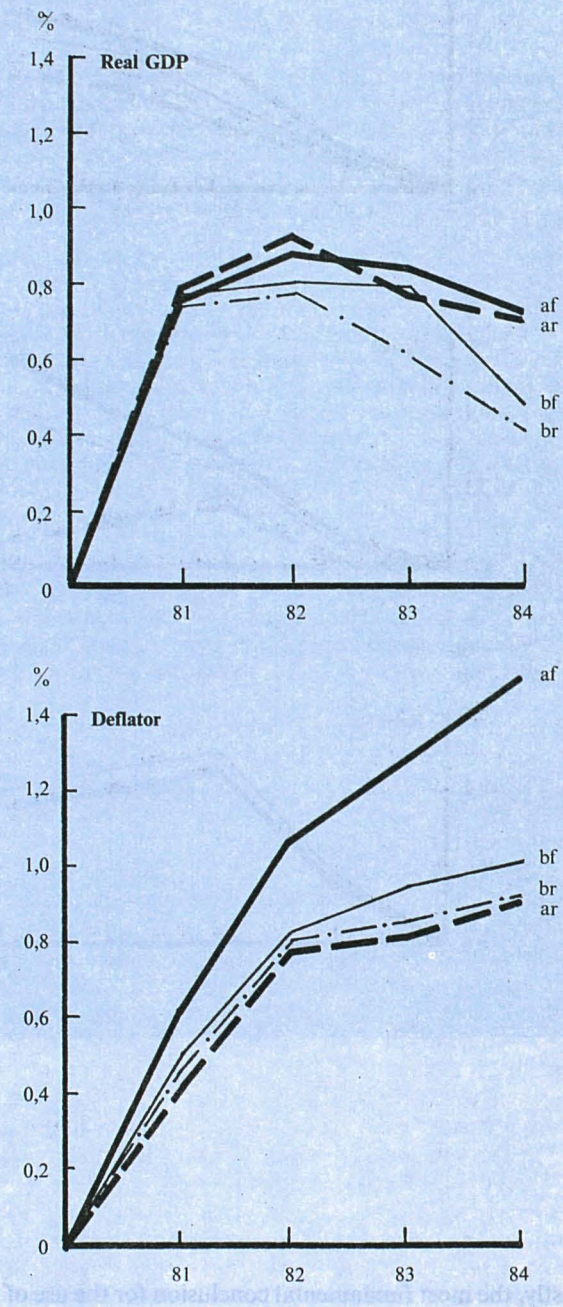
GRAPH 8.2: **Comparative dynamic profile of the multipliers linked to an increase in public investment equal to 1% of 1981 real GDP — Average of the four Eurolink countries**

(a = accommodating monetary policy; b = non-accommodating monetary policy; r = fixed exchange rate; f = flexible exchange rate)

Case 1: **Concerted action**

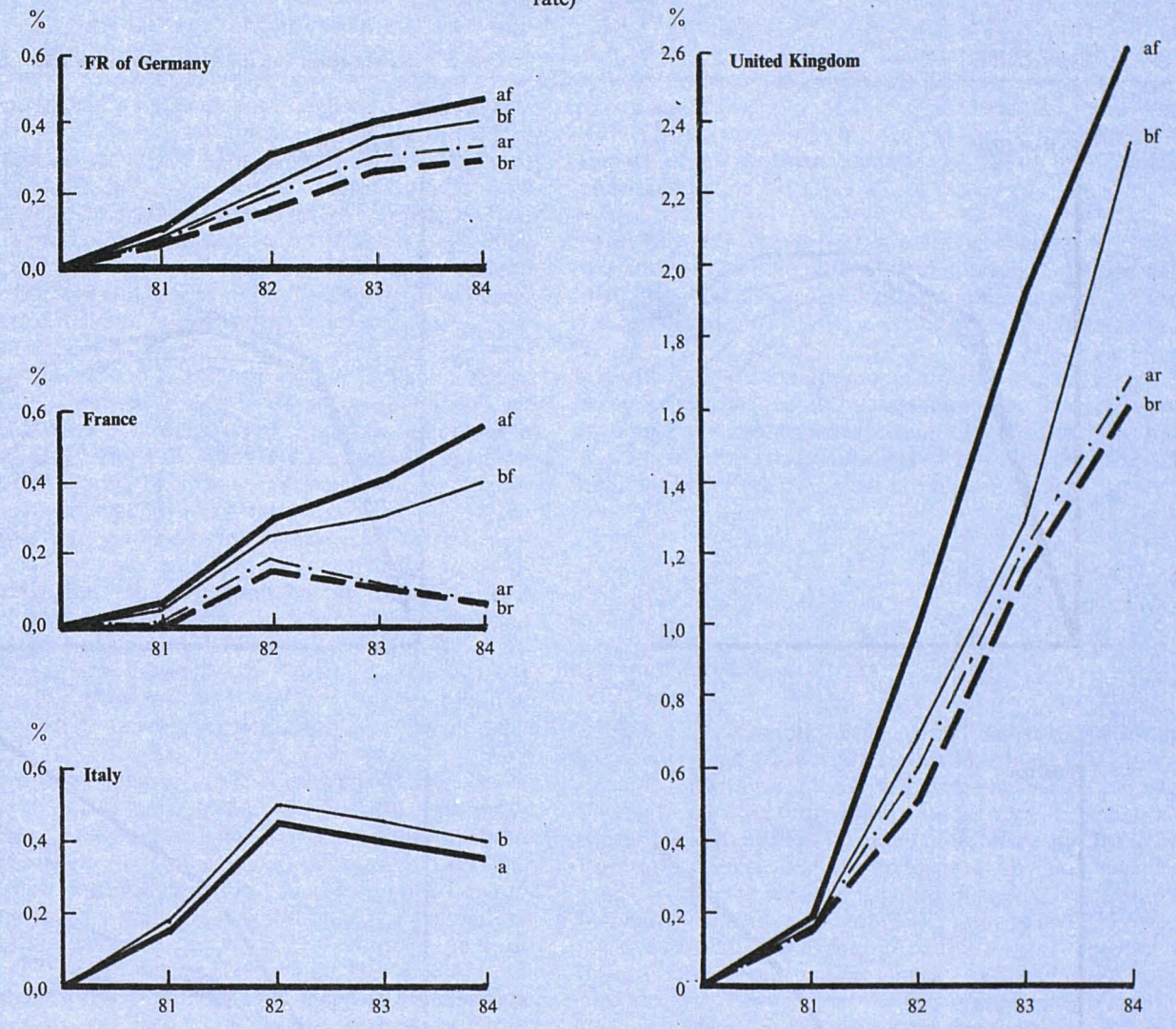


Case 2: **Concerted action with rise in the price of raw materials**



GRAPH 8.3: **Comparative dynamic profile of the multipliers linked to an increase in public investment equal to 1% of 1981 real GDP — Impact on GDP price**

(a = accommodating monetary policy; b = non-accommodating monetary policy; r = fixed exchange rate; f = flexible exchange rate)



Lastly, the most fundamental conclusion for the use of these models seems to be that they will always gain by being used in a multinational linkage (even a very simplified one) if they are not to produce appreciable biases with respect to the multipliers for foreign trade, the inflation rate and the interest rate.

The Eurolink model

Two opposite approches may be adopted in modelling the economies of the European Community member countries: either a set of 10 *ad hoc* models is built *ex nihilo*, giving them an identical structure and using a harmonized Community data base, or the national models considered to be the most representative or just the most accessible are brought together and interlinked by a set of bilateral international trade flows.

Each of the two approaches has advantages and disadvantages which would take too long to go into here but which, in fact, make them complementary rather than antagonistic. The Commission uses both approaches, the 'centralized' approach being represented by the Comet model and the 'decentralized' approach by the Eurolink model.

Eurolink does not cover the entire Community; for essentially logistical reasons, it groups only the four largest countries, Germany (the Sysifo model—University of Hamburg), France (the Metric model -INSEE) Italy (the Prometeia model—University of Bologna) and the United Kingdom (HM Treasury model). The system in addition includes the United States component of the Federal Reserves multinational model (MCM) and a linkage block connecting the five countries with each other and with the rest of the world via bilateral flows and prices.

All these models are large and cover the real and monetary sectors of the economy at a far finer level of disaggregation than is possible with Comet. They therefore represent a very valuable information base on the structure of the economies considered, which can be used both for short-term forecasting (the system is based on quarterly data) and for simulation analyses of the effects of economic policy measures.

Nevertheless, despite their considerable size, the Eurolink models are still no more than a considerably simplified representation of the economy as a whole. Consequently, the results obtained will be influenced by simplifying assumptions made by the authors in the light of the underlying theoretical options, for example, the degree to which the monetary sector is integrated into the behaviour of the real economy.

To take just a few examples, it will be seen that the Treasury model strongly reflects the effect of crowding out private expenditure under an expansionary budgetary policy; this affects the model's responses although it cannot necessarily be claimed that such crowding out effects are really stronger in the United Kingdom than elsewhere, all other things being equal.

Similarly, the interest rate/inflation rate relationships will depend on how the 'user cost of capital' variables are defined and how they are taken into account in determining prices. In the Treasury model, a two percentage point increase in the Treasury Bill rate works through to an identical rise in mortgage rates, which itself works through to a 0,7 point rise in the retail price index. Raising the interest rate therefore accelerates inflation despite negative effects on output and employment. In the other models, by contrast, this mechanism is either ignored or treated less directly, producing a deceleration of inflation rates when the interest rate is raised.

The international comparison of economic policy simulations is therefore still very difficult because, despite the model's mathematical objectivity, it is based on theoretical economic options which, while ensuring its internal coherence, may make it incomparable with other models.

Annex

This annex gives a sample of the Eurolink system's multipliers. Table 1 shows the relative differences between the 1981-84 baseline solution and the levels obtained as a result of economic policy shocks for real GDP (1975 prices) and the GDP price deflator.

The multiplier values correspond to measures taken in isolation in each country, in the linked model, under a non-accommodating monetary policy, and under a fixed exchange rate.

The modifications of the multipliers' dynamic profile in the case of joint measures and/or floating rates are presented in graphic form.

The following abbreviations are used to identify the shocks:

+ID: + 1% of nominal GDP to direct taxes;

+II: + 1% of nominal GDP to indirect taxes;

+CS: + 1% of nominal GDP to social security contributions;

+G: + 1% of real GDP to public consumption;

+VG: + 1% of real GDP to public investment;

+TS: + 1% of nominal GDP to social transfer payments;

−W: − 2% to the average growth rate of nominal wages;

+is: + 2% to short-term interest rates;

−Po: − 20% to the price of crude oil:

Dev: 10% devaluation against the dollar;

Rev: 10% revaluation against the dollar.

Table 1

Multipliers of GDP and of the GDP deflator

GDP	Germany				France				Italy				United Kingdom			
	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984
+ ID	−0,74	−1,35	−1,24	−0,55	−0,08	−0,26	−0,31	−0,28	−0,21	−0,38	−0,42	−0,35	−0,39	−0,59	−0,60	−0,48
+ II	−0,58	−1,02	−0,95	−0,54	−0,42	−0,40	−0,39	−0,52	−0,18	−0,49	−0,66	−0,63	−0,36	−0,69	−0,79	−0,68
+ CS	−0,07	−0,39	−0,63	−0,46	−0,17	−0,41	−0,67	−0,78	−0,19	−0,58	−0,71	−0,73	−0,17	−0,48	−0,61	−0,49
+ G	1,12	1,33	1,28	1,02	1,05	1,37	1,33	1,35	0,52	0,55	0,50	0,42	0,94	0,99	0,73	0,46
+ VG	1,15	1,23	0,98	0,59	1,18	1,01	0,95	0,94	0,72	0,89	0,95	0,94	0,84	0,90	0,59	0,29
+ TS	0,76	1,39	1,40	0,74	0,94	1,51	1,40	1,31	0,21	0,38	0,42	0,35	0,29	0,34	0,16	0,00
− w	−0,04	−0,02	−0,03	−0,11	−0,40	−0,70	−0,50	−0,40	0,03	0,15	0,33	0,52	−0,06	0,17	0,66	1,12
+ is	−0,18	−0,42	−0,49	−0,30	−0,04	−0,12	0,04	0,10	−0,03	−0,13	−0,16	−0,19	−0,04	−0,12	−0,26	−0,24
− Po	0,10	0,49	0,80	0,75	0,24	0,48	0,78	1,01	0,36	1,23	1,63	1,68	0,02	0,14	0,38	0,49
Dev	0,08	0,15	0,56	1,05	1,01	1,93	1,73	1,36	1,61	1,80	1,62	1,77	0,60	1,06	1,06	0,67
Rev	−0,04	0,09	−0,23	−0,97	−0,98	−2,04	−1,93	−1,44	−1,86	−2,17	−1,98	−2,19	−0,55	−0,93	−0,90	−0,59
GDP deflator	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984
+ ID	−0,03	−0,20	−0,40	−0,40	0,00	−0,04	0,04	0,04	0,02	−0,03	−0,08	−0,10	0,03	0,15	0,06	−0,12
+ II	0,41	0,49	0,39	0,41	1,03	1,42	1,73	2,02	0,82	1,17	0,96	0,80	1,03	1,15	1,06	0,80
+ CS	0,30	0,75	0,79	0,70	0,57	1,39	1,96	2,46	0,27	0,32	0,30	0,28	0,65	0,95	0,81	0,49
+ G	0,15	0,25	0,35	0,33	0,76	0,80	0,92	0,90	0,14	0,37	0,35	0,35	0,11	0,55	1,11	1,56
+ VG	0,05	0,20	0,29	0,23	0,01	0,18	0,11	0,06	0,28	0,50	0,45	0,40	0,15	0,60	1,21	1,68
+ TS	0,02	0,19	0,39	0,40	−0,12	−0,19	−0,13	−0,14	−0,02	0,03	0,08	0,11	0,10	0,37	0,68	0,92
− w	−0,36	−1,28	−2,39	−3,54	−0,60	−1,30	−1,92	−2,39	−0,14	−0,45	−0,77	−1,08	−0,76	−1,91	−3,09	−4,21
+ is	0,00	−0,03	−0,08	−0,10	−0,03	−0,10	−0,16	−0,11	−0,04	−0,08	−0,09	−0,06	0,12	0,30	0,36	0,30
− Po	−0,25	−0,66	−1,22	−1,48	0,69	−0,28	−1,19	−2,15	−0,42	−1,09	−0,74	−0,76	−0,85	−1,91	−2,45	−2,51
Dev	0,22	0,67	0,73	0,96	0,29	1,37	3,59	5,77	0,38	2,72	2,93	2,74	0,33	2,47	4,04	5,45
Rev	−0,10	−0,45	−0,44	−0,66	−0,19	−1,31	−3,37	−4,72	−0,20	−2,45	−2,65	−2,40	−0,24	−1,99	−3,37	−4,36

Table 2

Public investment multiplier for different variants

a: accommodating monetary policy
r: fixed exchange rates
b: non-accommodating monetary policy
f: floating exchange rates

(average of the four Eurolink countries as a percentage of shift from the baseline simulation)

Real GDP	Isolated action country by country [1]				Concerted action four European countries				Concerted action, four European countries plus the United States (impact on the four European countries)				Concerted action, five countries, with increase in raw material prices (impact on the 4 European countries)			
	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984
af	1,01	1,18	1,16	1,06	1,09	1,30	1,28	1,32	1,22	1,56	1,57	1,67	1,07	1,27	1,27	1,36
ar	1,04	1,11	1,04	0,99	1,14	1,24	1,19	1,24	1,27	1,46	1,46	1,57	1,10	1,21	1,19	1,30
bf	1,04	1,09	1,01	0,78	1,12	1,20	1,11	0,92	1,25	1,42	1,36	1,17	1,08	1,18	1,19	0,97
br	1,01	1,04	0,87	0,67	1,11	1,16	1,00	0,84	1,24	1,37	1,18	1,07	1,07	1,14	0,96	0,88
Deflator	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984
af	0,11	0,43	0,78	1,00	0,12	0,51	0,91	1,18	0,13	0,55	1,00	1,32	0,66	1,15	1,40	1,67
ar	0,09	0,26	0,46	0,52	0,10	0,31	0,56	0,61	0,11	0,35	0,61	0,68	0,45	0,87	0,88	1,01
bf	0,08	0,24	0,45	0,52	0,09	0,28	0,53	0,61	0,10	0,33	0,58	0,69	0,55	0,96	1,04	1,14
br	0,09	0,30	0,48	0,55	0,10	0,33	0,56	0,64	0,11	0,38	0,61	0,72	0,45	0,91	0,92	1,02

[1] These figures are purely theoretical indicators, calculated as the weighted average of the effects, on each country, of individual actions.

Table 3

Public investment multipliers for various aggregates

(increase by 1% of real 1981, ex-ante)

Variables	Germany				France				Italy				United Kingdom			
	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984	1981	1982	1983	1984
Private consumption	0,16	0,42	0,48	0,36	0,13	0,20	0,18	0,18	0,36	0,61	0,74	0,70	0,13	0,28	0,22	0,14
Private investment (plant and equipment)	2,90	4,11	1,50	−2,09	3,52	1,66	1,75	0,85	0,30	2,05	3,71	4,65	1,07	2,14	1,37	0,06
Current balance (% of nominal GDP) [1]	−1,78	−2,91	−2,88	−1,83	−1,30	−0,81	−0,43	−0,56	−3,06	−4,65	−5,87	−6,89	−0,44	−0,69	−0,65	−0,61
Total employment	0,47	0,60	0,61	0,47	0,27	0,44	0,44	0,44	0,26	0,42	0,47	0,48	0,30	0,65	0,54	0,27
Long-term interest rate [1]	0,29	1,08	1,28	0,98	0,30	−0,20	−0,13	−0,15	0,16	0,53	0,52	0,54	1,07	2,12	2,88	3,58
Wage-cost rate	−0,54	−0,26	−0,06	0,07	−0,03	0,09	0,27	0,35	0,05	0,22	0,22	0,19	−0,32	0,67	1,66	2,24
Net lending, public authorities (% of nominal GDP) [1]	−0,82	−0,76	−0,72	−0,66	−0,90	−0,83	−0,78	−0,70	−0,88	−0,78	−0,66	−0,68	−0,70	−0,70	−0,60	−0,80

[1] Expressed as absolute difference between shock and base case, in percentage points.

Commission report of 6 July 1983 on budget discipline and economic convergence, and on restructuring public expenditure in favour of productive expenditure

Commission communication of 20 April 1983 on financial integration

Commission communication of 24 May 1983 on the promotion of the international role of the ECU

Commission report on budget discipline and economic convergence, and on restructuring public expenditure in favour of productive expenditure

Brussels, 6 July 1983

Part I

Budget discipline and economic convergence

I. Control over public expenditure

In its communication of 1 July 1982 on budget discipline and economic convergence [1] the Commission stressed that, to improve convergence of economic trends in the Community, it was important to increase the degree of control over the main budget headings. In particular, it adverted to the need for a reduction, or at least a stabilization, in net borrowing, a slower rate of expansion of public expenditure, adjustment of taxation and social security contributions, and more frequent recourse to increases in public service charges and licence fees.

It emphasized, moreover, that the structure of public expenditure should be modified in favour of budget appropriations intended to expand production capacity.

Although the estimates for general government budget outturns are still only provisional, they show encouraging results; nevertheless, they imply that more vigorous efforts are still needed in certain areas.

Expenditure in cash terms has increased much less than in 1982, but there has also been a pronounced decline in inflation rates, In real terms, public expenditure by main items has contracted only in three Community countries: the Federal Republic of Germany, Belgium and Ireland. In most of the Member States, however, the expansion in cash terms has been lower than planned, which shows that the general approach to budget management has been restrictive.

The trend of budget resources illustrates clearly the influence of cyclical weakness: not only have they expanded less than in 1982, but they have even been lower than initially estimated (except in Denmark, Italy and the Netherlands), in spite of increased tax rates and higher thresholds in some countries.

Borrowing requirements at budget level have been consistent with the Commission's recommendations, having contracted in all the countries with external equilibrium problems. However, the outturns are less favourable than the initial estimates in Luxembourg, the Netherlands and the United Kingdom.

[1] COM (82) 422 final.

In all the Member States except Denmark and the United Kingdom, where the Treasury actually managed to consolidate part of the floating public debt, Treasury financing has generated considerable liquidity. Public borrowing increased much faster than the money supply in Belgium, France, Ireland, Italy and the Netherlands.

In spite of the progress made, foreseeable outturns for 1983 still give cause for serious concern: borrowing requirements (defined broadly as the deficit of general government or the public sector including loans, advances and purchases of equity) as a percentage of GDP range from about 10% in the Netherlands to 18,5% in Ireland through 11,5% in Denmark and Greece, 14,5% in Belgium and about 16% in Italy. With these orders of magnitude, interest on the public debt represents a very heavy burden, particularly in just those countries that have best managed to control inflation, where the rate of growth of nominal GDP—and consequently tax revenue—is below 10%.

To reduce the deficit, the only alternative to increased taxation is to reduce certain items of expenditure, and often it is investment expendiure that is crowded out.

II. Budget procedure and management

In its communication to the Council of 1 July 1982, the Commission proposed guidelines for improving budget management and adapting certain procedures, taking the view that the exercise of budgetary powers in accordance with the main economic equilibria is an essential factor in improved convergence of economic trends.

The discussions that have been held by several bodies, in particular the Economic Policy Committee, and the studies undertaken on this subject since last summer, have concentrated on two main areas: the monitoring and adaptability of public expenditure, and medium-term budget planning.

1. *The monitoring and adaptability of expenditure*

All the Member States organize periodic monitoring of the management of budget appropriations, but methods obviously differ according to national budget systems.

The parliamentary voting procedure could, however, be speeded up in most of the Member States, and take place more frequently both to improve information on implementation of the budget and to avoid the need for financing from advances to be ratified subsequently by the legislature, or to prevent excessive financing from unlimited appropriations. The technique of using reserve funds can avoid the need for

too frequent recourse to parliamentary approval and make for more flexible management, but strict rules must govern the use of such funds so that available appropriations are not used up too rapidly.

When appropriations are carried over from one year to the next, this can weigh very heavily on the authorities' commitments, as in Italy; such operations could be limited to cases where a project takes several years to complete, and apply only to commitments that are strictly necessary.

Monitoring would also be improved, and overshooting less frequent, if the actual preparation of the budget were organized on the basis of more accurate assessments. A large proportion of budget appropriations depends on the implementation of existing laws, and if savings are to be made here, amendments to these laws must be prepared in good time, or incorporated in the approval of the draft budget. It would be particularly useful to provide an opportunity for reconsidering the application of indexation mechanisms that apply to certain categories of expenditure in the light of the economic situation and financing possibilities.

The most appropriate method for containing expenditure under other headings is systematic review, every year. This procedure seems more efficient than the frequent method of applying a linear reduction to proposals from the various government departments.

Changes in the scope of application (where items are removed from or reincorporated in the budget) are usually a logical consequence of political choices by the executive or legislativle authorities. For the sake of clarity and easier monitoring, the budgetary consequences of such changes should be made explicit; a document listing items of expenditure with an indication of the extra-budgetary fund involved would also be helpful.

National laws, finally, are not always strict enough to ensure that expenditure by social security funds and local authorities is properly monitored, with all due respect for the autonomy of the authorities concerned.

In the countries where expenditure on social protection is not an integral part of the general budget, such expenditure is frequently kept in check by imposing the requirement for a balanced budget on the sector concerned while maintaining, although strictly limiting, the contribution from the central government budget, As to local authorities, access to the financial market is supervised in all the Member States, but it is more difficult to keep the current account in line with the budget adopted because of the time required for gathering information on its implementation.

2. *Medium-term public finance planning and budgetary norms*

All the Member States are anxious to situate the annual approval of public budgets in a context of medium-term financial planning, although planning is formally organized only in Denmark, Germany, Italy, the Netherlands and the United Kingdom.

Reference to a medium-term plan has numerous advantages: in particular, it makes for a more accurate assessment of the budgetary situation in the prevailing economic context, for evaluations of the permanent volume of expenditure resulting from new initiatives, for the establishment of links with medium-term monetary planning and thus for more consistency between monetary and budget policies.

However, it may have disadvantages if estimated expenditure is regarded by the prospective recipients as a definite promise rather than as a provisional estimate that should be flexible and adaptable to circumstance.

Generalized financial planning in the Community would be a potential means of ensuring greater convergence, for it would make it possible to measure more precisely the medium-term consequences of initial budget and monetary policies, thus indicating whether certain changes were suitable. If the extension of such planning to all Member States is to be useful, it should be organized with reference to uniform basic notions and apply to revenue as well as to expenditure.

Similarly, it is worth while to examine the possibility of adopting certain benchmarks for assessing the medium-term trend of the budget position, In its communication to the Council of 1 July 1982, the Commission pointed out that the budget situation appeared more satisfactory in 1982 in the Member States that at least managed to achieve balance on current transactions. However, for reasons of short-term regulation in particular, it might be too severe to impose as a rule that current expenditure and revenue must be in balance. But it would perhaps be worthwhile to check how far the adoption of the notion of a permanent budget position, already used to some extent in Germany, the Netherlands and the United Kingdom, for example, could contribute to improving the convergence of budget policies in the Community.

III. Financing criteria

In its communication of 1 July 1982, [1] the Commission suggested that certain types of financing should be avoided

[1] COM (82) 422.

Principal public finance aggregates [1]

Table 1: General government expenditure

	As % of GDP			Percentage change				
	1970	1980	1983	1981	1982	1983		
						X-82	I-83	V-83
B	36,5	53,9	60,0	12,9	10,3	9,0	—	6,1
DK	43,1	58,6	61,7	16,4	15,8	11,0	—	11,8
D	37,6	46,9	49,4	6,8	4,5	5,1	—	3,4
GR	29,1	35,6	42,1	(33,5)	(24,4)	24,1	—	25,7
F	38,9	46,2	52,2	18,5	18,2	13,3	—	12,6
IRL	40,1	55,2	59,2	27,2	23,1	17,5	—	10,5
I	33,4	46,3	55,5	30,0	22,8	19,6	—	20,4
L	33,4	57,0	61,4	9,4	11,8	8,8	—	12,2
NL	44,7	57,9	63,8	7,2	7,9	4,8	—	5,8
UK	39,4	44,3	46,0	12,5	9,6	8,6	—	8,9
EC	37,9	47,1	52,0	14,7	12,0	10,8	—	9,5

Table 2: General government receipts

	As % of GDP			Percentage change				
	1970	1980	1983	1981	1982	1983		
						X-82	I-83	V-83
B	35,4	44,8	48,3	6,1	11,6	10,2	—	8,3
DK	46,1	52,5	52,2	8,0	12,0	10,8	—	11,2
D	37,9	43,5	45,6	4,2	4,8	4,9	—	3,7
GR	26,8	30,2	35,6	22,1	39,5	26,9	—	26,7
F	39,8	46,6	49,1	12,4	16,2	13,4	—	11,8
IRL	36,1	42,0	46,0	23,7	23,9	20,5	—	16,7
I	30,6	37,8	44,2	23,4	23,7	22,1	—	23,3
L	36,3	55,7	58,4	7,5	11,1	8,5	—	8,6
NL	43,9	54,2	57,0	6,3	5,7	5,3	—	5,5
UK	42,0	40,7	43,8	15,4	11,9	9,7	—	7,6
EC	38,2	43,6	46,6	11,2	12,1	11,1	—	9,4

Table 3: General government net lending (+) or borrowing (−), as % of GDP

	1970	1980	1981	1982	1983		
					X-82	I-83	V-83
B	−1,1	−9,4	−13,3	−12,7	−12,1	−12,3	−11,7
DK	3,0	−5,9	−7,1	−8,9	−9,6	−9,7	−9,5
D	0,3	−3,5	−4,0	−3,9	−4,1	−4,1	−3,8
GR	−2,3	0,4	−10,1	−6,4	−8,6	−8,9	−6,5
F	0,9	0,0	−1,5	−2,7	−3,0	−3,1	−3,1
IRL	−4,0	−12,8	−15,4	−15,8	−15,1	−13,0	−13,2
I	−2,8	−8,4	−11,9	−11,9	−11,0	−10,5	−11,3
L	2,9	−1,8	−0,7	−1,0	−1,0	−1,6	−3,0
NL	−0,8	−3,4	−4,6	−6,4	−5,5	−6,2	−6,8
UK	2,6	−3,5	−2,1	−1,7	−0,5	−0,9	−2,2
EC	0,3	−3,5	−5,2	−5,3	−4,9	−5,0	−5,4

[1] The definitions used are national accounts definitions. Figures do not necessarily add up because of rounding.
1. Expenditure: current and capital expenditure excluding loans, advances and equities.
2. Receipts: direct and indirect taxes, social security contributions, other current resources and consumption of fixed capital.
3. Net lending or borrowing: balance of receipts-expenditure (2-1).

Sources: Eurostat and services of the Commission.

or at least limited; direct financing of the Treasury by the central bank; monetization of public debt securities by the banking system; compulsory subscription to public debt securities on favourable terms; index-linked public debt; the issuing of securities with very short maturities (j.e. shorter than some specified minimum); massive recourse to short-term issuing, public borrowing abroad and Government guarantees for such borrowing by public-sector and private-sector undertakings.

When the Monetary Committee met on 15 December 1982, it expressed its approval of these principles.

In fact, some of these practices are of limited application. Index-linked government securities exist only in Ireland and the United Kingdom, and are subject to very strict terms that confine them to certain categories of savers. Favourable terms for public debt securities, and the issue of very short-term certificates are extremely rare.

Central bank financing of the Treasury is kept within certain limits; these limits have been widened in recent years in several countries (e.g. Belgium, Greece, France, Italy, Netherlands). [1]

The monetization of public debt securities and the issuing of short-term loans are more frequent, and constitute an important source of financing in Belgium, Greece, France, Italy and Ireland.

With the steep increase of public deficits, national capital markets have not managed to satisfy demand—sometimes despite substantial monetary financing of the public debt; recourse to foreign markets has increased particularly in Belgium, Denmark, Ireland, Italy and to a lesser extent France. Denmark has outstandingly increased public borrowing abroad to finance the current account deficit of the balance of payments.

[1] In some cases the adaptation is automatic.

PART II

The restructuring of public expenditure in 1983

The joint Council meeting (Ecofin and Social Affairs) of 16 November 1982 concluded that, in 1983, 'in connection with the annual approval of budget guidelines and on the basis of a Commission report, the Council (Economic and Financial Affairs) would undertake an analysis of Member States' public sector budgets in order to review the evolution of productive public expenditure', taking account however of 'the risk which could arise if all the Member States undertook, to the same extent, restrictive measures with regard to public expenditure, irrespective of their levels of inflation, real interest rates or their financial situations'.

The present report has been drawn up to meet this request. It has been prepared with the active help of the Economic Policy Committee and in particular its working party on public finance.

1. *Introduction*

In recent years, the adaptation of economic structures in response to the changes that have occurred, particularly with regard to growth rates, world trade and technology, have become a more pressing cause for concern among those responsible for economic policy, who had previously concentrated on the problem of the appropriate response to short-term developments by means of traditional demand management measures. The emphasis of budgetary policy has accordingly shifted away from the control of the main budgetary aggregates and the balance between revenue and expenditure.

If growth potential is to be improved by encouraging structural adjustment, then the main budgetary aggregates must be reorganized in such a way as to promote the best possible development of production capacity, with regard both to capital and to labour.

The restructuring of budgetary resources was dealt with in a Commission communication on 'Tax and financial measures in favour of investment' (COM(83)218 final of 18 April

1983), which analysed existing arrangements and put forward suggestions for measures that would have a favourable impact on the magnitude and structure of productive potential.

This report considers, from a similar viewpoint, the possibilities for adapting the structure of public expenditure and analyses, against this background, the efforts made by the Member States within the framework of the public sector budgets for 1983.

2. *Restructuring public expenditure and the possibilities for future growth*

It is generally accepted that the budget of the public sector can contribute in a variety of ways (direct investment, capital transfers, loans, equity purchases, tax concessions) to increasing productive potential, improving its structure, and improving productivity and efficiency in the private sector. During a recession the selection of budgetary priorities becomes particularly difficult especially when the question is whether public expenditure of a structural kind (geared to future growth), should be preferred to expenditure in support of demand. To the extent that the latter results from the operation of the automatic stabilizers, the choice may be temporarily avoided; but eventually in the medium-term the need to control the balance between revenue and expenditure imposes itself.

With the considerable slowdown in overall economic growth since the mid-1970s the restructuring of public expenditure in favour of so-called productive expenditure implies a deliberate reduction in other categories of expenditure; there are at least three reasons for this:

(i) The growing share of expenditure accounted for by the operation of the automatic stabilizers;

(ii) The increase in the relative share of expenditure required to service public sector debt, itself a result of the growing total of accumulated public sector deficits;

(iii) The limits on public sector deficits imposed by anti-inflationary policies while, at the same time, the elasticity of tax revenue is on a downward trend.

The stabilization of the financial situation may even mean reducing the overall total of public expenditure; if it does, any increase in that part of public expenditure in favour of increasing productive potential, will require even more vigorous reductions elsewhere.

The authorities thus find themselves confronted to an extent which varies from country to country according to their economic circumstances, by a double constraint made up of:

(i) The need to favour the most productive forms of public expenditure with a need to promoting economic development over the longer term;

(ii) The near impossibility of reducing the part taken up by other types of expenditure, other because of their very nature (public sector debt) or because of the social costs that would result from such a move.

3. *Policies implemented in 1983*

A. Problems of definition

Macroeconomic analysis alone is insufficient to identify, *a priori*, the items of public expenditure that will contribute to improving or extending productive capacity. Most categories of expenditure have widely differing effects in this context, and only microeconomic analysis, which takes account of profitability, can supply a clear answer.

As it is impossible in practice to analyse each item of expenditure individually, a more approximate analysis must suffice, concentrating on the main areas of expenditure that are assumed to correspond most closely to the methodology under study.

Comparison with the development of other categories of expenditure may be useful to assess progress. It is apparent even from a cursory examination that the usual distinction in the national accounts between current and capital expenditure is unsuitable for the purposes of this study. Some items of current expenditure contribute to improving or maintaining productive potential, while some items of capital expenditure make a direct contribution to public or private consumption.

After considering the different options in detail, the Commission departments have adopted a framework for classification intended to monitor the trend of public expenditure in a practical way (breaking it down into capital expenditure, consumption expenditure and other current expenditure), by identifying:

(i) Items of expenditure that improved the productive capacity and/or productivity of resident undertakings in the private and public sectors;

(ii) Items of expenditure that increase the productive capacity of government departments;

(iii) Other expenditures, distinct from transfers (both current and capital) abroad, and interest on the public debt, that deserve separate treatment.

This classification is tabulated in Annex 1, and provides a framework that makes possible an approximate assessment

of the contribution of public expenditure to the growth of production potential and improvement of productivity on the one hand or public and private consumption on the other. The experts from the Member States have provided statistical information based on, although not strictly adhering to, this framework.

B. The main thrust of national policies and restructuring

A number of common features are apparent:

1. The promotion of productive public expenditure is a major objective of budgetary policy everywhere;
2. However, adoption of this general aim does not always lead to the required result because the aggregate volume of in public expenditure is subject to the constraint of the deficit; some member countries even consider that the best policy is to reduce the share of public expenditure in national income;
3. Private and public investment is often complementary so that relative weakness in one often leads to a decline in the other;
4. Infrastructure investment depends very much on population trends, which may lead to an increase or a decrease in its relative share, depending on the country concerned;
5. Some categories of expenditure, especially transfer payments to households are still on a strongly rising trend, in particular because existing legal arrangements tend to bring about such a result;
6. In more and more countries the burden of the public debt is so heavy that other categories of expenditure, and especially so-called productive expenditure, are being crowded out.

The role of the budget as an instrument for improving productivity and productive potential thus depends as much on the judicious choice of certain forms of action as on alternative spending allocations within clearly defined budgetary limits; those allocations themselves are subject to the adverse effects of the almost inevitable expansion of certain items of expenditure.

C. Restructuring policy in the Member States

Belgium: The government has given priority to placing the budget on a sounder footing by aiming for a major reduction in net borrowing by 1985. The restructuring of budget expenditure is thus subject to the pressing constraint of an overall reduction.

In practice, there is no room for manoeuvre to increase the efforts to stimulate the economy, with respect to productive expenditure, in the short term (until 1985-86).

Belgium's efforts are concentrating, therefore, on improving the utilization of public investment programmes by favouring, in the allocated programmes, particular expenditures of a productive nature. At best the level of such expenditures could be stabilized in real terms (maximum forecast growth 6,5% per annum in current prices).

Formerly, the use of investment programmes was, above all, subjected to quantitative modifications as an instrument of short-term economic policy.

Belgium has made extensive use of budgetary expenditure to encourage and stimulate initiatives of the private sector and of companies, in favour of productive investment, with various priorities (energy-saving, contribution to risk capital, etc.).

Denmark: One of the main aims of the government that took office in October 1982 is to reduce the public sector budget deficit and increase the scope for the private sector in the economy, whilst giving priority to public expenditure that will tend to improve the structure of the economy. The drive to put the budget on a sounder footing involves a considerable decline in the rate of growth of public expenditure, which is not always possible without a reduction in real capital expenditure.

Nevertheless, aggregate expenditure for 'structural improvement' continues to increase in real terms (by about 2,5%) in 1983, after a large increase in 1982, while expenditure for traditional purposes, and on aid to households remains stationary.

In December 1982, the government launched a programme for the recovery of productive investment that was intended, in particular, to change some of the priorities of education and research,to carry out infrastructure investment, and to relax rules applying to enterprises. The programme also included changes in tax legislation and market arrangements to promote risk capital.

Germany: The structure of public expenditure has deteriorated, mainly because of increasing unemployment and weaker public investment especially that of local authorities, which are suffering from the effects of a reduction in their tax revenues.

The restructuring of public expenditure in favour of productive expenditure is considered to be a priority.

In 1983, the declining trend of investment may at least be halted, while the accent is on strictly limiting the expansion of

expenditure on public sector employees and on social transfer payments. This policy will be continued in 1984 and reinforced by changes in the tax regime that involve using the increase in VAT applicable from 1 July, to reduce taxes that fall specifically on enterprises, so as to gear tax arrangements to the promotion of innovation and investment.

Greece: The development of public investment is a very important feature of the 1983 budget (it increases by 48%). The main effort involves infrastructure investment in transport, education and regional development.

This approach will, in 1983, reverse the tendency for the share of investment to decline. However, the 1983 budget implies a relative reduction in subsidies (particularly to agriculture), aggregate wages in the civil service, and transfers to the social security system. As in other Community countries, the burden of the public debt is expanding rapidly.

France: In 1983, in line with the efforts undertaken in 1982, the accent has been on expanding investment expenditure strongly (22%) [1] combined with the restraining of operating expenditure (8.4%). This policy is aimed particularly at developing the productive sector by encouraging research, improving the effectiveness of aid to private industry, and providing financial support for the newly-nationalized industrial groups. This is accompanied by a major budgetary effort in favour of vocational training. On the other hand, expenditure on public sector services has been reduced by 8% in real terms, and in 1983, State intervention will be systematically reviewed.

Ireland: For a long time, major efforts have been made to expand public investment and investment by firms in the public sector. However, the correction of the public sector deficit has now been given absolute priority. Moreover, in view of the growing burden of public sector debt and of unemployment, and the weakness of private investment, the share of 'productive ' public expenditure declined in 1983. The government is still doing its best to give this type of expenditure priority in the allocation of budget resources.

Italy: The structure of public expenditure is considerably distorted by a substantial increase in interest payments on the public debt (85% in two years). However, the government has confirmed, in the 1983 budget, the reversal of trends established in 1981-82, when public capital expenditure began once again to expand faster than current expenditure. The main accent is on the development of housing, road networks, means of transport and the southern regions, while aid directed towards the development of technology, in small and medium-sized firms, has expanded sharply.

The uncertainty due to forthcoming elections and the formation of a new government could, however hamper the programme.

Luxembourg: The government reinforced its strict position in 1983, in view of the outlook for zero economic growth in the medium-term, which will affect future resources. The restructuring of expenditure is thus hampered by the strict limits placed on the development of budgetary expenditure overall. Nevertheless, the specific efforts to stimulate economic growth, ensure a satisfactory level of employment and bring about structural transformation in the economy have been reinforced, in particular through direct and indirect assistance to the consolidation and diversification of industry and to research and innovation.

A budgetary programme for the restructuring and modernization of the Luxembourg steel industry and for maintaining the competitiveness of the economy was recently drafted by the government within the framework of negotiations with the two sides of industry.

The Netherlands: The large increase in the public deficit is forcing the authorities to reduce public expenditure severely in relation to what it would have been had no changes in legislation occurred. Most of the savings come from salaries, expenditure on health and social transfer payments. The government attaches great importance to strengthening the position of the private sector, and regards stabilizing the burden of taxation and reducing the borrowing requirements, as key elements in this strategy.

In these circumstances, the process of reinforcing productive capacity is essentially a process of negative selection, intended to waive, as far as possible, the application to productive expenditure, of general restrictions. Indeed, the percentage of 'consumption' expenditure increased rapidly, not only during the 1960s and 1970s, but also in recent years.

United Kingdom: The government does not, in principle, regard direct public investment as one of the principal means of promoting economic growth. In the authorities' view, this objective can best be attained by creating a climate conducive to the efficient development of the private sector.

Within the budgetary amount allocated to public investment, priority has been given to productive investment rather than the development of infrastructures.

Morevover, public investment is required to fulfil the criterion profitability (a real rate of return of at least 5%), not only in the nationalized industries,but also in such categories of investment as the development of roads, and means of transport for the benefit of manufacturing industry.

[1] According to payment appropriations in the 1983 Finance Act; however, later decisions have since reduced this figure.

D. Analysis of tendencies observed in 1970-80 and 1982-83 (see attached tables in Annex 2)

The experts from the Member States have provided Commission departments with public expenditure figures broken down into categories according to the framework reproduced in Annex 1.

To avoid excessively laborious research, the best possible grouping under present circumstances has been made; the detailed scheme of classification, the range of application, as well as the reference period may differ from country to country.

For example, some countries have sent figures for the public sector, others for general government, and others for central government.

Consequently, developments over time in individual countries should be considered rather than comparisons between countries.

The instructions for the classification into the 12 boxes in the table were not always strictly adhered to, because sufficiently detailed figures were not always easily available.

A great deal of caution is also required in interpreting the figures.

For example, in category IA, it was not always possible to separate capital transfers or lending to firms to improve productivity and structures; subsidies to cover operating deficits are probably also included. Similarly, in the same category, infrastructure investment to improve general economic conditions is not always separably identified (for example, the building of certain roads may in certain cases not provide sufficient social returns). Similar remarks could be made about research and development expenditure. Some items of expenditure on education and vocational training, on the other hand, may lead to a major increase in the productivity of capital. It would therefore be dangerous to assume that expenditure in category II is always less 'productive' than that in category I. With these reservations, the tables in Annex 2 show two features common to all countries.

From 1970 to 1980, the share of category IA (extension of capacity or the improvement of productivity in private sector and public sector enterprises) in the total has clearly contracted, whereas there has been a relative increase in transfers to households and interest on public debt. In certain countries there has also been a fall, in relative terms, in public consumption expenditure. The available partial information suggest that these trends continued from 1980 to 1983.

4. *Conclusions*

No-one denies that it is useful and opportune to restructure public expenditure in favour of 'productive' spending. This objective does, however, imply that the authorities manage to control the expansion of other categories of expenditure, otherwise it would be impossible in most of the Member States to create the required room for manœuvre.

Annex 1

Classification of the direct effects of public expenditure
by broad economic category

(showing the main items in the relevant boxes)

		Expenditure devoted to expand productive capacity and/or to increase the productivity of domestic private or public enterprises	Expenditure devoted to maintain or expand the productive capacity of the domestic government sector (capacity to provide government services)	Expenditure not having any influence on the domestic productive capacity of enterprises or of the government sector (serving private consumption)	Expenditure not attributable to groups I, II or III
		I	II	III	IV
Capital expenditure (a) investment (b) capital transfers (c) loans, advances and equities	A [1]	— Public infrastructure investment in so far as it promotes productivity and improves the general conditions for the economy — Research investment — Capital transfers and lending to enterprises devoted to improve productivity or structures	— Public investment serving social consumption (schools, hospitals, sports facilities, parks, etc.)	— Capital transfers and lending to enterprises and households for residential construction — Other capital transfers and lending to enterprises not devoted to bring about structural change (aids towards continued operation) — Other capital transfers and lending to private households	— Capital transfers and lending abroad
Expenditure on current purchases of goods and services (government consumption)	B [1]	— R & D expenditure in so far as it is such as to help improve productivity	— Expenditure on government employees — Expenditure on military buildings and equipment — Other consumption expenditures		
Other current expenditure (a) subsidies (b) other current transfers (c) interest on public debt	C	— Interest subsidies and other current transfers to promote investment and structural changes — Research subsidies		— Subsidies for the purposes of the use of housing — Subsidies to enterprises for the purposes of reducing prices and temporarily maintaining production and incomes — Current transfers to households	— Current transfers abroad — Interest on public debt

[1] Major maintenance expenditure is included in row A and minor maintenance expenditure in row B in accordance with the classification of the relevant investment.

Annex 2

Classification of public expenditure by broad economic category

%

		I. Expenditure devoted to expand productive capacity and/or to increase the productivity of domestic private or public enterprises				II. Expenditure devoted to maintain or expand the productive capacity of the domestic government sector (capacity to provide government services)				III. Expenditure not having any influence on the domestic productive capacity of enterprises or of the government sector (serving private consumption)				IV. Expenditure not attributable to groups I, II or III				Total I to IV
		A	B	C		A	B	C		A	B	C		A	B	C		
		Capital expenditure	Government consumption expenditure	Other current expenditure	Total I	Capital expenditure	Government consumption expenditure	Other current expenditure	Total II	Capital expenditure	Government consumption expenditure	Other current expenditure	Total III	Capital expenditure	Government consumption expenditure	Other current expenditure	Total IV	
Belgium	1970	10,4	—	4,6	15,0	3,2	39,0	—	42,2	0,4	—	22,8	23,2	1,0	5,7	12,9	19,6	100
Central government	1980	8,1	—	1,7	9,8	3,1	37,3	—	40,4	1,4	—	28,7	30,1	0,7	4,9	14,1	19,7	100
	1982	8,2	—	1,9	10,1	3,1	33,5	—	36,6	1,1	—	28,5	29,6	0,7	4,3	18,6	23,7	100
	1983	7,2	—	1,8	9,0	2,6	33,9	—	36,5	1,1	—	28,0	29,1	0,8	4,3	20,2	25,3	100
Denmark	1970-71	14,6	—	—	14,6	—	47,0	—	47,0	1,5	—	32,4	33,9	—	—	4,4	4,4	100
Public sector	1975-76	10,5	—	—	10,5	—	51,1	—	51,1	0,9	—	32,7	33,6	—	—	4,8	4,8	100
	1980	8,1	—	—	8,1	—	47,7	—	47,7	0,8	—	33,5	34,3	—	—	9,9	9,9	100
	1982	7,0	:	—	7,0	—	47,0	—	47,0	—	—	:	:	—	—	:	:	100
Greece	1970	16,6	0,1	1,5	18,2	3,6	66,1	—	69,7	0,8	—	6,3	7,1	—	—	5,0	5,0	100
	1975	14,4	0,1	4,1	18,5	5,0	63,6	—	68,6	0,4	—	6,5	6,9	—	—	6,0	6,0	100
	1980	9,5	0,1	1,9	11,4	3,4	68,7	—	72,1	0,6	—	5,2	5,8	—	—	10,7	10,7	100
FR of Germany	1970	11,0	—	2,2	13,2	9,6	46,6	—	56,2	5,1	—	19,1	24,2	0,8	—	5,7	6,5	100
	1975	8,7	—	2,0	10,7	8,5	46,7	—	55,2	3,6	—	21,5	25,1	0,6	—	7,6	8,2	100
	1980	8,2	—	1,5	9,7	7,0	46,4	—	53,4	4,3	—	20,8	25,1	0,8	—	10,6	11,4	100
	1983	7,6	—	1,8	9,4	5,6	47,1	—	52,7	3,4	—	20,9	24,3	0,8	—	14,2	15,0	100
France		:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:
Ireland	1970	11,3	0,9	3,3	15,5	3,6	38,4	—	42,0	5,5	—	26,4	31,9	—	—	10,6	10,6	100
Public authorities	1975	15,5	0,8	2,6	18,9	2,8	35,1	—	37,9	7,2	—	27,4	34,6	—	—	8,6	8,6	100
	1980	:	0,8	2,7	:	:	37,7	—	:	:	—	27,1	:	—	—	12,4	12,4	100
Central government	1980	11,2	0,9	2,8	14,9	2,5	38,2	—	40,7	5,2	—	26,3	31,5	—	—	12,9	12,9	100
	1983	8,7	0,7	2,2	11,6	1,8	36,2	—	38,0	5,1	—	28,7	33,8	—	—	16,6	16,6	100
Italy		:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:
Luxembourg		:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:
Netherlands	1970	11,4	1,6	0,1	13,1	3,5	30,4	—	33,8	4,5	—	40,0	44,5	1,7	—	6,8	8,5	100
General government	1975	9,9	1,3	0,1	11,3	2,7	28,6	—	31,3	3,7	—	45,4	49,1	0,4	—	8,0	8,3	100
	1980	9,2	1,2	0,1	10,5	2,2	27,3	—	29,5	3,3	—	47,5	50,8	0,4	—	8,8	9,1	100
Central government	1980	10,6	0,8	3,1	14,5	1,8	19,0	19,7	40,5	6,7	—	29,9	36,6	1,4	—	7,0	8,4	100
	1983	10,5	0,8	2,3	13,6	1,5	17,9	16,4	35,8	8,6	—	28,2	36,8	1,3	—	12,5	13,8	100
United Kingdom	1977-78	3,7	3,5	4,2	11,4	3,6	45,8	3,5	52,9	5,4	1,7	28,6	35,7	—	—	—	—	100
Public sector	1981-82	4,9	3,4	6,3	13,6	2,8	46,5	3,3	52,7	2,3	1,7	29,8	33,8	—	—	—	—	100
	1982-83	5,0	3,3	5,4	13,6	2,6	46,4	3,2	52,3	2,0	1,7	30,5	34,1	—	—	—	—	100
	1983-84	4,4	3,3	5,1	12,7	2,8	46,6	3,1	52,4	2,5	1,8	30,6	34,8	—	—	—	—	100

Note: The breakdown of public expenditure, according to the large groupings laid down in the Economic Policy Committee's (budget team) classification schedule, has not been completely adhered to by certain countries; thus only the breakdown according to economic categories is in compliance. Nevertheless it has been possible to establish a provisional table, the following comments on which should be noted:

DK: Capital expenditure has been split between Group I (investments and capital transfers to enterprises) and Group III (capital transfers and lending to enterprises); public consumption expenditure is largely included in Group III. Other current expenditure is split between Group III (subsidies and transfers to household) and Group IV (transfers abroad and public debt interest).

UK: Transfers abroad and public debt interest which would normally appear in Group IV are included in the Group III data.

Communication from the Commission to the Council on financial integration

Brussels, 20 April 1983

Introduction

The considerable development of international financial relations over the past 20 years—the spectacular growth of Euromarkets being the most striking example—contrasts sharply with the sluggishness of European progress in the area of finance.

Indeed, it is amazing that free trade in goods is so much easier to achieve than freedom to provide insurance services, or that the mechanisms of cooperation among European currencies apparently do not facilitate portfolio arbitrage among the investment instruments available on the various Community markets.

This day-to-day reality can be expressed analytically by observing that the degree of financial integration in the Community is far from an optimal situation which would have two features:

(i) the existence of a single, homogeneous market open to the outside world on an orderly basis. Market operators seeking to optimize the return on their investments would be in a position freely to buy, sell and trade in financial assets, which would ensure maximum mobility of capital within the Community's financial sector;

(ii) mechanisms and instruments tailored to providing the financial basis for efficient mobilization of Community savings and their allocation to productive investments.

This means that the process of financial integration involves the mobilization, circulation and allocation of financial resources within the Community. Consequently, the barriers set up by exchange regulations and taxation techniques must be removed, and, beyond the field of Community financial instruments, the coordination of policies for regulating financial markets must be encouraged. This effort must be backed up by a common, or at least coordinated, approach to organizing international monetary and financial relations and by greater solidarity with the Member States with balance of payments problems. It goes without saying that the scope and rate of integration, both financial and monetary, depend on the degree of convergence of economic policies; this convergence is essential to stabilize the expectations of investors and savers.

Taking into account the vast domain over which it applies, the movement of financial integration can and must be undertaken through intermediate stages involving greater freedom for capital movements, more stable exchange rates, closer convergence of economic and monetary policies and fuller institutional harmonization. In fact this process has not developed over so wide a front, so that the specifically financial dimension of European construction is at present undeveloped and fragmentary. The failure to progress towards financial integration contrasts with hard-earned achievements in other fields of Community integration.

There are probably historical and economic reasons for this situation. And yet the conditions for financial integration now appear in quite a new light. A European financial market is as necessary as ever: its failure to appear is hampering the reinforcement of the common market and preventing the Community economy from efficiently tapping available savings.

This communication describes the present situation, assesses possibilities for progress and points to practical initiatives that could, if adopted lead the way to renewed progress towards financial integration.

I. Deadlock in the process of financial integration

1. The facts

(a) Unlike the Treaty's provisions concerning the right of establishment and the free movement of goods, services and persons, the provisions on freedom of capital movement are not directly applicable, as a recent Court of Justice judgment has confirmed. The Member States' obligations are thus at present defined in the Council Directives of 1960 and 1962 for the implementation of Article 67 of the Treaty.

Certain transactions are unrestricted, and freedom can be suspended only by applying the safeguard clauses provided for in Articles 73, 108 and 109 of the Treaty. These transactions are: direct investments, operations in securities dealt in on a stock exchange, commercial credits and capital movements of a personal character or connected with the supply of services. A second group of transactions may be restricted on certain conditions: a Member State may maintain or reintroduce restrictions operative on the date of entry into force of the Directive, or on the date of accession, where free movement of capital might form an obstacle to the achievement of its economic policy objectives. These transactions are: flotation of foreign securities on domestic markets and introduction of foreign securities on a domestic stock exchange, transactions in unquoted securities, acquisition of units in unit trusts and the granting and repayment of financial credits. For the remaining transactions, concerning mainly short-term capital movements, the Member States are free to impose restrictions as they see fit.

The adoption of these two Directives was the last occasion on which any progress was made towards freedom of capital movements. None of the subsequent attempts to advance one step further towards the goal came to anything. Indeed, financial markets are probably even less integrated now than

in the 1960s since capital movements within the Community are less free now, and the differences between the Member States are more marked. Exchange restrictions for all capital transactions have been discontinued in Germany, the United Kingdom, Belgium and Luxembourg (although there is a two-tier exchange market in those two countries). In the Netherlands, obligations to the Community are respected and capital transactions not covered by the requirement for free movement are treated liberally. In France, Italy, Ireland and Denmark, controls have been maintained for most capital movements, and these countries have been authorized by the Commission under the safeguard clauses to introduce restrictions on some of the capital transactions freed by the provision of the Directives of 1960 and 1962.

(b) The possibility of restrictions when movements of capital lead to disturbances in the functioning of the capital market in a Member State (Article 73 EEC) or when a Member State is in difficulties or is seriously threatened with difficulties as regards its balance of payments (Article 108 EEC) is one of the aspects of solidarity between the Member States. But the spirit and scope of the safeguard clauses implies that such measures should be exceptional: they should not be kept in force—although they have in fact been—for long periods. Otherwise, direct exchange controls become a permanent economic policy instrument, which is incompatible with the intentions of the Treaty.

There is a tendency to prefer recourse to the safeguard clauses rather than another, better but also more difficult, expression of solidarity: mutual assistance. Apart from credit mechanisms between central banks the Community has added two instruments to its arsenal since the beginning of the 1970s: medium-term financial assistance and the Community loans mechanism. Under both these instruments, the support is conditional upon observance by the recipient country of certain jointly agreed economic policy conditions. The instruments of mutual support ought not to be regarded as a last resort: on the contrary they should be brought into play early enough to prevent balance of payments crises and facilitate the required adjustments in conformity with the obligations under the Treaty. In fact, in spite of a considerable increase in the amounts available, the mutual support instruments have not been used since 1977.

(c) At institutional level, a series of Directives has been adopted to cover the activity of financial intermediaries and stock markets. The arrangements that have gradually been introduced are intended to translate into reality the right to freedom of establishment within the Community for banks and insurance companies and to safeguard their freedom to supply services. The aim in connection with stock markets was to increase transparency and make it easier for issuers to enter the stock markets of the various Member States.

But the incidence of past and future progress towards institutional harmonization of the activities of financial intermediaries and markets will inevitably be limited if it is not backed up by parallel progress towards free capital movements. Free establishment alone does not lead to the integration of markets, even though it permits some interpenetration of the markets through the opening of agencies and branches. Similarly, the freedom to provide financial services or to choose the desired investments on behalf of the savers is sharply constricted if the corresponding movements of funds are subject to restrictions.

2. The explanation

The approach laid down in the Treaty and the economic analysis on which it was based were coherent. In a situation of fixed exchange rates, implicitly assumed in the Treaty, the twofold objective of free trade in goods and services and free capital movement implies that national monetary policies must take account of the requirements of the balance of payments situation. Since most Member States wished to keep control of monetary policy for purposes of domestic regulation, they have had to ignore one or more of the other constraints, or come to terms with them in various ways. They obviously preferred to loosen what looked like the weakest constraint: free capital movements. There are two attitudes that seem to make this constraint less than urgent. First, fluctuations in capital movements are sometimes due as much to speculation as to the trend of basic economic variables. Secondly, a net outflow of long-term capital is often regarded as a loss of real resources for the national economy, the resulting accumulation of claims on the rest of the world being ignored. This explains why the Bretton Woods system justified restrictions on capital movements when such restrictions were essential to ensure the freedom of current transactions and the stability of exchange rates (see Article VI of the Articles of Agreement). The EEC Treaty, while it lays down the principle of 'the abolition, as between Member States, of obstacles to freedom of movement for ... capital', (Article 3(c)), permits the abolition of restrictions to be 'progressive ' to the extent necessary to ensure the proper functioning of the common market (Article 67).

II. The need to relaunch efforts towards financial integration

It is an evident disadvantage from the point of view of Community law, that Europe is not an integrated financial area. It is also, increasingly, a serious obstacle to reinforcing the common market, to restructuring the Community economy and even to stabilizing the international financial system. The economic policy considerations that long justified this situation have now become much less relevant.

1. **Macroeconomic incompatibility has been attenuated**

Experience has constantly shown that direct controls contribute little to restoring basic economic equilibrium, and in particular that the impact of direct controls of capital movements on the balance of payments fades away quickly.

More generally, the Member State governments are finding that controlling financial flows is less and less certain to ensure a degree of autonomy in the pursuit of economic policy. The extent of convertibility of currencies and persistent external deficits in most of the Member States singularly restrict monetary policy independence. But most of all, major progress towards coordinating economic and monetary policies in the Community, helped by the interplay of the European Monetary System, has widened the margin available to the authorities in defining arrangements for capital movements. It is therefore possible to reconsider traditional controls introduced or reinforced under the Bretton Woods system, when the coordination of economic policies was embryonic and the economic cycles in the national economies were not synchronized.

Experience has also shown that control mechanisms have most effect on long-term capital movements, easier to identify but usually corresponding to the investment or reallocation of savings; short-term capital movements, which are more likely to involve speculation, are more difficult to regulate, since operators are very clever at finding ways through the tangled web of national rules.

2. **The reinforcement of the internal market also involves the question of financial services**

If firms are to exploit to the full the possibilities provided by the large single market of the Community, they must be in a position not only to move products around but also to choose the location of their production establishments without sacrificing the economies of scale obtainable through centralized management of a number of departments, especially those dealing with financial and banking matters. Freedom to carry out direct investment, which is now almost complete in the Community, is not enough to ensure actual mobility of the factors of production. Firms develop through the accumulation of financial assets as well as through productive investment. In recent years, net purchases of financial assets have represented some 20% to 30% of capital formation by German, French and UK companies, and even more in Italy.

Financial costs are absorbing a growing proportion of firms' gross operating surpluses. These costs could usefully be minimized through increased competition and economies of scale if the common market in banking were reinforced. Freedom to provide insurance services would also help: premiums on insurance against damage now often account for over 3% of gross operating surplus. If industrial groups are to operate efficiently on the single market, they must not be artificially forced into fragmented and piecemeal financial relations.

3. **Direct tapping of European savings would make for more effective restructuring of the Community economy**

Considerable capital is required for the ordered restructuring of industrial sectors in difficulty and the development of new activities.

Gross savings in the Community amounted in 1980 to 430 000 million ECU compared with a figure of only 340 000 million ECU for the United States. Very little of this total is tapped by national financial markets. Total transferable securities issued on the five major markets (Germany, France, Italy, the Netherlands and the United Kingdom) amounted to 142 000 million ECU, much lower than the corresponding figure of 212 000 million for the US market. The disproportion is even more striking in the specific area of venture capital: the market capitalization of national shares quoted on Community stock exchanges amounts to only about 40% of that of shares quoted on Wall Street alone.

In general, financial flows between Community countries are extremely underdeveloped in comparison with trade in goods and services. It is striking that long-term capital movements [1] between Member States involve less than one-twentieth of the value of commercial flows (average sums between 1976 and 1980 were 10 000 million ECU and 230 000 million ECU respectively).

This partitioning of Community financial markets is even more paradoxical in the light of the fact that foreign borrowing on those markets by non-member countries [2] is much greater than that of non-member countries, and covers almost the same proportion of their borrowing requirements. In 1987, Community borrowers issued loans totalling USD 2 200 million on the markets of their partners, accounting for 8% of their foreign borrowing, while non-member borrowers issued a total of USD 10 000 million, covering 6% of foreign borrowing. The only significant contribution to capital movements in the Community is that of the Community institutions, more than half of whose loans were floated on Member States' markets in 1981. [2]

[1] Direct investment, portfolio investment, other long-term capital including banking capital.

[2] Including international loans denominated in Community currencies.

The activity of financial intermediaries is never neutral in its effects on the allocation of available savings. The partitioning of financial circuits at national level leads to waste; but the free application of the criterion of maximum financial yield does not always ensure maximum economic efficiency. Similarly, at the level of the Community, it may be that a financial system with too many internal partitions and not enough homogeneous regulation of external relations, which encourages too far the diversion of savings to outside destinations, does not serve the best interests of productive investment in the Community.

4. **Excessive intermediary activity for European savings on international markets and for non-member currencies probably undermines the stability of the international financial system**

The considerable development of the international financial system originated to a large extent in the Community. Community financial centres deal with about two thirds of Euro-loans. This demonstrates remarkable technical capacity, which it is in the Community's interests to preserve.

However, the Euromarkets' contribution to connecting up national markets is indirect and imperfect, because of the wide variety of national exchange rules governing the conditions in which residents have access to Euromarkets. In particular, communication via the Euromarkets usually involves non-member currencies and conditions beyond the control of the authorities of the member countries.

An unnecessarily large share of Community savings actually moves through international markets, for ill-defined economic purposes and subject to somewhat uncertain arrangements, as recent events have shown.

Only half the Member States' trade involves non-Community trade partners, but it is estimated that two thirds of their external long-term financial transactions take place outside Community financial circuits. Similarly, the BIS has established that the assets of non-bank Community residents with reporting banks amounted to the equivalent of about USD 70 000 million at the end of 1981; it is estimated that at least 80% of this amount is in the form of deposits in non-Community currencies.

III. Practical proposals for a realistic process of financial integration

To get the gradual process of financial integration under way, a set of specific initiatives is required; no single one on its own is determinant, but their simultaneous application would represent considerable progress towards affirming the financial identity of the Community and reinforcing its financial network. Such progress would supplement and support the Community's existing identity as a trading area and its emerging identity as a monetary union.

1. **A financial system of more direct service to the Community's economic development**

(a) *Gradual dismantling of partitions between capital markets*

The Commission recognizes that the present balance-of-payments situation in several Member States prevents substantial immediate liberalization of capital movements, but restrictions retained under Articles 73 and 108 of the EEC Treaty should be kept to a minimum.

It intends to consider the situation as a whole during the coming year, so as to explore, jointly with the Member States concerned, the possibility of gradually removing restrictions applied pursuant to the safeguard clauses.

At the same time, action should be taken concerning the Commission's proposal for a list of exchange control measures and monetary policy measures with equivalent effect that can hamper current transactions, with a view to prohibiting such measures where they affect relations with other Member States unless they have been agreed at Community level and apply for a limited period.

Apart from the above-mentioned consideration of restrictions under the safeguard clauses, the Commission feels that the gradual removal of barriers to capital movements in the Community should concentrate on the establishment of a European venture capital market.

In the initial stages the restrictions on transactions in transferable securities applied pursuant to the safeguard clauses could be gradually lifted for purchases of shares traded on a Community stock exchange and issued by Community companies. Foreign exchange should be available at official market rates for such transactions.

Where institutional investors are authorized to invest in venture capital, there should be no discrimination between the securities of national companies and those of the companies of other Member States. The principle of non-discrimination should be extended to cover tax incentives for venture capital investment in the framework of the coordination of such incentives.

It is worth noting that the full effects of freeing venture capital movements would be felt if, at the same time, corporation tax systems in the Community were harmonized. The Commission would recall that it has presented a relevant proposal, at present under discussion in Parliament,

to avoid a situation where decisions about investment in shares at Community level are taken, all other things being equal, on the basis of tax considerations.

(b) *A more unified network of financial services*

1. The initial aim for banking was to encourage integration through the establishment of agencies and branches. The Directive of 12 December 1977 laid down rules for the coordination of national laws in this respect. The Commission intends to continue and step up its work in this field concentrating in particular on adjusting systems of control so as to facilitate the development of banking transactions within the Community.

2. In the field of insurance, the right of establishment has been a practical reality since the First Directive of 24 July 1973 was adopted. The same is not true of freedom to provide services, in spite of the direct effect of the relevant provisions, Articles 59, 60 and 106 of the Treaty. A proposal for a directive on insurance other than life assurance was sent to the Council in late 1975, with the purpose of ensuring freedom to provide services; it was followed by a proposal for amendments in early 1978. Since then, participations have been at a standstill for technical reasons.

The development of services in this branch will help to strengthen the internal Community market. As to its financial impact on balances of payments, the transfer of premiums abroad will not be a one-way process, and will probably not affect more than a small percentage of total premiums paid in any one Member State, and there would probably be some correspondence between the descriptions of premiums collected and placements made. Management would be easier for those firms whose activity at Community level had developed most. Competition between insurers would encourage new insurance techniques, to the advantage both of customers and of the insurers themselves who are desirous of expanding their international activities.

3. In the field of stock exchanges, the Commission thinks that links between national stock markets should be strengthened so that orders from clients may be carried out on the market offering the best terms at any given moment.

The idea is not to set up a new stock market, but to link existing exchanges so that Europe can pool its resources and end the present compartmentalization. In the first stages the link-up could be confined to European shares quoted on several exchanges, eventually spreading to other securities and other markets. The Commission, in close collaboration with the European Stock Exchange Committee, is at present considering ways of achieving this aim. It is prepared to consider granting financial assistance if necessary to get the link-up system currently under study of the ground, and in particular to help with investment in data-processing and information technology infrastructures.

If stock exchanges in all the Member States are to be in a position to participate fully in the system from the outset, the restrictions on listing foreign shares which some of them apply should be lifted.

Moreover, to avoid distortions of competition between the exchanges of the different Member States, the Council must rapidly adopt the proposal for a Directive on indirect taxation of transactions in securities, with a view to eliminating double taxation and reducing the burden of taxes on such transactions as a first step to abolishing them.

The Commission also feels that the development or establishment of markets for unlisted securities, particularly geared to the financing needs of small and medium-sized firms, could help to reinforce European markets and boost venture capital markets in Europe.

Encouragement should also be given to collective investment undertakings for transferable securities (CIUTS) established in the Community to play a role in the interpenetration of Community markets. Consequently the two proposals for Directives concerning, respectively, the coordination of national provisions relating to CIUTS and freedom for transactions in their units should be adopted as soon as possible by the Council to enable CIUTS to provide services.

(c) *New instruments for tapping savings in the Community*

The Community institutions, including the EIB, have a useful contribution to make here. At the same time, it is necessary to develop financial instruments that can result in the effective interpenetration of financial circuits and ensure efficient tapping and circulation of capital within a geographically wider financial sector.

The Commission intends to take action on three fronts:

1. It will encourage closer collaboration between medium-term and long-term credit institutions on programmes or projects of common interest, and in particular develop cofinancing operations like those already carried out by the Community's club of specialized long-term credit institutions. Such collaboration might be based for example on a programme of unified loans issued simultaneously on the Member States' markets.

2. It may consider the establishment of collective investment undertaking for industrial purposes; their units would be placed freely on the markets in the Member States and their portfolio made up of shares issued by Community firms. The adoption of the two Directives on CIUTS mentioned above

would make it easier to set up such undertakings and distribute their units.

3. The third type of action concerns mortgage loans. Housing credit establishments financed by the issuing of mortgage bonds should be allowed to place their bonds, up to a certain ceiling, in other Member States, using the proceeds for mortgage loans in the country of issue. The establishments financed by deposits, whose freedom of establishment is hampered at the moment by administrative barriers, should be authorized to move into the markets of other Member States.

2. Contributing to better balanced international financial relations

The Community should set itself for international financial relations a goal similar to that adopted on the monetary front: an area of stability, to help create more balanced relations between the world's major financial centres. To take this approach, the Community must assume a financial personality *vis-à-vis* the rest of the world.

(a) *Greater control of capital flows between the Community and the rest of the world*

The steps taken towards freeing capital flows early in the Community's existence were the product rather of a movement towards global financial exchanges. At the same time, within the Community national measures governing financial flows to the outside world were in force in several Member States. To date, Article 70 of the Treaty, which provides for the progressive coordination of the exchange policies of the Member States in respect of the movement of capital between those States and third countries, has only once been applied: in the 1972 Directive on regulating international capital flows and neutralizing their undesirable effects on domestic liquidity. The instruments created by the Member States in this respect are of general application, with no differentiation between capital movements within the Community and those between the Community and non-Member States. Some of them were or are solely intended to improve control over speculative inflows of capital (e.g. the *Bardepot* system). [1]

The Community's aim should be to maintain a high degree of freedom in relation to the rest of the world and to safeguard the international activity of its financial centres. At the same time, the relevant Community authorities should consider whether instruments should be set up at Community and international level to be used if necessary to improve control over flows of capital between Member States and the rest of the world, and if so, how.

(b) *Joint consideration of international banking supervision*

Once the Community has well-defined instruments of integration at its disposal, it can, through the coordination of banking laws, create an area of stability that would not only achieve a homogenous internal structure control at international level in a way better adapted to banks' growing international exposure.

For example, the Commission has drawn up a proposal for a Directive on banking supervision on a consolidated basis in close collaboration with the EEC's Banking Advisory Committee on the basis of work done at the Bank for International Settlements; the proposal is intended to enable the supervisory authorities of the country where the parent company of a banking group has its headquarters to assess the financial situation of the entire group, including subsidiaries in other Member States.

The Commission has also taken steps concerning annual accounts of banks and the content of regular returns to be supplied to the supervisory authorities, the supervision of large exposures, in particular large loans granted by banks and cooperation between credit information exchanges; the calculation of banking solvency and liquidity ratios; procedures for the reorganization, or if necessary winding up of international banks in a critical situation.

Among these measures the calculation of coefficients (which the Banking Advisory Committee considers very important) is especially likely to lead to international cooperation in the field of capital requirements and day-to-day supervision of banks operating at international level, particularly since the methods of calculation are also being considered outside the Community, by a Committee of the Group of Ten in Basle.

In the Commission's opinion, action on these fronts, and in particular the adoption of the Directive on supervision on a consolidated basis, is a necessary first step to proper assessmen of the international activity of European banks. These measures could also help to improve the management of international risks. The basic techniques developed should be used for a Community approach to official discussion of the risks to the international financial system, and the rescheduling of the external debt of countries in difficulty. A common position is especially necessary when these matters involve geographical regions or countries with which the Community's relations are intense or privileged.

[1] In 1972 and 1973 the German authorities introduced the requirement for a frozen deposit, called the *Bardepot*, corresponding to a certain percentage (it has varied from 20% to 50%) of foreign borrowing by residents.
It does not operate in the same way as the compulsory non-interest-bearing deposit that Italian rules have required on several occasions (under measures taken in 1974, 1976 and 1981) on purchases of foreign currency by residents.

(c) *Coordinating the foreign borrowing policies of the Member States*

A joint attempt at Community level to find the proper balance between the constraint of international adjustment and the advantages of external financing is one of the basic factors in the convergence of the Member States' economic policies.

As announced in the programme put forward in 1980 in its report on recycling, the Monetary Committee has just set up a mutual information and monitoring procedure on the balance-of-payments and external indebtedness position of the member countries. This work should lead to the definition of general guidelines for foreign borrowing policy. This opportunity should be taken to assess whether Community instruments are suitable in view of the new technical features of financial markets, and whether they are adequate to meet the needs of the Member States.

3. **Promoting the use of the ECU**

Financial integration in the Community cannot make genuine progress unless it is based on a higher degree of monetary identity. At this stage, the development of the role of the ECU is an essential factor here, both as the most important vehicle for increased transferability of financial assets within the Community and as the expression of an emerging monetary union that aspires to be one of the three pillars of an ordered international monetary system.

(a) *Recognition of foreign currency status*

It would be a decisive step forward if the ECU were recognized as a foreign currency so that transactions denominated in ECUs could be treated as transactions in a convertible currency. Official rates for the ECU quoted on all the Community's exchange markets, even if the rates are based on those for the component currencies, would sanction the ECU's status in the eyes of operators.

(b) *Privileged treatment for financial transactions in ECUs*

Community residents should be able to carry out transactions in securities denominated in ECUs, at least within certain limits, under normal conditions; in several Member States this would mean waiving rules now in force.

(i) First, all residents of Member States should be allowed to subscribe freely, at official exchange rates, to ECU issues floated by Community borrowers, and in particular to issues of this type floated by Community institutions.

(ii) Under the rules governing the composition of the portfolios of institutional investors, securities denominated in ECUs should be assimilated to national securities of the same type, subject to possible provisions to limit the exchange risk.

(iii) Any new instrument for tapping savings introduced at Community level should preferably be based on the ECU.

(c) *Enlarging the official role of the ECU*

At present, official use of the ECU between central banks participating in the EMS takes place in a closed circuit. If the EMS is opened to the outside, as recommended by the Commission in its communication of 15 March 1982 on strengthening the EMS, this would extend the area of stability of the system by associating in exchange and intervention mechanisms the currencies of non-member countries having special economic and financial links with the Community and its Member States. It would also increase opportunities for using and mobilizing the official ECU, and, by setting an example, contribute to developing private use of the ECU by operators outside the Community.

Conclusions

With a view to ensuring the development of productive activity and to tapping savings to obtain required financing, the Commission would ask the Council:

1. To recognize the need for the financial integration process to get under way once more, with the removal of partitions and the establishment of interconnections between capital markets the actual provision of financial services and the gradual establishment of genuine financial unity in Europe, *vis-à-vis* non-member countries.

2. To note the Commission's intention to present the Monetary Committee with a request for an opinion based on this communication, to help it assume its responsibilities of management and proposal, concerning in particular:

(i) consideration by the Commission of justification for partial or complete retention of national measures authorized under Articles 73 and 108 of the Treaty;

(ii) the proposed list of exchange control measures or monetary policy measures of equivalent effect liable to hamper current transactions in the Community, which Member States should not introduce unless there has been a joint decision under the procedures of the safeguard clauses;

(iii) the definition of instruments, and the conditions of their use, which the Member States could set up to control

exchange and regulate capital movements involving non-member countries.

3. To request the Member States, irrespective of the consideration of safeguard clauses to be undertaken by the Commission, to take the required steps:

(i) to remove barriers to the free movement of shares issued by Community undertakings and traded on a Community stock exchange, and to bring arrangements for investment in equity, in particular rules governing institutional investors and tax incentive measures, closer into line with a Community approach;

(ii) to recognize the ECU as a convertible currency with the same status as all major currencies, and to treat transactions denominated in ECUs, especially loans floated by Community institutions, as privileged transactions for the purposes of exchange control regulations and provisions applying to institutional investors.

4. To set itself the following aims:

(i) the adoption of the Directive coordinating national provisions concerning insurance services other than life assurance to facilitate freedom to provide services, as a priority measure for strengthening the internal market;

(ii) the adoption by the end of 1983 of the Directive on banking supervision on a consolidated basis;

(iii) the adoption as soon as possible:

(a) of the two Directives on collective investment undertakings for transferable securities, in particular to make it easier to set up CIUTS with an industrial purpose and to place their units on the markets of the Member States;

(b) of the Directive concerning indirect taxation of transactions in securities;

(iv) the intensification of efforts to smooth the way for the gradual emergence of a common market in banking, both from the point of view of conditions of entry to the market and from that of the coordination of measures on prudential control and the establishment of harmonized accounting procedures;

(v) further coordination of foreign indebtedness policies, with consideration of the respective roles of the various forms of official borrowing;

(vi) the association of non-member central banks in the mechanisms of the European Monetary System; in the present international economic and monetary situation this would be particularly useful in strengthening the EMS.

Communication from the Commission to the Council on the promotion of the international role of the ECU

Brussels, 24 May 1983

1. The conclusions of the Presidency of the European Council in Bremen stipulated, in paragraph 1 of the annex, that the ECU should be at the heart of the EMS; the Resolution of the Brussels European Council foresaw, in paragraph 2.7, that the ECU would be at the centre of the EMS. Both national and Community authorities have repeatedly stressed the need to develop the role and usage of the ECU, both public and private. This communication deals only with the private use of the ECU.

2. The private use of the ECU, which commenced only two years ago, has taken off rapidly: it is a method of invoicing which is becoming more and more widespread, particularly in the case of multinational companies; its role as a means of payment should be reinforced by a better exploitation of the existing usage possibilities; it is, in some Member States, an increasingly important instrument for the denomination of financial investment; finally, the volume of ECU-denominated isuues makes it the third most used currency, after the dollar and the German mark for the floating of bonds on the international markets.

3. Nevertheless, steps must be taken to secure the development of the private use of the ECU; such a development is, in fact, a necessary means of reinforcing the European monetary identity, internal and external.

(a) Increased use of the ECU would constitute, first of all, an important element in a renewed movement towards internal financial integration in the Community; it is clear that the ECU, the expression of a monetary zone in formation, cannot continue to be subject, within the EEC, to those restrictions which in some Member States are imposed on foreign currencies.

(b) It is even more necessary that the development of the ECU in international markets should permit the progressive distributions over all Community currencies of capital movements which, at present take place between, on the one hand, the dollar, and, on the other, those European monies which are alternatives to the US currency. The enlargement of the ECU market would, moreover, bring about a better equilibrium between the source of funds, at present very limited geographically, and their use.

4. The Commission proposes that the promotion of the role of the private ECU should take place under three main headings:

(a) *Status of the ECU*

The ECU is treated differently, *de facto* or *de jure*, in the various Member States. This differentiation ranges from a total ban to complete freedom, encompassing formulae which, while not forbidding operations in ECUs nevertheless result in increased costs for such operations.

The Commission proposes that the necessary measures be taken, in all Member States, to accord foreign currency status to the ECU. To this end, it proposes that the Council adopt the draft Resolution attached in the annex.

(b) *Use of the ECU*

Transactions in ECU-denominated bonds must be liberalized, that is to say, made accessible to Community residents under normal conditions. This privileged access to the ECU market by residents requires, on the part of several Member States, derogations from their exchange control laws.

The Commission has made proposals in this respect in its communication on financial integration.

(c) *Protection of the ECU trade mark*

Although the banking profession follow uniform procedures when referring to the ECU, private initiatives, taken in the context of national regulations, often designed for other purposes, risk giving rise to divergent applications of the ECU and, therefore, prejudicing its development.

The Commission will, therefore, propose, when all Member States have recognized the ECU as a foreign currency, a document which will constitute a reference text for the ECU. This text will define the status of the ECU and clearly state the rules which users will have to follow; it will reproduce the various texts regarding the definition of the ECU, refer to its recognition by the Member States and assure the protection of the ECU trade mark.

Annex

The Commission request the Council and the Member States to adopt the following draft Resolution regarding the ECU:

' The Council considers that the development of the role of the ECU is an important part of the internal consolidation of the EMS and the affirmation of its external role.

It has noted the communication of the Commission in the matter and, particularly, the suggestions made to facilitate the treatment and promotion of the use of the ECU. The relevant authorities have expressed their intention to take all the measures necessary to ensure that ECU operations are treated, in the context of their internal regulations, as foreign currency operations.'

Technical annex

1. Basic concepts and forecasting techniques

1.1 Aggregation in Community data

In general, national accounts variables in national currencies for the Member States are aggregated using Purchasing Power Standards (PPS) for domestic variables and market exchange rates (ECU) for foreign trade variables. Volume series (constant price series) are aggregated on the basis of 1975 prices and 1975 PPS/exchange rates. Value series (current price series) are aggregated on the basis of current prices and current PPS/exchange rates. National accounts implicit price deflators are obtained by dividing current price series by the corresponding constant price series.

Money supply indices for the Community are derived from geometrically-weighted indices for the Member States, the weights being the share of each country in total Community GDP at current prices and current PPS in the year in question. Long-term and short-term interest rates for the Community are similarly derived as a geometrically-weighted average of rates in the Member States, the weights being the same as for the money supply calculations.

1.2 Forecasting procedures

Short-term forecasts are prepared by the Directorate-General for Economic and Financial Affairs twice a year, in May-June and September-October. The time horizon of these forecasts is to the end of the following year. The forecasts contained in this *Review* are those given by the September-October 1983 exercise. The forecasts are built up separately for each of the 10 member countries of the Community, but within a framework of common assumptions about the external environment, exchange rates and interest rates, and subject to controls and checks on the consistency of foreign trade forecasts. The forecasts are made on the basis of the assumption of unchanged government policies.

The forecasts for each Community country cover the main components of gross domestic product in volume, price and value terms; the income and expenditure accounts of households and of general government; the current account of the balance of payments; saving, investment and the financial balance of the main institutional sectors; employment and unemployment; and domestic money supply and its counterparts. Figures are mainly compiled on an annual basis, but half-yearly estimates are made for gross domestic product and its components in volume terms and for certain other key indicators such as industrial production, unemployment, and the current account balance. Quarterly profiles for gross domestic product are also made for the whole forecast period.

Although in principle the definitions used are those of the ESA, in practice national definitions and sources are used in some cases because the statistics become available more quickly, and in order to facilitate discussion of the forecasts with national authorities.

The forecasting round starts with the setting of assumptions about exchange rates, interest rates, and demand and prices in the rest of the world. These initial assumptions may be amended as the round progresses in the light of new information and of the emerging forecast for the Community countries.

(i) Exchange rate forecasts are normally based on the rates implied by the forward exchange markets, modified to take account of the EMS and other considerations. In the present forecast the forecast rates were based on those future rates prevailing at the beginning of July 1983.

(ii) Short-term interest rate assumptions are set for the USA and for each of the Community countries taking account of exchange rate developments, domestic monetary policies, etc.

(iii) Forecasts are made for the growth of real GDP and its components for the USA, Canada and Japan, and in a more summary form for each of the other non-EC member countries of the OECD. In the light of output growth and other considerations, forecasts of the change in the volume of total imports of goods are made for each of these countries, and for three other world zones—OPEC, non-oil developing countries, and other countries (consisting principally of the centrally planned economies, South Africa, and Yugoslavia). An assumption is made, having regard to oil market conditions and recent OPEC decisions, about the export price of oil, and forecasts are also made for the world export prices of the main groups of non-oil primary commodities (based on UN indices) and for the export prices of manufactured goods of the major non-EC developed countries.

The forecasts of the change in import volumes for the non-EC countries and zones, together with initial import forecasts for each of the Community countries, are weighted together according to the structure of exports to provide estimates of 'export market growth' for each country. Similarly, the forecasts of rest-of-the-world export prices for primary commodities and manufactures, together with initial forecasts of total export prices of goods for each of the Community countries and with the necessary exchange rate adjustments, are weighted together according to the structure of imports to provide estimates of 'import costs' for each country. On the basis of this and other information the country desks make their first forecasts of export volumes and import prices and, if necessary, revise their forecasts of import volumes and export prices, with in all cases a split between trade within the Community (intra-EC) and trade

with non-EC countries (extra-EC). Particular attention is paid to ensuring that the changes in total intra-EC imports and exports should be close in both volume and price terms. Checks are also made at world level to make sure that world exports and imports are in line with each other. In order to reach this desired convergence and in response to the country desks' forecasts which are being developed at the same time, this procedure for achieving trade consistency is reiterated several times.

2. Balance of payments exchange rate and competitiveness concepts

2.1 Sources of balance of payments and related data

Indices of the terms of trade (Tables 7.1 and 7.2) refer to merchandise trade. The sources are Eurostat for EC countries, the IMF ('International Financial Statistics' and 'World Economic Outlook') for other groups of countries.

Tables on nominal and real adjustment (Tables 7.1 and 7.2) are based on data for current balances taken from Eurostat for EC countries (except for 1983 forecasts, which are made by the EC Commission) and from the IMF ('World Economic Outlook') and the OECD ('Economic Outlook') for other groups of countries. The data in these tables for trade in goods and services at constant 1975 prices, which exclude investment income flows, are based on balance of payments figures, deflated by price indices of exports/imports of goods and services (expressed in ECU or dollar terms) taken from the national accounts of the country, or group of countries concerned, where such data are available. Where price deflators for goods and services are not available (i.e. in the case of oil-exporting and non-oil developing countries) merchandise unit values have been used.

In Tables 7.3 and 7.4 the terms 'primary products' and 'manufactures' denote respectively categories 0-4 and 5-9 of the Standard International Trade Classification.

In Table 7.9, gross reserves are defined to include foreign currency, SDR, IMF reserve positions, ECU and net positions *vis-à-vis* the EMCF. They exclude the 80% of official gold reserves which are not swapped against ECU. For comparability with later years, the figures for 1978, before the EMS was established and the ECU came into existence, include 20% of official gold reserves valued at market prices. The same procedure has been applied for all years to Greece, which is not a member of the EMS and has no official holdings of ECU. Note that this definition of gross reserves differs from that used in Table 40 of the Statistical Annex, which includes total official gold reserves.

2.2 Effective exchange rates

Changes in the effective exchange rate of a currency *i* measure the average change in the exchange rates between currency *i* and a representative sample or 'basket' of other currencies between two points in time in order to express in a single figure the average direction and magnitude of change over the period in question. The model used in the Commission to calculate these average exchange rate changes involves 20 countries—the members of the Community (with Belgium and Luxembourg treated as a single entity), the two candidates for membership (Spain and Portugal), and the nine other countries with the greatest importance in world trade. An effective exchange rate change for currency *i* is obtained by multiplying the percentage change against each of the other 19 currencies in the model by that currency's weight and summing the results.

The weights attributed to each currency reflect the importance of the currency concerned, both as a bilateral trading partner for country *i* and as a competitor against exports from country *i* in third markets. For this reason the term 'trade-weighted exchange-rate changes' is sometimes used in place of the term 'effective exchange rate changes'. The weights used are based on trade data for the year in question up to and including 1980. For subsequent years, the weights are based on 1980 trade data.

For certain purposes it may be useful to use a more restricted sample of currencies. For example, following a realignment within the EMS it is possible to calculate the effective exchange rate of each EMS currency against all other EMS currencies taken together using the same technique as described above, but using a 'basket' composed of EMS currencies only.

2.3 Statistical measures relating to the European Monetary System (EMS)

2.3.1 *Bilateral divergence between currencies of the European Monetary System (EMS)*

The width of the EMS band depends on the positions of the two currencies that diverge most in relation to their bilateral central rate. The maximum divergence allowed between two currencies is 2,25%, although the lira may diverge by up to 6%; sterling is not in the exchange mechanism.

The average point in the band is determined by half the bilateral divergence of the two currencies with the widest divergence (not counting the lira). In the graph, the currencies do not diverge by more than 1,25% from the average point.

2.3.2 *Divergence indicator in the European Monetary System (EMS)* [1]

The divergence indicator (DI) measures the degree of movement of a specific currency against its maximum divergence spread (MDS), which differs for each currency as a function of its weight in the ECU basket. The formula for the divergence indicator is:

$\pm$ 2,25 x $(1 - p_i)$, where p_i is the weight of the currency in the ECU basket.

For a given currency, the divergence indicator is obtained:

(i) first by calculating the premium (P) or discount (D) shown by the market rate of the ECU in terms of that currency against its ECU-related central rate;

(ii) and then by comparing the result obtained with the maximum divergence spread.

In order to permit a comparison of movements in the divergence indicators for each of the EMS currencies, the maximum divergence spread for each currency is assigned an index of 100. The indicator will therefore be expressed as a figure from 0 to 100. A currency reaches its divergence threshold when the indicator stands at 75.

Expressed as a formula, calculation of the indicator is as follows:

$$P \text{ or } D = \frac{\text{ECU market-ECU central}}{\text{ECU central}} \times 100$$

$$DI = \frac{P \text{ or } D}{MDS} \times 100$$

The result is adjusted to ensure that the indicator for currencies observing narrow margins of 2,25% against one another is not distorted by exchange rate movements in the lira and the pound sterling outside those margins (which are not, of course, operationally compulsory for Italy and the UK).

2.4 Unit labour costs and competitiveness

An index of competitiveness for country *i* is derived by multiplying the effective exchange rate index (see above) for currency *i* by an index of relative inflation (calculated in exactly the same way, except that it measures changes in price or cost levels, expressed in national currency, rather than average changes in exchange rates). The resulting index shows how prices or costs in country *i*, when corrected for exchange rate changes, have moved in relation to a weighted average of 19 other countries' prices or costs, also corrected for exchange rate changes, over a given period. Such an index is usually referred to as an index of price or cost competitiveness.

In this *Review* competitiveness is measured in terms of unit labour costs in manufacturing (see Chapters 3 and 7).

Labour cost per unit of output is defined as the ratio of compensation of employees (including employers' social security contributions) in manufacturing at current prices to value added in manufacturing at constant prices (base 1970 to 1975 = 100).

'Manufacturing' in principle refers to branch 3 of the NACE ('Nomenclature des activités dans les Communautés européennes'). For the period 1960-69, data on value added in manufacturing were as far as possible taken from Eurostat for Community countries and from OECD sources for non-member countries. Where figures were not available from these sources, national sources were used. Thus in Denmark prior to 1965 the figures include repairs and maintenance. Irish figures for the whole period are from national sources and relate to industry, i.e. they include construction and energy. For Switzerland, figures were not available on a national accounts basis and the OECD index of industrial production was used. For a number of other countries data were unavailable from 1960 to 1962 and industrial production indices were linked to the value added series for these years. For figures on income from employment, national sources were used for Denmark, Luxembourg, Italy, France, the Netherlands and Ireland (including construction and energy) OECD data were used for the United Kingdom and the Federal Republic of Germany. For Belgium estimates were made on the basis of the change in total remuneration of employees. Figures for Japan were from national sources and for Switzerland and Austria were constructed on the basis of indicators of changes in hourly earnings, hours worked and employment (source OECD). The remaining figures are from OECD national accounts data except in certain cases for the period 1960-62 where indicators were used.

For the period 1970 to 1981, Eurostat data were used for the Community countries and OECD data were used for other countries. For the period 1982 to 1984, estimates of Commission services were used.

In order to calculate relative costs, non-EC countries had to be taken into account so that the study covers 20 OECD countries whose foreign trade is more than 1% of total world trade: EC [2] plus USA, Canada, Japan, Austria, Australia, Switzerland, Norway, Sweden, Spain, Finland and Portugal.

[1] For a detailed explanation of the EMS, see *European Economy*, No 3 of July 1979.

[2] Belgium and Luxembourg aggregated in the calculations of relative data.

Labour costs per unit of output are then weighted by an effective exchange-rate matrix, the weights being those used by Commission services in competitiveness index calculations. The weighting matrix used is that described in section 2.2 above. The actual weights used are shown in Table A1. The weighting coefficients take account not only of bilateral trade but also of the intensity of competition in third markets and in the domestic market of each country. The exchange rate used is that of the number of dollars per unit of national currency. This first calculation gives a 'competitors' labour cost'. The ratio of labour cost per unit of output calculated on the basis of national currency data to this 'competitors' cost' gives the 'relative cost'.

The same calculation can be made without including the exchange rate, giving a 'relative cost in national currency'. Thus, three series are used as a basis for the study.

(i) Labour cost per unit of output:

$$ULC = \frac{RSN}{=VA_{75}}$$

(ii) Relative labour costs in national currency:

$$ULCR_i = \frac{ULC_i}{\text{antilog} \sum_{j=1}^{20} W_{ij} \text{ Log } ULC_j}$$

(iii) Relative labour costs in USD:

$$ULCR\ USD_i = \frac{ULCUSD_i}{\text{antilog} \sum_{j=1}^{20} W_{ij} \text{ Log } ULCUSD_j}$$

$$= ULCR_i \times \frac{TCH_i}{\text{antilog} \sum_{j=1}^{19} W_{ij} \text{ Log } TCH_j}$$

RSN = Compensation of employees (wages plus total social security charges) in national currency;

VA_{75} = Value added in manufacturing 1975 prices;

TCH_i = Exchange rate of the currency of country i against the USD;

$ULCUSD_i$ = $ULC_i \times TCH_i$ = labour cost per unit of output in USD;

W_{ij} = Weighting for country i.

$$\frac{TCH_i}{\text{antilog} \sum_{j=1}^{19} W_{ij} \text{ Log } TCH_j} = \text{effective exchange rate}$$

All the data have been calculated on the basis of costs in national currencies expressed as an index (base 1970 to 1975 = 100) for each country.

The data relating to the effective exchange rate for the Community are calculated for the ECU by reference to a weighted average of the ten competing countries, the Community being considered as one market. Relative labour costs for the Community were calculated using the same matrix of weighting coefficients.

3. Prices and costs

3.1 Origin of price increases

The deflator of total final expenditure (TFE) at market prices in period O (P_o^d) is defined as follows:

$$P_o^d = \frac{D_o}{d_o} = \frac{W_o + N_o + T_o - M_o}{d_o} \qquad (3.1.i)$$

where D = total final expenditure at market prices;

W = income from employment;

N = gross operating surplus (profits and self-employment income);

T = indirect taxes less subsidies;

M = imports.

Upper-case variables are expressed in current prices and lowercase variables in constant prices.

$$\text{Thus } \dot{P}^d = \frac{\frac{W_o \cdot \dot{W}}{D_o} + \frac{N_o \cdot \dot{N}}{D_o} + \frac{T_o \cdot \dot{T}}{D_o} + \frac{M_o \cdot \dot{M}}{D_o}}{\dot{d}} \qquad (3.1.ii)$$

Where a dot over a variable here denotes its value in period 1 divided by its value in period 0.

Defining unit labour costs (ULC), profits and self-employment income per unit of output (UNC) and indirect taxes per unit of output (UTC) as income from employment, profits and self-employment income and indirect taxes, respectively, divided by gross domestic product in constant prices (y), then

$$\dot{P}^d = \frac{\dot{y}\left(\dot{ULC} \cdot \frac{W_o}{D_o} + \dot{UNC} \cdot \frac{N_o}{D_o} + \dot{UTC} \cdot \frac{T_o}{D_o}\right) + \dot{m} \cdot \dot{P}^m \cdot \frac{M_o}{D_o}}{\dot{d}} \qquad (3.1.iii)$$

where P^m is the import price deflator.

Then if $\dot{ij} \simeq \dot{m}$:

$$\dot{p}^d \simeq \dot{ULC} \cdot \frac{W_o}{D_o} + \dot{UNC} \cdot \frac{N_o}{D_o} + \dot{UTC} \cdot \frac{T_o}{D_o} + \dot{p}^m \cdot \frac{M_o}{D_o} \qquad (3.1.iv)$$

i.e., one plus the rate of change of the TFE deflator is approximately equal to one plus the base-weighted sum of the rates of increase in unit labour costs, profits and self-employment income per unit of output, indirect taxes per unit of output and import prices. Table 4.2 is based on the approximate equation (3.1.iv) to allow the 'contributions' of unit labour costs, import prices, etc., to be presented in an easily recognizable form. In consequence, the sum of the components in the table is, in general, not exactly equal to the increase in the TFE deflator, but the differences are all very small.

For the Community as a whole, the import weight (Mo/Do) used in this *Review* (see Table 3.2) is the share of extra-EC imports in TFE. In last year's *Review* (Table 4.2), the share of total imports was used. As a result of this change, the 'contribution' of import prices to the increase in the TFE deflator is this year shown as being smaller than was shown last year.

The rise in import prices results from a number of different phenomena and measures of these influences have been attempted in this year's presentation.

Two basic effects have been isolated in the first stage. The first is the effect of the increase in world export prices on import prices of the country in question and the second is the change in the nominal effective exchange rate.

Various measures of nominal effective exchange rates are available (import, export, double weighted). While it would have been more appropriate to use the import weighted effective exchange rate in this case, as the first stage of the analysis is to find the effect of the increase in export prices of suppliers on the country in question, the more normal double weighted measure, used elsewhere in this *Review* and generally regarded as 'the' effective exchange rate, is used since at the second stage of the analysis competitiveness (in terms of relative unit labour costs in the total economy expressed in a common currency) is measured: this last requires the double weighted measure. Another problem arises in so far as the trade weighting matrix relates to goods, while the price increases relate to goods and services. Other more minor problems which arise are:

1. the fact that the trade weighting matrix covers only 20 countries and that exchange rate movements of countries outside this sample will be regarded as movements in basic export prices rather than exchange rate movements;
2. the problem of invoicing in third currencies, which can distort the breakdown in some countries;
3. the rationale of attributing the rises in world prices to exogenous factors.

In the second stage of the analysis the effect of the change in the nominal effective exchange rate on prices is ascribed to two factors:

(i) the effect on prices of changes in real exchange rates;
(ii) the effect of the exchange rate change which would be required to compensate for movements in domestic costs relative to competitors' costs.

The breakdown of the total increase in import prices into the three elements identified follows the methodology described above for the breakdown of increases in the TFE deflator, except that the elements are weighted geometrically rather than arithmetically. The three elements therefore do not, in general, exactly sum to the total import contribution previously identified.

3.2 **Real product wage**

The real product wage is in this *Review* defined identically with real unit labour costs adjusted for the changing proportion of self-employment in total employment. The change in real unit labour costs is derived as the change in:

$$\frac{W \div E}{GDP \div N} \Big/ P_{GDP}$$

where W = total compensation of employees;
E = number of occupied persons;
GDP = gross domestic product at constant factor cost;
N = number of employees;
P_{GDP} = deflator of GDP at factor cost.

It can be seen that this expression is equivalent to that for the adjusted labour income ratio: the share of compensation of employees in GDP, adjusted for the ratio of the number of employees to the total number of occupied persons. The adjustment is equivalent to attributing to self-employed persons, as labour income, the average amount of compensation per employee.

The consistency, in an *ex post* accounting sense, of the measure of the movements of the real product wage adopted here with movements in the labour-income ratio does not remove the need for great caution in interpretation of such movements.

First, the measure of the real product wage used in this *Review* refers to the economy as a whole, and movements in it can therefore be created simply by shifts in the sectoral pattern of production, the exploitation of oil and gas reserves in the United Kingdom and the Netherlands providing a good example.

Second, the assumption embodied in the adjustment for the share of employees in total employment may not be adequate in the presence of segmented labour markets. This may pose an important problem, for instance in the case of countries in a state of transition from a predominantly low-productivity agricultural economy to a more industrially-oriented economy.

Third, the measure computed in the *Review* covers the public sector as well as the private sector. The conventional nature of the measurement of productivity in the public sector thus causes problems. Further, the principles on which public sector employment is determined are not the same as those governing the labour-hiring decisions of the private sector. Indeed, during the 1970s it may not have been an untypical experience for a weakening of private sector employment associated with the emergence of a 'real wage problem' to be offset by increased public sector employment, so that the 'real wage problem' manifested itself not so much (or at least not exclusively) in a shortfall of total employment as in a sectoral employment shift and in budgetary and balance of payments disequilibria.

Fourth, the interpretation which can be given to any movement of the real product wage is very dependent on the parameters of the production function which is supposed to underlie it. As long as the elasticity of substitution is, in the short run, less than unity, a *ceteris paribus* increase in wages will increase the real product wage and the labour income ratio. However, if the elasticity of substitution is higher in the long run than in the short run, the real product wage and the labour income share will subsequently decline as labour-shedding produces a rise in labour productivity. A 'real wage problem' may still exist, but may eventually disappear from view in the real product wage statistics. Thus it may be the case that a sudden upward movement in the real product wage, assuming an equilibrium position to begin with, may be *prima facie* evidence of the emergence of a 'real wage problem'. However, subsequent movements of the real product wage may be a very poor guide as to the extent to which that problem has been resolved or as to how that problem has been resolved.

Fifth, movements in the real product wage may for long periods have had little impact on output, investment and employment decisions in some countries which have, or had at some time during the period examined, low wage levels and 'abnormally' high profits during the process of industrialization.

Further problems are encountered if an attempt is made, using data on real product wages, to frame policies on the basis of a classification of unemployment as either 'Classical' or 'Keynesian'.

First, labour productivity has often behaved procyclically in the past and even now there is almost certainly a cyclical influence on productivity, and hence on real product wages, even if that influence is in some cases swamped by other factors.

Second, there may be confusion between the symptoms of a wage problem and those of a demand shortfall. Thus in a large, relatively closed economy where mark-up pricing was prevalent, a wages push (or a fall in productivity following some other supply shock) might be more likely to result in higher prices and interest rates and in a loss of price competitiveness, and thence 'Keynesian' unemployment' than in the emergence of excessive real wages and thence 'classical' unemployment, even though the problem could be thought of as initially arising on the supply side. By contrast, in a small, open economy a shortfall of world demand might manifest itself principally in downward pressure on output prices. If wages did not adjust, the real product wage would rise in the short run (before the process of an induced rise in productivity started) and might be followed by a fall in employment. Analysts could easily be led into classifying this fall in employment as a 'classical' or supply-side phenomenon, even though the root of the problem was a shortage of demand.

4. Monetary and budgetary concepts and definitions

4.1 Money supply

Each country uses several definitions of money supply, which do not coincide with those of other countries since financial structures and behaviour mean not only that some assets are regarded as money in one country but not in another, but even that definitions in the same country may change as structures and behaviour evolve.

The basic elements for defining the money supply are:

(a) the characteristics of monetary assets;

(b) the holders of monetary assets;

(c) the issuers of monetary assets.

There are two main definitions of money supply: money supply narrowly defined (M1), comprising circulating coins and notes and current bank accounts; money supply broadly defined (M2 or M3), comprising M1 and various assets with

banks and other financial institutions in the form of deposit accounts, savings accounts or short-term notes. The principal components of money supply broadly defined (M2 or M3) for each country are described below.

Belgium: Money supply broadly defined (M2).

(a) *Monetary assets:* Coins and notes, current bank accounts and all other assets with a maximum maturity of one year in national or foreign currency.

(b) *Holders:* Resident households and private firms.

(c) *Issuers:* Central bank, commercial banks and other financial intermediaries; the figures from 1982 onwards include monetary claims on the external sector.

Denmark: Money supply broadly defined (M2: new definition from 1975).

(a) *Monetary assets:* Coins and notes, current bank accounts, deposit accounts, foreign currency deposits, Treasury bills.

(b) *Holders:* Resident households and firms, non-monetary financial institutions, local authorities.

(c) *Issuers:* Central bank, commercial banks, main savings banks, postal service.

FR of Germany: Money supply broadly defined (M3).

(a) *Monetary assets:* Coins and notes, current bank accounts except those of the authorities with the central bank, deposit accounts, banking commitments up to four years, savings accounts with a legal period of notice, foreign currency deposits.

(b) *Holders:* Resident households and firms, local authorities.

(c) *Issuers:* Central bank, commercial banks, with the exception of building societies.

Greece: Money supply broadly defined (M3).

(a) *Monetary assets:* Coins and notes, current accounts' savings and deposit accounts.

(b) *Holders:* Resident households and firms, public authorities.

(c) *Issuers:* Central bank, commercial banks and special credit institutions.

France: Money supply broadly defined (M2R from 1982).

(a) *Monetary assets:* Coins and notes, current bank accounts, current bank books, five year home-purchase saving plans, time deposits (all maturities), bank tap notes up to five years, foreign currency accounts.

(b) *Holders:* Resident households and firms, certain central government agencies, local authorities, social security funds.

(c) *Issuers:* Central bank and commercial banks, postal cheque office, *banques populaires,* cooperative banks, savings banks, Treasury.

Ireland: Money supply broadly defined (M3).

(a) *Monetary assets:* Coins and notes, current and deposit accounts.

(b) *Holders:* Resident households and firms, including government and local authority deposits with licensed banks.

(c) *Issuers:* Central bank and licensed banks.

Italy: Money supply broadly defined (M3).

(a) *Monetary assets:* Coins and notes, current and deposit accounts, current accounts in foreign currency, savings accounts, postal savings certificates, Treasury bonds up to 12 months, foreign currency deposits.

(b) *Holders:* Resident households and firms, local authorities, social security funds.

(c) *Issuers:* Central bank, commercial banks, savings banks, Treasury postal service.

The Netherlands: Money supply broadly defined (M2).

(a) *Monetary assets:* Coins and notes, current bank and post office accounts, bank and post office time deposits up to two years, foreign currency deposits, savings accounts with high velocity of circulation, Treasury liabiltiies in the form of bonds, certificates and loans or deposits, and liabilities up to two years of the *Bank voor Nederlandsche Gemeenten* and the *Nederlandse Waterschapbank.*

(b) *Holders:* Resident households and firms, local authorities.

(c) *Issuers:* Central bank and commercial banks, Treasury and local authorities.

United Kingdom: Money supply broadly defined (sterling M3).

(a) *Monetary assets:* Coins and notes, all types of sterling bank deposits including certificates of deposit.

(b) *Holders:* Resident households and firms, general government.

(c) *Issuers:* Central bank, commercial banks, discount houses.

4.2 **Monetary targets**

At present, monetary targets are set in Germany, France, Italy, the United Kingdom, Ireland and Greece.

The aggregates used are as follows:

FR of Germany: Central bank money (MZ), comprising notes in circulation and compulsory reserves of banks calculated as a constant fraction of residents' claims on banks: 16,6% on current accounts, 12,4% on deposit accounts, 8,1% on savings accounts.

Greece: Private sector bank credit (PSCE) and notes in circulation (MO).

France: Money supply broadly defined (M2). M2 is equal to M2R plus the deposits of non-residents.

Ireland: Private sector credit (PSCE): lending by licensed banks in Irish pounds and foreign currency to households, private firms and State-sponsored bodies.

Italy: Total domestic credit (TDCE), including bank loans and loans from special credit institutions, bonds issued by firms and local authorities, and the public sector borrowing requirement (Treasury, Cassa Depositi e Prestiti, Cassa del Mezzogiorno and public utilities, except Treasury financing of financial intermediaries).

United Kingdom: Broadly defined money supply, national currency (£ M3) and, from March 1982, money supply narrowly defined (M1) and private sector liquidity 2 (PSL2 = £ M3 plus deposits with savings institutions, securities issued by these institutions and money market instruments held outside the banking system).

4.3 **Counterparts of the money supply**

The money supply and its counterparts are analysed on the basis of the consolidated balance sheet of money-creating financial institutions which is analysed into:

(a) *public sector credit;*

(b) *private sector credit;*

(c) *miscellaneous items,* covering residual items which vary from country to country;

(d) *external contribution,* the balance of financial institutions' external liabilities and claims;

(e) *non-monetary liabilities,* covering medium-term and long-term liabilities and, for some countries, proprietors' funds.

Domestic money creation is the sum of aggregates (a), (b), (c) minus the amount of aggregate (e).

In countries where the Treasury and other public institutions have monetary liabilities (coinage, short-term Treasury bonds, etc.), these are included as liabilities in the consolidate account of financial institutions, and an equivalent amount is added under the heading for public sector credit.

National monetary analyses also differ according to the definitions of the three sectors: public sector, private sector, foreign sector. For example, loans to local authorities and social security funds may be included either in public sector or in private sector credit, and banking claims on non-bank non-residents may be included either in the private sector or in the foreign sector.

In the following descriptions, the financial institutions are those described as issuers of the money supply in Section 4.1 'Money supply'.

Belgium:

(a) *Public sector credit:* Net claims (loans and purchases of securities) of financial institutions on general government (except social security funds) and net foreign borrowing by general government.

(b) *Private sector credit:* Claims of financial institutions on households and firms.

(c) *Miscellaneous:* Capital and own resources, items in transit, statistical residuals, social security debt.

(d) *External contribution:* Net external position of financial institutions plus net foreign borrowing by general government.

(e) *Non-monetary commitments:* Claims, with maturities of more than one year by firms and households on the financial institutions.

Denmark:

(a) *Public sector credit:* Net claims (loans and purchases of securities) of financial institutions on central government (including public borrowing abroad sterilized in the central bank).

(b) *Private sector credit:* Claims of financial institutions on households and firms, local authorities public sector undertakings and non-money-creating financial institutions.

(c) *Miscellaneous:* Capital and own resources, items in transit, statistical residuals.

(d) *External contributions:* Surplus on current external payments, net borrowing abroad by business, local government authorities, etc. and net sales of krone-denominated bonds to non-residents.

(e) *Non-monetary liabilities:* None.

FR of Germany:

(a) *Public sector credit:* Claims (loans and purchases of securities at issue) of financial institutions on general government.

(b) *Private sector credit:* Claims (loans and purchases of securities) of financial institutions on household and firms, the railways, federal postal services, State corporations and home-savings institutions.

(c) *Miscellaneous:* Items in transit, statistical residuals, authorities' deposits with the central bank.

(d) *External contribution:* Net external position of financial institutions, including balance on financial institutions' foreign dealings in securities.

(e) *Non-monetary liabilities:* Liabilities of financial institutions other than M3 held by households, firms and authorities.

Greece:

(a) *Public sector credit:* Claims (loans and purchases of securities) of financial institutions on central government, local authorities, social security and public corporations.

(b) *Private sector credit:* Claims (loans and purchases of securities) of financial institutions on households and private firms.

(c) *Miscellaneous:* None.

(d) *External contribution:* Net external position of financial institutions.

(e) *Non-monetary liabilities:* Private blocked deposits, deposits, other than sight deposits, of authorities, securities issued by financial institutions, items in transit, capital and reserves.

France:

(a) *Public sector credit:* Claims (loans and purchases of Treasury bonds) of financial institutions on the Treasury, postal cheque deposits and deposits with Treasury branches.

(b) *Private sector credit:* Loans to households, firms and local authorities, excluding loans to non-resident households and firms.

(c) *Miscellaneous:* Items in transit.

(d) *External contributions:* Net external position of money creating banks.

(e) *Non-monetary liabilities:* The balance between certain liabilities of financial institutions (capital, reserves, securities issued) and certain assets (buildings and securities portfolio); net commitments towards other financial intermediaries.

Ireland:

(a) *Public sector credit:* Loans by financial institutions to central government, local authorities and State-sponsored bodies (net of central government deposits with the central bank), plus government bond issues to finance the purchase of agricultural products on behalf of the EEC.

(b) *Private sector credit:* Loans by financial institutions to households and private firms, not including purchase of government bonds issued to finance the purchase of agricultural products on behalf of the EEC.

(c) *Miscellaneous:* None.

(d) *External contribution:* Net external position of licensed banks, official external reserves.

(e) *Non-monetary liabilities:* Items in transit, capital and reserves.

Italy: Balance sheet of financial institutions consolidated with supply and demand in the securities market.

(a) *Public sector credit:* Borrowing requirement of Treasury and other government agencies, excluding public financing of the private sector and foreign borrowing.

(b) *Private sector credit:* Claims of financial institutions and special credit institutions on households firms, local authorities and social security funds; net issue of private bonds and shares not held by financial institutions.

(c) *Miscellaneous:* Capital and own resources, items in transit.

(d) *External contributions:* Net external position of financial institutions.

(e) *Non-monetary liabilities:* Assets of households and firms consisting of: deposits with special credit institutions (ICS), bank acceptances, bonds issued by firms and ICS, public securities and shares.

The Netherlands:

(a) *Public sector credit:* Short-term loans by financial institutions to central government and local authorities.

(b) *Private sector credit:* Short-term and long-term loans to households, firms in the private and public sectors and institutional investors, as well as investments on the capital market.

(c) *Miscellaneous:* Items in transit and statistical adjustment.

(d) *External contribution:* Net external position of financial institutions and Treasury.

(e) *Non-monetary liabilities:* Liabilities of financial institutions other than M2 held by housholds, firms, institutional investors and the authorities, and the capital and own resources of financial institutions.

United Kingdom:

(a) *Public sector credit:* Net claims of commercial banks, the Banking and Issue Departments of the Bank of England and the Exchange Equalization Account on general government and public corporations.

(b) *Private sector credit:* Loans by banks to the private sector and commercial bills held by the Issue Department of the Bank of England.

(c) *Miscellaneous:* Net claims by banks on residents in foreign currency.

(d) *External contribution:* Net external position of commercial banks; official reserves net of liabilities to IMF.

(e) *Non-monetary liabilities:* Liabilities of financial institutions other than sterling M3 including capital and reserves.

4.4 Components of changes in budget deficits

The calculation is intended to break down the actual year-to-year change in the budget deficit into a number of components which may be useful for purposes of policy analysis.

The calculation is based on the definition:

$$dB = dA + dI + dR,$$

where dB is the actual change in the deficit, dA is the effect on the deficit of changes in the level on activity (see below), dI is the effect of changes in net interest payments (receipts) from general government to (from) other domestic and foreign sectors, and dR is the residual component. dR is identified with the effects of changes in budgetary policy, defined in terms of changes in the average net tax rate (taxes, social security contributions and other government charges, minus transfers other than interest flows and unemployment benefits, expressed as a percentage of GDP) and changes in general government consumption and investment spending as a percentage of potential output.

The effect of a change in activity on the budget balance in a given year is here defined as the difference between the actual budget balance and what the budget balance would have been had activity, defined as the ratio of actual to potential output, in that year been at the same level as in the previous year. Changes in activity affect the budget balance through changes in taxes and transfers under a given set of tax/transfer rules. (General government consumption and investment is assumed to be unaffected by variations in the level of activity.) In the calculations, a single marginal overall tax rate is used and is assumed to be equal to the average tax rate. Social transfers vary with the level of unemployment.

The methodology does not necessarily imply that deviations of actual from potential output are 'cyclical' or represent either an excess or an insufficiency of aggregate demand. The notion of potential output, as used here, can be seen simply as corresponding to the expected trend of output; random supply disturbances can thus equally well cause deviations of actual from potential output.

A plus sign in the table indicates a reduction in the budget deficit. Thus, for example, in a year in which activity, as defined here, declined dA would be negative. If both dI and dB were zero dR would be positive and equal in (algebraic) magnitude to dA, indicating that discretionary changes in budgetary policy worked in the direction of reducing the deficit.

5. Labour force, employment, unemployment and hours worked definitions

The civilian labour force in the Community and Member States comprises all persons employed (including self-employed and family workers but excluding the armed forces) plus the unemployed. The national concept is used: all employed or unemployed persons resident in the territory of the country in question are included. Basic data are annual averages except for Belgium, Greece and the United Kingdom, where the data relate to 30 June of each year.

Total employment in the Community and Member States includes all persons in employment or self-employment, as well as family workers. The domestic concept is used: all persons employed or self-employed within the territory of the country in question, whether or not they are resident, are included.

The *unemployment rate* in the Community and Member States is defined as the number unemployed as a percentage of the civilian labour force; data for numbers unemployed and the labour force relate to the same year, i.e. the 1981 unemployment rate is the average number unemployed in 1981 as a percentage of the 1981 labour force. Rates for 1970-82 are historical data supplied by Eurostat; 1983-84 rates are estimates using Eurostat definitions based on forecasts, prepared by the Commission departments, for numbers unemployed and the labour force. Data for *unemployed persons* are derived from statistics of registered unemployed supplied to Eurostat by national agencies in accordance with standardized procedures: in principle, the definition of unemployed persons covers persons without a job, seeking employment as an employee and immediately available for work. For more specific detail on the individual series for Member States, see *Employment and Unemployment* (Eurostat, 1983).

Total hours is obtained by multiplying the number of employees by the average number of hours worked per employee (average hours).

5.1 *The Community labour force survey* is a sample survey, harmonized and synchronized, carried out every two years ince 1973 in each Member State (from 1981 onwards in Greece), in a sample of households resident in these Member States at the time of the survey. The sample size is between 60 000 and 100 000 households in the Federal Republic of Germany, France, Italy and the Untied Kingdom; between 30 000 and 50 000 for Belgium, Greece, the Netherlands and Ireland; between 30 000 and 40 000 for Denmark and around 10 000 for Luxembourg. Information is gathered on each of the members of the households included in the sample. The survey covers: (a) the individual characteristics of these persons; (b) their employment activity (occupational status, branch of activity hours of work, etc.) at the time of the survey and one year before it; (c) job search, taking account of the type of employment sought and the methods and duration of search; (d) participation in training courses; (e) employment experience of working-age people without an occupation.

The results of the survey are published in *Labour Force Sample Survey* (Eurostat, 1980, 1981).

Table A1

Competitiveness weighting matrix

(1980 trade flows - export aspect)

	B/L	DK	D	GR	F	IRL	I	NL	UK	EC [1]
Belgium/Luxembourg	—	3,1	5,8	4,1	6,4	5,0	5,4	9,7	5,6	—
Denmark	1,3	—	1,6	1,2	1,1	1,2	1,2	1,8	1,7	—
FR of Germany	24,1	21,4	—	16,5	16,6	11,9	18,4	23,6	15,1	—
Greece	0,5	0,6	1,1	—	1,0	0,4	1,2	0,8	0,6	—
France	18,7	8,2	16,6	12,8	—	8,1	13,2	12,5	10,0	—
Ireland	0,5	0,6	0,5	0,4	0,6	—	0,6	0,7	2,9	—
Italy	7,6	6,8	10,9	12,7	14,6	6,0	—	7,8	6,3	—
The Netherlands	10,5	4,9	8,8	7,0	7,7	6,8	7,0	—	7,2	—
United Kingdom	10,1	13,3	10,4	8,9	11,5	30,0	10,8	11,7	—	—
Norway	1,2	4,3	1,4	0,9	1,2	2,3	1,1	1,6	1,5	2,2
Sweden	2,2	9,2	3,5	1,8	2,4	2,2	2,3	2,9	3,9	8,7
Austria	1,2	1,4	5,0	1,9	1,8	1,0	3,0	2,0	1,4	6,3
Switzerland	3,6	2,6	5,5	2,3	4,9	1,8	4,9	3,5	5,8	8,5
Japan	4,2	5,5	6,6	8,0	7,3	4,1	7,6	4,9	8,6	21,2
Canada	1,2	1,5	1,9	1,9	1,9	2,2	1,9	1,3	2,6	4,2
USA	9,4	11,1	14,6	14,7	14,5	12,6	15,2	10,6	19,6	35,7
Austria	0,7	0,9	1,2	1,4	1,0	1,0	1,2	0,8	2,1	4,4
Spain	1,7	1,5	2,3	1,8	3,6	1,9	3,2	2,1	2,6	5,7
Portugal	0,5	0,5	0,7	0,5	0,8	0,5	0,7	0,6	0,9	—
Finland	0,8	2,6	1,6	1,2	1,1	1,0	1,1	1,1	1,6	3,1
	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0

[1] Fixed 1974 weights.

Note: The figures in each column show the importance, on all markets, of the countries listed on the left of the table as trading partners and competitors of the countries listed in the head of the table.

Statistical annex

Notes on the statistical annex

General remarks

This year's November edition of *European Economy* again gives in its statistical annex updated time series of annual data, starting in 1958 with the beginning of the European Economic Community.

Unless otherwise specified, aggregates up to 1981 are defined as in the ESA (European System of Economic Accounts). National accounts figures for 1958 and 1959, generally not available in terms of ESA, have been adjusted as far as possible but are not fully comparable with subsequent years. National accounts figures for 1982 and 1983 are estimates and forecasts made by Commission staff using the definitions and latest figures available from national sources, and so they are not fully comparable with ESA figures for earlier years. However, in those tables showing the level and structure of GDP (Tables 4, 6, 7, 10, 12, 14, 16, 26, 30) an attempt has again been made to avoid major discontinuities by projecting forward ESA figures from 1980 using estimates of volume and price changes in 1982 and 1983.

Community totals are for EC 10 unless otherwise stated. Community totals for national accounts data are aggregated using purchasing power parities, except in Tables 6, 28, 29, 32-34, 45-47, where current exchange rates have been used.

List of tables

Table 1

Population; total

('000 persons)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	9 024	4 515	54 292	8 173	44 789	2 853	49 476	311	11 185	51 870	236 488
1959	9 072	4 547	54 876	8 258	45 240	2 846	49 831	313	11 347	52 157	238 487
1960	9 119	4 581	55 433	8 327	45 684	2 832	50 198	314	11 483	52 559	240 530
1961	9 166	4 617	56 175	8 398	46 163	2 818	50 523	317	11 637	52 954	242 768
1962	9 218	4 647	56 837	8 448	46 998	2 830	50 843	321	11 801	53 414	245 357
1963	9 283	4 684	57 389	8 480	47 816	2 850	51 198	324	11 964	53 691	247 679
1964	9 367	4 720	57 971	8 510	48 310	2 864	51 600	328	12 125	54 033	249 828
1965	9 448	4 758	58 619	8 550	48 758	2 876	51 987	331	12 293	54 378	251 999
1966	9 508	4 797	59 148	8 612	49 164	2 884	52 332	334	12 455	54 653	253 887
1967	9 556	4 839	59 286	8 716	49 548	2 900	52 667	335	12 597	54 933	255 377
1968	9 590	4 867	59 500	8 741	49 914	2 913	52 987	336	12 726	55 157	256 731
1969	9 613	4 891	60 067	8 773	50 318	2 929	53 317	338	12 873	55 372	258 490
1970	9 638	4 929	60 651	8 793	50 772	2 950	53 661	339	13 032	55 522	260 287
1971	9 672	4 963	61 284	8 831	51 251	2 978	54 005	342	13 194	55 712	262 233
1972	9 709	4 992	61 672	8 889	51 701	3 024	54 412	347	13 330	55 869	263 945
1973	9 738	5 022	61 976	8 929	52 118	3 073	54 913	350	13 438	56 000	265 558
1974	9 768	5 045	62 054	8 962	52 460	3 124	55 413	355	13 543	56 011	266 735
1975	9 795	5 060	61 829	9 047	52 705	3 177	55 830	359	13 660	55 981	267 443
1976	9 811	5 073	61 531	9 167	52 891	3 228	56 168	361	13 773	55 959	267 962
1977	9 822	5 088	61 400	9 308	53 077	3 272	56 461	361	13 856	55 919	268 564
1978	9 830	5 104	61 327	9 430	53 277	3 314	56 714	362	13 939	55 902	269 199
1979	9 837	5 117	61 359	9 548	53 480	3 368	56 914	363	14 034	55 946	269 966
1980	9 847	5 123	61 567	9 642	53 714	3 401	57 070	364	14 148	56 010	270 886
1981	9 852	5 122	61 682	9 740	53 962	3 443	57 197	366	14 247	56 290	271 901
1982	9 858	5 118	61 639	9 820	54 579	3 483	57 340	366	14 312	56 337	272 853
(1983)	9 864	5 114	61 639	9 900	54 835	3 523	57 434	366	14 363	56 395	273 433

Table 2

Employment; total economy

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	−1,1	0,7	0,4	:	−0,3	−1,5	0,0	0,0	−0,9	−1,1	−0,3
1959	−0,6	3,1	0,9	:	−0,9	−0,7	0,0	0,0	1,0	0,3	0,2
1960	0,3	2,8	1,4	:	0,1	−0,5	−0,2	0,1	1,9	−0,1	0,5
1961	0,8	1,5	1,4	1,1	0,1	−0,2	0,2	1,1	1,5	1,2	0,8
1962	1,6	1,5	0,4	−0,8	0,2	0,7	−1,1	0,3	2,0	0,7	0,2
1963	0,7	1,2	0,2	−0,9	1,0	0,6	−1,6	−0,4	1,4	0,1	0,1
1964	1,3	2,1	0,1	−0,9	1,1	0,5	−0,1	1,7	1,8	1,1	0,6
1965	0,2	1,8	0,6	−0,8	0,4	−0,2	−2,0	0,9	0,9	0,9	0,1
1966	0,5	0,5	−0,3	−0,8	0,8	−0,3	−1,6	0,5	0,8	0,6	−0,0
1967	−0,3	−0,6	−3,3	−0,9	0,3	−0,6	1,2	−1,1	−0,3	−1,5	−1,0
1968	−0,1	1,1	0,1	−0,9	−0,1	0,3	−0,2	−0,4	0,9	−0,7	−0,2
1969	1,7	0,9	1,6	−0,8	1,7	0,3	0,4	1,4	1,7	0,1	0,9
1970	−0,5	0,7	1,3	−0,8	1,0	−1,2	1,2	1,8	1,2	−0,5	0,6
1961-70	0,6	1,1	0,2	−0,7	0,6	−0,0	−0,4	0,6	1,2	0,2	0,2
1971	1,0	0,6	0,3	−0,9	0,4	0,2	−0,1	3,1	0,6	−1,5	−0,2
1972	−0,1	2,1	0,1	0,4	0,5	−0,5	−1,1	2,6	−0,9	−0,1	−0,1
1973	1,3	1,2	0,7	0,5	1,3	0,7	0,8	1,9	0,0	2,4	1,2
1974	1,4	−0,3	−1,3	−0,1	0,7	1,1	1,5	2,5	0,0	0,4	0,2
1975	−1,4	−1,2	−2,8	0,6	−1,0	0,4	0,2	1,6	−0,7	−0,5	−1,1
1976	−0,6	1,8	−0,8	1,3	0,7	−0,8	0,8	−0,6	−0,2	−0,7	−0,0
1977	−0,2	0,8	−0,2	−0,9	0,8	1,8	0,7	0,3	0,2	0,2	0,3
1978	0,1	1,0	0,6	1,6	0,4	2,5	0,6	0,0	0,7	0,1	0,5
1979	1,2	1,2	1,3	1,5	−0,1	3,2	1,0	1,0	1,3	0,9	0,9
1980	−0,1	−0,4	0,9	1,7	0,0	1,6	0,9	1,1	0,5	−1,6	0,1
1971-80	0,3	0,7	−0,1	0,6	0,4	1,0	0,5	1,3	0,2	−0,0	0,2
1981	−2,1	−1,9	−0,7	0,1	−0,7	−1,9	0,5	0,2	−1,3	−5,3	−1,6
1982	−1,7	0,1	−1,9	−1,3	−0,8	−1,1	−0,4	0,1	−2,5	−1,7	−1,3
(1983)	−2,0	−0,4	−2,0	−1,0	−1,0	−2,5	0,5	−1,1	−2,1	−0,6	−0,9

Table 3

Unemployment

(as % of civilian labour force)

	B	DK	D	F	IRL	I	L	NL	UK	EC 9
1958	3,1	3,2	2,9	0,5	5,7	8,1	0,1	1,8	1,9	3,3
1959	3,5	2,2	2,1	0,7	5,4	7,7	0,1	1,2	1,8	3,0
1960	3,1	1,5	1,0	0,7	4,7	7,2	0,1	0,7	1,6	2,5
1961	2,5	1,2	0,7	0,6	4,2	6,6	0,1	0,5	1,4	2,2
1962	2,0	1,1	0,6	0,7	4,2	5,5	0,1	0,5	1,9	2,0
1963	1,5	1,5	0,7	0,7	4,5	5,2	0,2	0,6	2,3	2,1
1964	1,5	0,9	0,6	0,6	4,3	5,2	0,0	0,5	1,6	1,9
1965	1,8	0,7	0,6	0,7	4,5	5,7	0,0	0,6	1,4	1,9
1966	2,0	0,8	0,6	0,7	4,3	5,5	0,0	0,8	1,4	1,9
1967	2,6	1,0	1,8	1,0	4,5	5,0	0,1	1,7	2,2	2,4
1968	3,1	1,7	1,3	1,3	4,8	4,7	0,1	1,5	2,3	2,3
1969	2,3	1,4	0,7	1,1	4,6	4,4	0,0	1,1	2,3	2,0
1970	2,2	1,0	0,6	1,3	5,3	4,4	0,0	1,0	2,5	2,0
1961-70	2,2	1,1	0,8	0,9	4,5	5,2	0,1	0,9	1,9	2,1
1971	2,2	1,2	0,7	1,6	5,2	5,1	0,0	1,3	3,0	2,5
1972	2,8	1,2	0,9	1,8	6,0	5,2	0,0	2,3	3,4	2,7
1973	2,9	0,7	1,0	1,8	5,6	4,9	0,0	2,3	2,4	2,4
1974	3,2	2,0	2,2	2,3	6,0	4,8	0,0	2,8	2,4	2,9
1975	5,3	4,6	4,1	3,9	8,5	5,3	0,2	4,0	3,7	4,3
1976	6,8	4,7	4,1	4,3	9,5	5,6	0,3	4,3	5,1	4,9
1977	7,8	5,8	4,0	4,8	9,2	6,4	0,5	4,1	5,4	5,3
1978	8,4	6,5	3,8	5,2	8,4	7,1	0,7	4,1	5,3	5,4
1979	8,7	5,3	3,3	6,0	7,4	7,5	0,7	4,1	4,9	5,5
1980	9,4	6,1	3,3	6,4	8,3	8,0	0,7	4,7	6,3	6,1
1971-80	5,8	3,8	2,8	3,8	7,4	6,0	0,3	3,4	4,4	4,2
1981	11,6	8,3	4,7	7,8	10,2	8,8	1,0	7,2	9,6	7,9
1982	13,2	8,9	6,8	8,9	12,5	10,5	1,3	12,0	11,1	9,6
(1983)	14,5	10,7	8,6	9,1	15,3	10,8	1,8	15,6	11,7	10,4

Table 4

Gross domestic product at current market prices

('000 million national currencies)

	B	DK	D	GR	F	IRL	I	L	NL	UK
1958	506,6	34,50	246,6	94,2	244,3	0,560	20 107	22,800	35,00	22,80
1959	522,5	38,10	264,9	97,9	265,0	0,600	21 351	23,300	36,80	23,90
1960	557,0	40,94	302,7	105,2	296,5	0,631	23 207	26,029	44,00	25,51
1961	592,4	45,43	331,7	118,6	323,5	0,680	25 810	27,272	46,46	27,24
1962	633,7	51,19	360,8	126,0	361,2	0,736	28 998	27,370	50,01	28,52
1963	681,3	54,49	382,4	140,7	404,9	0,791	33 215	29,484	54,26	30,32
1964	762,5	62,29	420,2	158,0	449,2	0,901	36 360	33,407	63,85	33,08
1965	830,0	69,97	459,2	179,8	483,5	0,959	39 124	35,142	71,31	35,54
1966	892,1	77,18	488,2	200,0	523,4	1,010	42 391	36,799	77,65	37,91
1967	955,3	84,81	494,3	216,1	565,4	1,104	46 695	37,769	85,19	40,04
1968	1 022,3	94,36	533,3	234,5	614,5	1,245	50 614	41,374	94,46	43,38
1969	1 134,2	107,32	596,9	266,5	700,7	1,438	55 876	47,573	106,98	46,44
1970	1 262,1	118,63	675,3	298,9	782,6	1,620	62 883	54,043	120,50	50,93
1971	1 382,0	131,12	750,6	332,3	872,4	1,853	68 510	55,970	136,36	57,16
1972	1 545,4	150,73	823,7	377,9	981,1	2,237	75 124	62,414	154,32	63,27
1973	1 755,0	172,86	917,3	484,2	1 114,2	2,701	89 746	76,405	176,80	72,84
1974	2 056,8	193,63	984,6	564,5	1 278,3	2,987	110 719	93,242	200,13	82,92
1975	2 271,1	216,26	1 026,5	672,2	1 452,3	3,728	125 378	86,631	220,25	104,49
1976	2 574,6	251,21	1 119,7	824,9	1 678,0	4,570	156 657	99,504	252,59	124,24
1977	2 780,3	279,31	1 196,1	963,7	1 884,6	5,492	190 083	101,869	274,93	143,40
1978	2 984,5	311,38	1 285,1	1 161,4	2 141,1	6,437	222 254	112,084	297,01	164,95
1979	3 182,0	346,89	1 392,5	1 428,9	2 439,6	7,448	270 198	123,322	315,96	192,95
1980	3 415,9	373,30	1 481,1	1 710,6	2 758,7	8,719	339 068	135,200	335,85	225,54
1981	3 530,3	414,11	1 543,9	2 033,8	3 094,4	10,376	398 125	143,202	350,54	247,72
1982	3 816,8	470,41	1 600,5	2 550,9	3 552,8	12,271	466 080	152,862	364,54	271,02
(1983)	4 053,2	516,44	1 661,1	3 048,6	3 888,8	13,641	531 912	161,466	371,41	292,42

Table 5

Gross domestic product at current market prices

(national currency, annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	0,8	4,5	7,1	5,1	15,1	3,6	7,4	−1,2	0,8	4,2	7,6
1959	3,1	10,9	7,4	3,9	8,5	6,9	6,2	2,8	5,1	4,8	6,6
1960	6,6	7,9	14,3	7,5	11,9	5,8	8,7	8,9	13,6	6,7	10,4
1961	6,4	11,0	9,6	12,8	9,1	7,7	11,2	4,8	5,6	6,8	8,9
1962	7,0	12,7	8,8	6,2	11,7	8,3	12,4	0,4	7,7	4,7	8,8
1963	7,5	6,4	6,0	11,7	12,1	7,5	14,5	7,7	8,5	6,3	8,9
1964	11,9	14,3	9,9	12,3	10,9	13,8	9,5	13,3	17,7	9,1	10,4
1965	8,8	12,3	9,3	13,8	7,6	6,5	7,6	5,2	11,7	7,4	8,4
1966	7,5	10,3	6,3	11,2	8,3	5,4	8,4	4,7	8,9	6,7	7,5
1967	7,1	9,9	1,3	8,1	8,0	9,2	10,2	2,6	9,7	5,6	6,1
1968	7,0	11,3	7,9	8,5	8,7	12,8	8,4	9,5	10,9	8,3	8,8
1969	10,9	13,7	11,9	13,6	14,0	15,5	10,4	15,0	13,3	7,1	11,2
1970	11,3	10,5	13,1	12,2	11,7	12,6	12,5	13,6	12,6	9,7	12,3
1961-70	8,5	11,2	8,4	11,0	10,2	9,9	10,5	7,6	10,6	7,2	9,1
1971	9,5	10,5	11,1	11,2	11,5	14,4	8,9	3,5	13,2	12,2	11,2
1972	11,8	15,0	9,8	13,7	12,5	20,8	9,7	11,5	13,2	10,7	11,1
1973	13,6	14,7	11,4	28,1	13,6	20,7	19,5	22,4	14,6	15,1	15,0
1974	17,2	12,0	7,3	16,6	14,7	10,6	23,4	22,0	13,2	13,8	13,4
1975	10,4	11,7	4,3	19,1	13,6	24,8	13,2	−7,1	10,1	26,0	12,2
1976	13,4	16,2	9,1	22,7	15,5	22,6	24,9	14,9	14,7	18,9	14,7
1977	8,0	11,2	6,8	16,8	12,3	20,2	21,3	2,4	8,8	15,4	11,2
1978	7,3	11,5	7,4	20,5	13,6	17,2	16,9	10,0	8,0	15,0	10,9
1979	6,6	11,4	8,4	23,0	13,9	15,7	21,6	10,0	6,4	17,0	12,5
1980	7,4	7,6	6,4	19,7	13,1	17,1	25,5	9,6	6,3	16,9	12,5
1971-80	10,5	12,1	8,2	19,1	13,4	18,3	18,4	9,6	10,8	16,0	12,5
1981	3,3	10,9	4,2	18,9	12,2	19,0	17,4	5,9	4,4	9,8	9,3
1982	8,1	13,6	3,7	25,4	14,8	18,3	17,1	6,7	4,0	9,4	9,0
(1983)	6,2	9,8	3,8	19,5	9,5	11,2	14,1	5,6	1,9	7,9	6,4

Table 6

Gross domestic product at current prices

('000 million ECU)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	9,2	4,6	53,5	2,9	53,0	1,4	29,3	0,4	8,4	58,2	220,9
1959	9,9	5,2	59,7	3,1	50,8	1,5	32,3	0,4	9,2	63,4	235,5
1960	10,5	5,6	68,2	3,3	56,9	1,7	35,2	0,5	11,0	67,6	260,5
1961	11,1	6,2	77,0	3,7	61,4	1,8	38,7	0,5	11,9	71,5	283,7
1962	11,8	6,9	84,3	3,9	68,4	1,9	43,4	0,5	12,9	74,6	308,8
1963	12,7	7,4	89,4	4,4	76,7	2,1	49,7	0,6	14,0	79,4	336,2
1964	14,3	8,4	98,2	4,9	85,0	2,4	54,4	0,6	16,5	86,6	371,3
1965	15,5	9,5	107,3	5,6	91,5	2,5	58,5	0,7	18,4	93,0	402,5
1966	16,7	10,4	114,1	6,2	99,1	2,6	63,4	0,7	20,1	99,2	432,6
1967	17,9	11,4	116,1	6,8	107,5	2,8	70,2	0,7	22,1	103,3	458,9
1968	19,9	12,2	129,6	7,6	121,0	2,9	78,7	0,8	25,4	101,2	499,2
1969	22,2	14,0	148,3	8,7	132,4	3,4	87,5	0,9	28,9	109,0	555,3
1970	24,7	15,5	180,5	9,7	137,8	3,8	98,4	1,1	32,6	119,6	623,7
1971	27,2	16,9	205,9	10,6	151,1	4,3	105,8	1,1	37,3	133,4	693,6
1972	31,3	19,4	230,3	11,2	173,4	5,0	114,8	1,3	42,9	140,9	770,5
1973	36,7	23,3	280,0	13,1	203,8	5,4	125,3	1,6	51,6	145,0	885,7
1974	44,3	26,7	319,3	15,8	222,9	5,9	142,7	2,0	62,5	162,7	1 004,8
1975	49,8	30,4	336,6	16,8	273,0	6,7	154,9	1,9	70,3	186,6	1 126,9
1976	59,6	37,2	397,7	20,2	313,9	7,4	168,4	2,3	85,5	199,9	1 292,0
1977	68,0	40,7	451,7	22,9	336,2	8,4	188,8	2,5	98,2	219,4	1 436,7
1978	74,5	44,4	502,8	24,8	373,0	9,7	205,7	2,8	107,8	248,5	1 594,0
1979	79,2	48,1	554,6	28,1	418,5	11,1	237,3	3,1	115,0	298,5	1 793,5
1980	84,1	47,7	586,7	28,8	470,0	12,9	285,1	3,3	121,7	376,8	2 017,3
1981	85,5	52,3	614,2	33,0	512,3	15,0	315,2	3,5	126,3	447,9	2 205,1
1982	85,4	57,7	673,8	39,0	552,9	17,8	352,6	3,4	139,5	480,8	2 403,0
(1983)	89,6	63,5	732,2	39,3	576,1	19,0	394,4	3,6	146,4	493,5	2 557,5

Table 7

Gross domestic product per head of population

(ECU)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	1 024	1 008	986	355	1 183	499	592	1 337	751	1 122	934
1959	1 091	1 148	1 088	375	1 123	557	649	1 407	808	1 216	987
1960	1 157	1 225	1 231	399	1 245	591	700	1 570	955	1 287	1 083
1961	1 211	1 335	1 371	441	1 330	633	766	1 613	1 024	1 349	1 169
1962	1 285	1 491	1 483	465	1 455	680	853	1 595	1 094	1 397	1 258
1963	1 372	1 574	1 557	517	1 603	727	970	1 701	1 171	1 478	1 357
1964	1 522	1 786	1 694	579	1 760	823	1 054	1 905	1 360	1 602	1 486
1965	1 642	1 990	1 831	655	1 877	873	1 126	1 982	1 498	1 711	1 597
1966	1 754	2 177	1 929	723	2 016	917	1 211	2 060	1 610	1 816	1 704
1967	1 878	2 361	1 958	776	2 171	982	1 332	2 118	1 754	1 880	1 797
1968	2 072	2 512	2 178	869	2 424	997	1 485	2 394	1 993	1 835	1 945
1969	2 309	2 862	2 468	990	2 632	1 153	1 640	2 758	2 246	1 969	2 148
1970	2 562	3 139	2 976	1 109	2 715	1 289	1 834	3 117	2 499	2 154	2 396
1971	2 809	3 408	3 359	1 197	2 949	1 452	1 959	3 214	2 826	2 394	2 645
1972	3 225	3 876	3 734	1 263	3 354	1 648	2 110	3 648	3 216	2 522	2 919
1973	3 770	4 641	4 517	1 467	3 910	1 750	2 281	4 560	3 838	2 589	3 335
1974	4 538	5 287	5 146	1 760	4 250	1 876	2 576	5 659	4 615	2 903	3 767
1975	5 088	6 000	5 444	1 858	5 180	2 095	2 774	5 296	5 143	3 333	4 214
1976	6 079	7 324	6 463	2 201	5 936	2 278	2 999	6 389	6 206	3 572	4 822
1977	6 924	8 007	7 356	2 463	6 334	2 568	3 344	6 893	7 086	3 923	5 350
1978	7 579	8 691	8 198	2 633	7 002	2 926	3 628	7 727	7 737	4 444	5 921
1979	8 053	9 404	9 038	2 948	7 825	3 303	4 170	8 458	8 191	5 335	6 644
1980	8 545	9 309	9 530	2 991	8 751	3 792	4 996	9 139	8 600	6 728	7 447
1981	8 677	10 205	9 957	3 389	9 494	4 361	5 510	9 483	8 866	7 956	8 110
1982	8 661	11 274	10 931	3 975	10 131	5 099	6 149	9 334	9 750	8 535	8 807
(1983)	9 081	12 414	11 879	3 966	10 506	5 402	6 867	9 750	10 193	8 752	9 353

Table 8

Gross domestic product at 1975 market prices

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	−0,7	2,6	3,4	3,4	3,0	−2,1	4,9	:	−1,0	0,4	2,2
1959	2,3	6,4	6,6	3,7	2,6	4,5	6,1	3,8	3,9	3,8	4,7
1960	5,8	6,6	10,5	3,8	7,2	5,8	6,7	5,6	9,9	5,0	7,6
1961	5,0	6,4	5,2	11,1	5,5	5,0	8,2	4,4	2,9	3,3	5,2
1962	5,2	5,7	4,5	1,5	6,7	3,2	6,2	1,4	4,3	1,0	4,3
1963	4,3	0,6	3,2	10,1	5,3	4,8	5,6	2,6	3,3	3,9	4,3
1964	6,9	9,3	6,7	8,3	6,5	3,8	2,8	7,5	8,6	5,2	5,8
1965	3,6	4,6	5,5	9,4	4,8	1,9	3,3	1,7	5,3	2,3	4,1
1966	3,2	6,4	2,7	6,1	5,2	0,9	6,0	1,7	2,7	2,0	3,7
1967	3,9	3,7	0,0	5,5	4,7	5,8	7,2	1,6	5,3	2,6	3,4
1968	4,2	3,8	5,7	6,7	4,3	8,2	6,5	4,2	6,4	4,1	5,2
1969	5,9	6,5	7,4	9,9	7,0	5,9	6,1	8,9	6,4	1,5	5,6
1970	6,2	2,3	5,2	8,0	5,7	2,7	5,3	2,2	6,7	2,2	4,8
1961-70	4,8	4,9	4,6	7,6	5,6	4,2	5,7	3,6	5,2	2,8	4,6
1971	3,9	2,4	3,3	7,1	5,4	3,5	1,6	4,3	4,3	2,7	3,4
1972	5,3	5,4	4,2	8,9	5,9	6,5	3,2	6,2	3,4	2,2	4,1
1973	6,2	3,8	4,5	7,3	5,4	4,7	7,0	10,8	5,7	7,5	5,9
1974	4,4	−0,7	0,7	−3,6	3,2	4,3	4,1	3,6	3,5	−1,0	1,7
1975	−1,9	−1,0	−1,6	6,0	0,2	2,0	−3,6	−6,1	−1,0	−0,7	−1,2
1976	5,7	6,9	5,4	6,4	4,9	1,9	5,9	1,9	5,3	3,6	5,0
1977	0,7	2,0	3,1	3,4	3,1	6,8	1,9	0,6	2,4	1,3	2,4
1978	3,0	1,8	3,1	6,7	3,3	5,9	2,7	4,5	2,7	3,7	3,2
1979	2,4	3,7	4,1	3,7	3,2	2,5	4,9	4,0	2,1	1,6	3,3
1980	3,0	−1,1	1,9	1,6	1,3	2,8	3,9	1,7	0,9	−2,0	1,3
1971-80	3,2	2,3	2,8	4,7	3,6	4,1	3,1	3,1	2,9	1,9	2,9
1981	−1,8	0,1	0,2	−0,7	0,2	1,1	−0,2	−1,8	−1,2	−2,0	−0,4
1982	1,0	3,4	−1,0	−0,0	1,8	1,2	−0,3	−1,1	−1,6	1,5	0,4
(1983)	−0,9	2,2	0,7	−0,2	−0,3	0,5	−0,8	−2,4	0,3	2,7	0,5

Table 9

Industrial production

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	−4,7	3,0	2,6	:	4,0	3,0	3,6	−4,3	2,2	−1,3	1,7
1959	4,6	11,5	7,1	:	1,1	8,8	10,6	4,5	8,7	5,2	5,7
1960	6,8	8,7	11,7	:	8,9	6,9	16,7	9,0	10,0	6,8	10,1
1961	6,2	5,1	6,1	:	5,5	8,5	9,5	2,9	3,6	0,0	4,8
1962	5,7	8,9	8,4	:	5,1	7,2	7,8	−4,2	3,5	1,1	5,7
1963	7,4	1,3	3,5	10,1	6,0	5,9	7,8	1,0	5,1	4,0	4,8
1964	6,5	11,7	7,8	10,8	6,2	7,6	1,3	9,2	9,7	7,9	6,8
1965	2,5	6,6	5,3	8,8	1,6	4,2	3,8	0,8	4,4	3,3	3,8
1966	2,0	2,9	1,2	15,7	5,9	3,2	12,0	−3,2	4,2	1,4	3,6
1967	1,8	3,9	−2,6	4,7	2,4	7,9	8,9	−0,6	2,7	0,2	1,1
1968	5,5	7,4	9,4	7,7	3,5	10,5	6,7	6,0	9,2	6,4	7,0
1969	9,7	12,4	12,9	11,8	10,9	7,2	3,0	12,8	10,8	3,5	9,0
1970	3,1	2,5	6,2	10,4	5,6	4,4	6,4	0,5	8,7	0,6	4,9
1961-70	5,0	6,2	5,7	:	5,2	6,6	6,7	2,4	6,2	2,8	5,1
1971	1,7	2,4	1,5	11,3	6,4	3,7	−0,5	−1,3	6,0	0,1	2,3
1972	7,5	4,4	4,1	14,2	5,5	4,2	4,9	4,2	4,7	2,2	4,3
1973	6,2	3,4	7,1	15,3	6,7	9,9	9,7	12,0	7,2	8,2	7,4
1974	4,0	−1,1	−1,1	−1,4	2,5	2,9	3,9	3,5	5,0	−2,6	0,6
1975	−9,8	−5,7	−6,2	4,3	−7,2	−6,1	−8,8	−21,9	−4,8	−4,8	−6,6
1976	8,1	9,3	7,4	10,5	8,6	8,7	11,6	3,8	7,7	2,8	7,4
1977	0,4	0,8	2,8	1,5	1,9	8,0	0,0	0,5	0,5	4,7	2,4
1978	2,4	2,3	2,0	7,5	2,3	7,7	2,1	3,2	0,8	3,7	2,5
1979	4,3	3,6	5,5	6,0	4,0	6,9	6,7	3,4	3,1	3,8	4,9
1980	−1,0	0,2	−0,8	0,9	−0,5	−1,8	5,0	−3,3	−0,1	−6,5	−0,9
1971-80	2,3	1,9	2,2	6,9	2,9	4,3	3,3	0,0	2,9	1,0	2,4
1981	−2,9	0,3	−1,4	−0,6	−2,3	1,4	−2,2	−6,8	−1,7	−4,0	−2,2
1982	−0,2	2,4	−2,8	−4,2	−1,0	0,4	−2,6	−3,7	−3,4	0,7	−1,6
(1983)	1,8	3,0	0,5	0,1	−0,8	3,0	−3,2	−5,1	2,0	2,1	2,0

Table 10

Private consumption at current prices

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	68,5	64,4	62,4	74,8	63,2	84,4	67,8	58,7	60,6	66,7	64,8
1959	69,5	62,7	61,2	77,0	62,5	80,2	66,6	59,5	60,0	66,8	64,1
1960	68,7	62,7	59,8	81,2	61,4	80,4	64,4	55,2	59,2	66,0	63,2
1961	67,4	62,7	59,7	77,9	61,6	78,9	63,4	55,5	60,4	65,0	62,8
1962	66,3	62,4	59,5	77,7	61,8	78,2	63,6	58,4	61,1	65,8	63,0
1963	66,7	62,1	59,7	75,7	62,4	77,5	64,7	58,3	62,7	65,8	63,4
1964	63,7	61,0	58,6	74,6	61,4	76,2	64,1	57,5	60,0	64,3	62,1
1965	63,8	59,5	59,2	73,9	61,0	75,8	64,0	58,6	59,9	63,7	62,0
1966	63,4	60,1	59,7	73,8	61,0	75,0	65,2	58,8	59,5	63,4	62,2
1967	62,4	60,3	60,9	73,6	61,1	73,5	65,3	58,3	58,6	63,1	62,4
1968	63,3	59,2	60,2	72,8	61,2	74,1	64,2	56,9	57,6	62,9	62,0
1969	61,8	58,0	59,2	70,3	61,2	72,5	63,7	52,9	57,7	62,5	61,4
1970	59,4	58,1	58,2	70,3	60,2	71,0	63,9	51,3	57,7	62,1	60,7
1961-70	63,8	60,3	59,5	74,1	61,3	75,3	64,2	56,6	59,5	63,9	62,2
1971	59,7	56,6	58,4	69,3	60,6	70,0	63,7	54,9	57,2	62,0	60,7
1972	59,6	54,3	58,9	67,7	60,5	66,0	63,9	54,0	56,9	63,2	61,0
1973	59,9	55,2	58,2	65,6	60,1	65,3	63,5	48,8	56,3	62,5	60,5
1974	59,2	55,2	54,0	69,1	61,2	69,4	63,9	46,2	56,1	63,5	61,3
1975	60,5	56,2	62,4	69,5	61,9	64,7	65,5	57,5	58,2	61,9	62,4
1976	60,4	57,1	62,0	68,4	62,1	64,2	64,1	56,5	58,0	60,5	61,8
1977	61,2	57,3	62,2	68,7	62,2	63,8	63,8	59,8	58,8	60,5	61,9
1978	60,7	56,5	61,6	68,4	62,3	63,1	63,5	57,9	59,0	60,3	61,7
1979	61,8	56,5	61,0	66,8	62,5	63,5	63,2	57,7	59,5	60,9	61,7
1980	62,5	56,4	61,5	68,3	63,6	63,6	63,2	58,5	59,6	60,2	62,0
1971-80	60,5	56,1	60,5	68,2	61,7	65,4	63,8	55,2	58,0	61,6	61,5
1981	64,9	56,5	62,1	71,9	65,2	63,6	64,2	60,5	59,4	60,8	62,9
1982	65,2	56,0	61,6	69,9	65,1	59,6	64,2	61,3	59,4	60,7	62,8
(1983)	64,1	54,9	61,5	70,6	65,0	57,4	64,1	62,0	59,0	61,3	62,7

Table 11

Private consumption at 1975 prices

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	−0,3	4,6	5,0	4,2	1,3	2,8	4,0	:	0,3	2,6	2,8
1959	1,9	5,5	5,7	2,4	2,5	1,0	5,0	:	4,4	4,3	4,2
1960	5,3	4,7	8,0	5,0	4,9	5,4	6,1	:	6,1	3,9	5,5
1961	1,7	7,1	5,5	7,2	5,9	3,1	7,5	4,9	5,4	2,2	4,9
1962	4,1	5,6	5,1	4,5	7,3	3,4	7,1	4,6	6,1	2,0	5,0
1963	4,3	0,2	3,1	5,4	7,1	4,3	8,9	4,5	7,1	4,2	5,4
1964	2,7	8,0	5,4	8,2	5,5	4,2	3,3	8,5	5,4	2,9	4,4
1965	4,2	3,4	6,8	7,8	4,2	0,8	3,7	3,9	7,2	1,5	4,2
1966	2,7	10,8	3,7	7,4	4,9	1,5	7,3	1,5	2,5	2,0	4,2
1967	2,8	3,3	1,7	5,8	5,0	3,8	7,0	−0,5	4,8	2,5	3,8
1968	5,5	1,5	4,9	6,6	3,6	8,9	5,0	4,3	6,1	3,4	4,4
1969	5,3	6,3	7,3	6,5	6,5	5,4	6,5	5,0	7,0	0,7	5,3
1970	3,3	3,4	6,8	8,7	4,7	2,0	7,4	5,9	7,9	2,8	5,4
1961-70	3,6	4,9	5,0	6,8	5,5	3,7	6,4	4,2	5,9	2,4	4,7
1971	4,7	−0,3	5,1	6,6	6,3	3,1	3,0	5,8	3,4	3,2	4,3
1972	5,8	1,8	4,9	7,2	6,1	3,9	3,4	4,3	3,5	5,9	5,0
1973	7,7	5,2	2,3	7,9	5,6	7,0	5,7	5,4	3,9	5,0	4,7
1974	3,0	−2,3	1,3	−0,7	3,2	1,7	2,7	5,0	2,4	−1,6	1,4
1975	0,4	3,3	4,2	6,1	3,2	−4,9	−1,3	5,1	3,1	−0,5	1,7
1976	5,0	8,4	4,0	6,2	5,4	2,4	3,6	3,0	5,2	0,7	3,8
1977	2,4	1,0	3,3	4,9	3,0	5,8	2,2	2,4	4,1	0,1	2,4
1978	2,3	0,7	3,7	6,5	4,6	7,6	3,0	3,0	3,9	5,1	4,1
1979	4,5	1,1	2,9	2,2	3,3	2,0	5,3	3,6	3,2	4,4	3,7
1980	1,4	−3,5	1,7	0,2	1,6	−0,4	4,3	3,2	−0,3	−0,8	1,4
1971-80	3,7	1,5	3,3	4,7	4,2	2,7	3,2	4,1	3,2	2,1	3,2
1981	−1,4	−0,5	−0,4	0,7	1,9	−0,4	0,2	1,7	−2,1	−0,1	0,2
1982	1,1	2,6	−2,2	0,6	3,5	−5,3	0,3	−1,6	−1,6	1,1	0,5
(1983)	−3,1	0,9	0,5	0,1	0,3	−3,5	−0,8	−1,5	−1,5	3,0	0,4

Table 12

Public consumption at current prices

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	11,9	14,0	10,5	11,0	13,1	12,6	12,1	11,7	14,3	16,3	13,1
1959	12,4	13,7	10,6	11,2	13,6	12,4	12,2	10,6	13,4	16,5	13,3
1960	12,4	13,4	10,6	11,7	13,0	12,5	12,8	9,8	12,8	16,6	13,2
1961	11,9	14,6	11,0	11,3	13,1	12,5	12,7	9,5	13,4	16,7	13,4
1962	12,3	15,3	11,8	11,6	13,3	12,6	13,1	10,9	13,9	17,1	13,8
1963	13,0	15,6	12,5	11,3	13,4	12,8	13,9	12,2	14,7	17,0	14,2
1964	12,5	15,7	11,8	11,6	13,3	13,4	14,3	10,8	14,8	16,5	13,9
1965	12,8	16,4	12,0	11,7	13,1	13,7	15,1	10,9	14,8	16,9	14,2
1966	13,1	17,1	12,0	11,8	13,0	13,6	14,9	11,4	15,2	17,2	14,2
1967	13,5	17,8	12,5	13,0	13,0	13,4	14,4	11,9	15,5	18,0	14,5
1968	13,6	18,6	11,7	12,9	13,5	13,4	14,5	11,8	15,2	17,7	14,4
1969	13,6	18,9	11,8	12,7	13,3	13,6	14,2	10,9	15,3	17,2	14,2
1970	13,4	20,0	11,9	12,6	13,4	14,6	13,8	10,7	15,6	17,7	14,3
1961-70	13,0	17,0	11,9	12,1	13,3	13,4	14,1	11,1	14,8	17,2	14,1
1971	14,1	21,3	12,6	12,4	13,4	15,2	15,5	11,7	16,0	18,0	14,9
1972	14,5	21,3	12,5	12,2	13,2	15,3	16,1	11,9	15,9	18,5	15,0
1973	14,5	21,3	12,8	11,5	13,2	15,7	15,5	11,3	15,6	18,4	14,9
1974	14,7	23,4	13,7	13,8	13,6	17,2	15,1	11,5	16,3	20,1	15,7
1975	16,4	24,6	14,2	15,2	14,4	19,0	15,4	14,9	17,4	22,0	16,6
1976	16,4	24,1	13,5	15,1	14,6	18,4	14,8	14,8	17,2	21,5	16,2
1977	16,9	23,9	13,4	16,0	14,7	18,0	15,3	16,0	17,4	20,4	16,1
1978	17,5	24,5	13,4	15,9	15,0	18,2	15,9	15,6	17,7	20,0	16,2
1979	17,7	25,0	13,4	16,3	14,9	19,5	16,2	15,8	18,1	19,9	16,3
1980	18,1	26,8	13,7	16,1	15,2	21,5	16,4	16,7	18,0	21,5	16,8
1971-80	16,1	23,6	13,3	14,5	14,2	17,8	15,6	14,0	17,0	20,0	15,9
1981	19,0	27,7	14,0	17,8	15,8	22,0	18,1	17,5	17,9	22,3	17,6
1982	18,5	28,0	13,8	18,0	16,1	22,0	18,3	17,5	17,9	22,2	17,6
(1983)	18,0	27,5	13,7	18,5	16,0	21,7	18,7	17,8	18,0	22,3	17,7

Table 13

Public consumption at 1975 prices

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	7,6	0,6	8,2	−0,9	−4,3	−0,7	5,5	:	−2,9	−2,2	0,7
1959	5,3	6,6	9,0	1,7	5,8	2,0	4,4	:	−1,3	2,1	4,9
1960	5,3	3,9	6,0	4,6	3,0	1,7	4,0	:	5,4	2,2	3,8
1961	1,9	5,3	6,8	4,4	4,7	2,1	4,4	1,2	3,6	3,5	4,6
1962	8,6	9,9	10,5	6,7	4,7	3,1	3,9	2,4	4,2	3,1	5,6
1963	11,6	2,9	6,2	4,2	3,4	4,0	4,3	5,8	6,7	1,6	4,1
1964	4,2	7,3	0,6	9,3	4,1	3,0	4,2	−0,8	1,7	1,6	2,5
1965	5,5	3,4	4,0	9,0	3,2	3,7	4,0	2,5	1,5	2,7	3,4
1966	4,7	5,5	1,0	6,3	2,7	1,0	4,0	5,8	1,7	2,7	2,6
1967	5,7	7,6	2,9	8,5	4,2	4,5	4,4	4,2	2,4	5,7	4,4
1968	3,5	4,7	−1,5	1,3	5,6	5,8	5,2	5,6	2,2	0,4	2,1
1969	6,3	6,8	4,6	7,7	4,1	6,9	2,8	3,3	4,5	−1,9	2,5
1970	2,2	6,9	4,4	5,9	4,1	11,3	2,6	4,1	6,0	1,5	3,4
1961-70	5,4	6,0	3,9	6,3	4,1	4,5	4,0	3,4	3,4	2,1	3,5
1971	5,5	5,5	3,9	4,9	3,5	8,6	5,7	3,8	3,3	3,0	4,0
1972	5,9	5,7	2,2	5,7	2,7	7,5	5,3	4,0	1,8	4,1	3,6
1973	5,2	4,0	3,6	6,8	3,2	6,7	2,4	3,3	0,7	4,7	3,6
1974	3,4	3,5	2,5	12,1	1,2	7,6	2,8	4,8	2,0	1,5	2,2
1975	4,8	2,0	1,1	11,9	4,7	7,0	3,2	6,6	3,9	5,4	3,9
1976	3,7	3,9	−0,0	5,1	5,7	2,4	2,2	1,9	4,0	1,0	2,3
1977	2,9	2,9	1,1	6,5	1,4	3,6	2,8	3,0	3,2	−1,0	1,3
1978	6,4	6,2	3,8	3,5	4,4	6,8	2,3	2,0	3,9	2,2	3,4
1979	2,4	5,9	3,8	5,8	1,8	6,9	1,6	4,7	2,7	1,8	2,6
1980	1,5	4,5	2,4	−0,8	1,3	6,3	2,1	4,6	0,9	1,9	1,9
1971-80	4,2	4,4	2,4	6,1	3,0	6,3	3,0	3,8	2,6	2,5	2,9
1981	0,6	3,0	1,7	6,5	2,4	−0,1	1,7	2,1	1,3	0,4	1,5
1982	−1,6	3,3	−1,1	1,0	1,7	3,3	1,8	0,3	0,7	1,2	0,8
(1983)	−1,6	1,1	−0,1	3,0	−1,1	0,0	1,8	−0,3	1,7	2,4	0,8

Table 14

Gross fixed investment at current prices; total economy

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	17,0	17,3	22,4	19,1	20,3	14,2	20,8	22,9	23,0	15,7	19,6
1959	17,8	18,8	23,6	21,8	20,1	13,9	21,1	22,3	23,8	15,9	20,0
1960	19,3	21,2	24,3	19,0	20,1	14,4	22,6	21,0	24,1	16,4	20,8
1961	20,7	22,8	25,2	18,2	21,2	16,3	23,2	23,2	24,8	17,3	21,7
1962	21,3	22,7	25,7	20,1	21,4	17,9	23,7	26,1	24,5	16,9	22,0
1963	20,7	21,6	25,6	19,2	22,1	19,5	24,0	29,9	23,8	16,7	22,0
1964	22,4	24,1	26,6	21,0	22,9	20,5	22,2	33,5	25,5	18,3	22,8
1965	22,4	23,7	26,1	21,6	23,3	21,4	19,3	28,0	25,1	18,3	22,2
1966	22,9	24,1	25,4	21,7	23,7	19,8	18,8	26,6	26,2	18,3	22,1
1967	22,9	24,2	23,1	20,3	23,8	20,1	19,5	23,3	26,3	18,8	21,7
1968	21,5	23,4	22,4	23,2	23,3	20,9	20,3	21,4	26,9	18,9	21,6
1969	21,3	24,6	23,3	24,6	23,4	23,3	21,0	21,7	24,6	18,5	21,9
1970	22,7	24,7	25,5	23,6	23,4	22,7	21,4	23,5	25,8	18,6	22,7
1961-70	21,9	23,6	24,9	21,4	22,9	20,2	21,3	25,7	25,3	18,1	22,1
1971	22,1	24,2	26,1	25,7	23,6	23,6	20,4	28,4	25,9	18,4	22,7
1972	21,3	24,6	25,4	27,7	23,7	23,7	19,8	28,2	23,7	18,3	22,3
1973	21,4	24,8	23,9	28,0	23,8	25,3	20,8	27,4	23,1	19,5	22,4
1974	22,7	24,0	21,6	22,2	24,3	24,6	22,4	24,7	21,8	20,3	22,2
1975	22,5	21,1	20,4	20,8	23,3	22,6	20,6	27,8	20,9	19,5	21,0
1976	22,1	23,0	20,2	21,2	23,3	24,8	20,0	24,5	19,3	19,0	20,7
1977	21,7	22,1	20,3	23,0	22,3	25,0	19,6	25,3	21,1	17,9	20,4
1978	21,6	21,7	20,8	23,9	21,4	27,9	18,7	23,9	21,3	18,0	20,2
1979	20,6	20,9	21,9	25,6	21,4	31,0	18,8	24,6	21,0	17,9	20,5
1980	21,2	18,3	22,8	23,4	21,6	28,9	19,8	26,2	20,8	17,5	20,8
1971-80	21,7	22,5	22,3	24,2	22,9	25,7	20,1	26,1	21,9	18,6	21,3
1981	17,9	15,7	22,0	20,9	21,2	29,8	20,3	23,3	19,0	15,9	19,9
1982	17,1	16,0	20,6	19,0	21,1	25,6	19,1	23,4	18,0	15,7	19,1
(1983)	16,7	16,0	20,8	19,4	20,3	22,5	18,2	22,5	18,0	16,0	18,8

Table 15

Gross fixed investment at 1975 prices; total economy

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	−7,2	6,6	4,2	33,4	5,8	−2,5	2,7	:	−12,2	0,8	2,1
1959	9,8	20,4	11,8	15,3	3,1	4,8	8,7	:	11,6	7,4	8,4
1960	13,8	9,5	10,1	29,5	7,8	6,8	12,3	:	11,5	9,2	9,8
1961	12,4	13,9	6,8	8,1	10,9	16,9	11,6	9,1	6,5	9,8	9,5
1962	5,9	6,7	4,1	8,4	8,5	14,7	9,8	7,8	4,4	0,2	5,5
1963	0,1	−2,4	1,3	5,5	8,8	12,0	8,1	14,2	1,9	1,3	4,1
1964	14,7	23,5	11,2	20,7	10,5	10,9	−5,8	21,0	18,9	16,8	9,3
1965	4,1	4,7	4,8	12,8	7,0	10,5	−8,4	−13,1	5,2	4,8	2,8
1966	6,8	7,0	1,2	3,2	7,3	−3,0	4,3	−5,1	8,0	2,5	3,9
1967	2,9	5,5	−6,9	−1,6	6,0	6,8	11,7	−9,0	8,5	8,5	3,6
1968	−1,3	1,8	3,6	21,4	5,5	13,2	10,8	−4,1	11,2	4,6	6,1
1969	5,3	12,1	10,5	18,6	9,2	20,4	7,8	10,2	−2,2	0,4	6,9
1970	8,4	2,4	9,9	−1,4	4,6	−3,3	3,0	9,2	9,5	2,7	5,5
1961-70	5,8	7,3	4,5	9,3	7,8	9,7	5,1	3,5	7,0	5,0	5,7
1971	−1,5	1,7	6,2	14,0	7,1	8,9	−3,2	15,1	3,4	1,5	3,3
1972	3,3	8,6	2,6	15,4	7,2	7,8	0,9	6,0	−2,8	0,4	3,0
1973	6,8	4,3	−0,2	7,7	6,1	16,2	7,7	11,4	4,5	6,9	4,8
1974	7,0	−9,0	−9,5	−25,6	0,9	−11,6	3,3	−5,2	−3,8	−3,0	−3,1
1975	−1,6	−12,2	−4,9	0,2	−3,2	−4,3	−12,7	−7,1	−4,9	−0,7	−5,2
1976	3,2	17,1	4,6	6,8	3,5	12,9	2,3	−5,2	−2,8	1,1	3,2
1977	−0,2	−2,0	3,8	7,8	−1,5	3,7	−0,4	1,8	11,7	−2,4	0,8
1978	2,4	1,4	4,9	6,0	0,4	17,2	−0,1	0,3	2,7	3,5	2,5
1979	−2,6	−0,2	7,2	7,9	2,7	13,0	5,8	7,0	−1,6	0,9	3,8
1980	5,3	−14,8	3,2	−8,7	1,2	−7,7	9,4	5,9	−2,5	−2,8	1,7
1971-80	2,1	−0,9	1,6	2,4	2,4	5,1	1,1	2,8	0,3	0,5	1,4
1981	−16,2	−15,7	−3,9	−10,1	−2,3	7,5	−0,2	−13,3	−10,8	−8,2	−4,7
1982	−2,6	3,6	−5,4	−1,0	1,1	−8,4	−5,3	−2,2	−5,0	4,8	−1,9
(1983)	−1,9	1,7	3,3	−2,2	−3,8	−10,4	−5,1	−5,8	0,7	5,1	−0,2

Table 16

Net stockbuilding at current prices

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	0,8	−0,5	1,5	2,0	3,2	−1,4	0,8	1,8	0,3	0,5	1,6
1959	0,2	2,3	1,5	1,3	2,2	4,0	1,0	2,0	0,7	0,7	1,4
1960	−0,1	4,3	3,0	−3,4	3,0	2,0	2,1	1,0	2,9	2,2	2,5
1961	0,5	1,8	2,0	0,8	1,7	1,4	2,3	5,3	2,2	1,0	1,7
1962	−0,0	2,8	1,6	−0,9	2,3	1,6	1,7	4,0	1,1	−0,0	1,3
1963	0,4	0,5	0,7	3,2	1,5	0,9	1,0	−0,2	0,6	0,6	0,9
1964	1,5	1,6	1,5	3,6	2,4	1,2	0,5	−1,9	2,5	2,2	1,7
1965	0,8	2,1	2,3	5,2	1,6	2,3	0,7	1,1	1,5	1,4	1,6
1966	1,0	0,8	1,1	1,7	2,0	0,8	0,8	0,6	0,8	0,8	1,2
1967	0,4	0,0	−0,1	1,6	1,8	−0,4	1,1	−1,6	0,5	0,8	0,8
1968	0,9	0,6	2,1	0,9	1,8	1,1	0,0	−0,2	0,3	1,1	1,2
1969	1,9	1,3	2,9	2,5	2,6	2,4	0,7	−0,1	2,1	1,2	2,0
1970	1,6	1,0	2,1	3,2	2,7	1,7	1,7	2,1	2,2	0,8	1,9
1961-70	0,9	1,2	1,6	2,2	2,0	1,3	1,1	0,9	1,4	1,0	1,4
1971	1,4	0,6	0,6	2,7	1,5	0,3	0,6	2,6	1,1	0,3	0,8
1972	0,5	0,2	0,6	3,1	1,9	1,4	0,6	1,3	0,6	0,1	0,8
1973	1,3	1,3	1,4	8,4	2,4	1,6	3,4	0,9	1,7	2,0	2,2
1974	2,2	1,2	0,5	6,7	2,4	4,4	4,2	−2,1	2,8	1,5	2,1
1975	−0,6	−0,2	−0,6	7,3	−0,3	−0,4	−0,3	−3,3	−0,2	−1,4	−0,5
1976	0,1	1,0	1,1	7,2	1,2	0,1	3,6	−0,0	1,3	0,7	1,6
1977	0,3	0,8	0,7	4,6	1,1	2,1	1,8	−3,1	0,6	1,3	1,2
1978	0,1	−0,2	0,6	3,1	0,6	0,2	1,3	3,2	0,6	1,0	0,8
1979	0,6	0,5	1,9	3,5	1,4	2,2	2,4	−0,1	0,5	1,5	1,7
1980	0,1	−0,4	1,2	2,5	1,6	−0,7	5,3	1,6	0,7	−1,2	1,5
1971-80	0,6	0,5	0,8	4,9	1,4	1,1	2,3	0,1	1,0	0,6	1,2
1981	0,2	−0,3	−0,0	1,5	−0,1	−1,1	1,1	2,4	−1,1	−1,7	−0,3
1982	0,3	2,1	0,5	7,5	0,7	0,0	1,4	2,3	−0,2	−0,7	0,5
(1983)	0,2	−0,2	0,7	6,0	0,3	−0,1	0,9	2,7	−0,2	0,2	0,5

Table 17

Price deflator of GDP at market prices

(national currency, annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	1,5	1,8	3,4	1,6	11,8	5,8	2,5	:	1,8	4,0	4,8
1959	0,8	3,6	0,8	0,2	5,7	2,7	−0,7	−1,8	1,2	1,1	1,7
1960	0,7	1,8	3,4	3,5	3,5	0,3	0,0	4,1	3,4	1,5	2,7
1961	1,3	4,3	4,2	1,5	3,4	2,5	2,8	0,4	2,6	3,4	3,3
1962	1,7	6,6	4,1	4,6	4,7	4,9	5,8	−1,0	3,2	3,7	4,5
1963	3,0	5,8	2,7	1,4	6,4	2,7	8,5	5,0	5,0	2,3	4,5
1964	4,7	4,6	3,0	3,7	4,1	9,7	6,5	5,4	8,4	3,6	4,6
1965	5,1	7,4	3,6	4,0	2,7	4,4	4,2	3,4	6,1	5,0	4,4
1966	4,2	3,6	3,5	4,8	2,9	4,4	2,2	3,0	6,0	4,5	3,6
1967	3,1	6,0	1,2	2,5	3,2	3,3	2,8	1,0	4,2	2,9	2,6
1968	2,7	7,2	2,0	1,7	4,2	4,2	1,7	5,1	4,2	4,0	3,2
1969	4,8	6,8	4,2	3,4	6,6	9,1	4,1	5,5	6,4	5,5	5,4
1970	4,8	8,1	7,5	3,9	5,6	9,7	6,9	11,1	5,6	7,3	6,8
1961-70	3,5	6,0	3,6	3,1	4,4	5,5	4,5	3,8	5,2	4,2	4,3
1971	5,4	7,9	7,6	3,8	5,8	10,5	7,2	−0,7	8,5	9,3	7,5
1972	6,2	9,0	5,4	4,5	6,2	13,4	6,3	5,0	9,4	8,3	6,8
1973	7,0	10,5	6,6	19,4	7,8	15,3	11,6	10,5	8,4	7,1	8,3
1974	12,2	12,8	6,6	21,0	11,1	6,1	18,5	17,8	9,3	15,1	12,5
1975	12,6	12,8	5,9	12,3	13,4	22,3	17,5	−1,1	11,2	26,9	14,8
1976	7,2	8,7	3,5	15,4	10,1	20,3	18,0	12,7	8,9	14,8	10,5
1977	7,2	9,0	3,6	13,0	8,9	12,5	19,1	1,7	6,3	14,0	9,7
1978	4,2	9,5	4,2	12,9	9,9	10,7	13,9	5,3	5,2	10,9	8,5
1979	4,1	7,4	4,1	18,7	10,4	12,9	15,9	5,8	4,2	15,1	9,4
1980	4,2	8,8	4,4	17,9	11,6	13,9	20,7	7,8	5,3	19,2	10,8
1971-80	7,0	9,6	5,2	13,7	9,5	13,7	14,8	6,3	7,7	13,9	9,9
1981	5,2	10,8	4,0	19,7	11,9	17,7	17,6	7,9	5,6	12,1	9,1
1982	7,0	9,9	4,8	25,4	12,8	16,8	17,5	7,9	5,7	7,8	9,1
(1983)	7,1	7,4	3,1	19,7	9,8	10,6	15,1	8,2	1,6	5,0	6,3

Table 18

Price deflator of private consumption

(national currency, annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	0,1	0,5	2,5	0,0	12,1	3,8	2,3	:	1,6	2,7	4,3
1959	−0,3	2,5	1,0	−0,5	5,8	0,4	−0,7	:	1,2	1,0	1,8
1960	2,4	2,9	1,0	3,1	3,6	0,9	1,4	:	2,5	1,1	1,7
1961	2,7	3,6	3,6	1,1	3,4	2,4	1,8	0,5	2,1	3,0	2,9
1962	1,0	6,2	3,2	1,3	4,4	3,6	5,3	0,9	2,7	3,9	4,0
1963	3,7	5,7	3,1	3,2	5,8	2,2	7,1	2,9	3,9	1,9	4,1
1964	4,1	4,0	2,3	2,2	3,4	7,3	5,0	3,1	6,9	3,6	3,8
1965	4,6	6,1	3,4	4,6	2,6	5,0	3,6	3,2	4,1	4,9	4,0
1966	4,1	0,4	3,5	3,5	3,2	2,8	2,9	3,5	5,5	4,0	3,5
1967	2,5	6,8	1,6	1,9	3,1	3,1	3,1	2,3	3,1	2,6	2,5
1968	2,9	7,7	1,7	0,8	5,1	4,4	1,4	2,5	2,7	4,5	3,3
1969	2,9	4,7	2,5	3,0	7,1	7,2	2,9	1,8	6,2	5,6	4,7
1970	3,6	7,1	4,1	3,2	5,0	8,2	5,0	4,0	4,3	6,0	5,1
1961-70	3,2	5,2	2,9	2,5	4,3	4,6	3,8	2,5	4,1	4,0	3,8
1971	5,2	8,0	6,1	2,9	5,5	9,4	5,5	4,7	8,5	8,6	6,6
1972	5,4	8,2	5,6	3,5	5,9	9,6	6,4	5,2	8,9	6,6	6,4
1973	6,0	10,9	7,5	15,0	6,8	11,6	12,4	5,0	9,1	8,6	8,7
1974	12,4	14,7	7,3	23,6	13,2	15,7	20,8	9,9	10,0	17,4	14,2
1975	12,5	10,1	5,9	13,0	11,4	22,3	17,6	10,2	10,7	23,5	13,7
1976	7,6	9,0	4,3	13,6	9,9	18,8	18,1	9,5	8,8	15,5	10,8
1977	7,0	10,4	3,7	12,0	9,2	12,9	18,2	5,8	5,9	15,2	9,9
1978	4,1	9,2	2,7	12,6	8,9	7,7	12,9	3,5	4,3	9,0	7,2
1979	3,8	10,2	4,2	17,5	10,6	14,2	15,0	5,8	4,0	13,2	8,9
1980	7,0	11,2	5,4	22,2	13,3	17,6	20,3	7,7	6,7	16,4	11,2
1971-80	7,1	10,2	5,3	13,4	9,4	13,9	14,6	6,7	7,7	13,3	9,7
1981	8,9	11,8	5,6	24,4	12,9	19,5	19,0	7,7	6,2	11,0	10,1
1982	7,4	9,8	5,3	21,1	10,9	17,1	16,7	10,0	5,7	8,1	8,7
(1983)	7,8	6,6	3,0	20,5	9,0	11,0	15,0	8,4	2,8	5,8	6,3

Table 19

Price deflator of exports of goods and services

(national currency, annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	−4,5	−4,6	−1,4	−5,1	7,1	3,0	−9,2	:	−5,2	−1,1	−2,0
1959	−6,3	2,7	0,1	−5,3	9,1	2,7	−6,2	:	−0,5	0,4	0,4
1960	2,4	−0,9	1,9	−2,0	1,8	−1,0	2,6	:	−0,4	0,4	1,3
1961	0,9	−1,6	−0,1	0,4	0,1	1,5	−1,9	−3,1	−1,8	1,2	−0,1
1962	1,0	2,1	0,2	1,5	1,0	1,0	0,3	−1,7	−0,9	0,8	1,0
1963	2,1	2,6	0,7	10,2	2,5	2,7	2,7	−0,0	2,4	1,1	2,1
1964	4,0	3,4	2,6	0,2	4,4	3,7	3,2	2,3	2,2	2,2	3,0
1965	1,3	1,7	2,5	−1,7	1,0	1,0	−0,8	1,4	2,2	2,2	1,5
1966	3,6	2,4	2,3	4,5	1,9	5,7	−0,0	0,7	0,3	2,9	1,8
1967	0,3	1,3	0,1	−3,2	−0,8	1,6	1,3	0,3	−0,3	2,3	0,5
1968	0,1	2,2	−0,4	−1,7	−0,9	7,3	0,1	1,2	−0,8	8,5	1,8
1969	4,7	7,5	4,4	0,6	4,6	7,5	2,7	6,7	2,0	2,4	3,8
1970	5,7	7,0	4,4	2,8	8,0	8,2	6,1	12,8	5,1	8,8	6,7
1961-70	2,3	2,8	1,7	1,3	2,1	4,0	1,3	2,0	1,0	3,2	2,2
1971	1,9	3,9	4,1	1,0	4,8	7,2	4,1	−2,9	2,9	4,6	4,0
1972	1,6	6,8	1,8	4,6	0,3	12,3	2,3	1,2	1,0	4,2	2,2
1973	8,3	12,5	6,4	28,4	7,5	20,5	15,5	15,5	6,9	12,6	10,1
1974	24,8	19,8	15,7	31,9	23,2	23,6	36,6	23,8	26,5	25,9	24,9
1975	4,8	7,5	4,2	12,7	4,4	18,6	11,0	−1,5	4,9	20,2	9,1
1976	6,1	6,2	3,4	9,1	8,8	23,3	20,5	7,7	6,5	20,0	11,2
1977	3,0	6,0	1,7	9,4	9,0	14,9	19,2	−1,2	3,5	15,5	8,9
1978	0,6	5,0	1,6	6,4	6,2	6,5	7,7	2,0	−1,5	7,0	4,3
1979	9,1	8,4	4,5	12,6	10,3	9,1	15,8	8,7	8,5	12,4	9,6
1980	9,2	15,7	6,5	37,5	11,6	10,2	18,0	5,7	12,5	13,8	11,3
1971-80	6,8	9,1	4,9	14,8	8,5	14,5	14,7	5,6	6,9	13,4	9,4
1981	9,4	14,5	6,0	6,0	13,5	16,8	20,4	1,3	14,7	9,4	11,0
1982	13,3	9,8	4,2	23,1	15,7	11,6	14,5	12,9	4,2	7,2	9,2
(1983)	5,2	4,4	1,7	26,1	12,4	8,1	9,9	4,4	0,8	6,9	5,6

Table 20

Price deflator of imports of goods and services

(national currency, annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	3,1	2,2	1,2	−8,4	8,4	5,3	5,3	:	4,7	2,3	3,9
1959	−6,7	−6,9	−7,3	−1,5	6,9	−3,7	−12,2	:	−5,5	−5,0	−4,7
1960	−1,6	−4,2	−2,0	−0,7	7,6	−2,1	−6,0	:	−3,0	0,0	−0,3
1961	2,6	0,1	−2,9	−1,8	0,1	1,4	−2,4	1,1	−2,0	−0,1	−0,6
1962	0,6	−0,5	−0,6	−0,8	2,9	−0,2	0,2	0,7	−1,4	−0,4	0,6
1963	4,1	1,9	2,3	2,6	1,0	1,7	1,7	1,0	1,4	2,6	2,3
1964	2,9	0,9	1,7	3,1	0,7	1,2	3,5	1,0	2,5	2,5	2,6
1965	0,0	1,2	2,7	0,4	1,5	2,9	0,5	1,5	0,6	1,4	1,7
1966	3,0	0,6	1,7	3,3	3,2	−0,3	1,7	1,3	0,7	1,4	1,5
1967	0,2	1,5	−1,9	−3,0	−1,4	0,3	0,7	−0,9	−0,9	1,0	−1,0
1968	0,5	4,8	0,2	0,3	−1,1	8,1	0,5	−0,0	−2,9	11,2	2,8
1969	3,3	3,4	2,5	0,0	4,9	5,1	1,2	3,0	3,3	2,8	3,2
1970	5,0	6,4	−0,2	4,1	9,8	5,8	3,5	11,0	6,5	7,1	5,2
1961-70	2,2	2,0	0,5	0,8	2,1	2,6	1,1	1,9	0,7	2,9	1,8
1971	3,4	5,6	1,5	3,0	3,7	5,3	5,2	4,9	4,4	3,7	3,7
1972	0,3	2,3	1,1	7,9	−1,8	5,6	3,7	0,2	−0,8	2,4	1,0
1973	7,6	15,1	9,5	21,6	6,8	14,1	26,2	9,7	7,5	23,7	14,6
1974	28,3	33,6	25,0	42,3	42,5	45,8	57,1	21,7	33,8	43,2	39,2
1975	5,8	4,2	0,8	17,9	−0,3	20,5	6,0	10,5	4,1	13,6	5,3
1976	7,1	7,2	6,1	11,1	10,5	19,0	24,0	5,6	6,3	21,7	13,1
1977	2,7	7,4	1,8	5,6	11,5	17,0	16,9	2,3	3,0	14,3	8,6
1978	0,8	2,0	−2,8	9,9	2,0	4,6	4,5	0,7	−2,1	2,8	1,1
1979	9,1	13,3	8,8	18,2	11,2	13,5	17,5	6,6	10,9	8,0	10,6
1980	13,8	23,5	13,0	35,0	19,9	18,2	22,0	9,0	14,6	10,3	15,3
1971-80	7,6	11,0	6,2	16,6	10,0	15,9	17,4	7,0	7,8	13,8	10,8
1981	13,9	17,2	10,0	13,0	18,8	18,6	27,8	4,0	15,9	5,1	14,0
1982	13,3	10,6	2,2	25,4	10,7	8,8	10,7	15,1	1,9	5,3	6,5
(1983)	4,9	3,4	0,3	23,1	9,0	6,3	8,4	4,7	1,8	10,0	4,7

Table 21

Terms of trade; goods and services

(1975 = 100)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	97,8	87,3	81,8	112,4	110,0	85,0	103,1	:	94,4	106,7	99,1
1959	98,2	96,3	88,3	108,1	112,3	90,6	110,1	:	99,4	112,8	104,4
1960	101,9	99,6	93,3	106,7	106,2	91,6	120,2	111,7	102,1	111,8	106,2
1961	100,1	97,9	96,0	109,2	106,1	91,7	120,8	107,0	102,3	113,2	106,7
1962	100,5	100,4	96,8	111,7	104,1	92,7	120,9	104,4	102,9	114,5	107,2
1963	98,6	101,1	95,3	120,0	105,6	93,7	122,1	103,4	104,0	112,9	106,9
1964	99,6	103,6	96,1	116,6	109,5	95,9	121,8	104,7	103,6	112,5	107,4
1965	100,9	104,0	95,8	114,2	109,0	94,1	120,1	104,5	105,3	113,4	107,2
1966	101,5	106,0	96,5	115,4	107,6	99,8	118,0	103,9	104,9	115,1	107,6
1967	101,5	105,8	98,5	115,2	108,2	101,0	118,7	105,1	105,5	116,5	109,2
1968	101,2	103,2	97,9	112,9	108,4	100,3	118,3	106,4	107,9	113,7	108,1
1969	102,6	107,3	99,6	113,6	108,1	102,6	119,9	110,3	106,4	113,3	108,8
1970	103,3	107,9	104,2	112,2	106,3	104,9	123,0	112,0	105,1	115,1	110,3
1971	101,8	106,1	106,8	110,0	107,4	106,8	121,7	103,7	103,6	116,1	110,6
1972	103,1	110,8	107,6	106,7	109,8	113,5	120,1	104,7	105,5	118,0	112,0
1973	103,8	108,2	104,6	112,7	110,5	119,9	109,9	110,3	104,9	107,4	107,5
1974	101,0	97,0	96,8	104,5	95,6	101,6	95,5	112,2	99,2	94,5	96,5
1975	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0
1976	99,1	99,0	97,5	98,1	98,4	103,7	97,1	102,0	100,2	98,5	98,3
1977	99,5	97,7	97,4	101,7	96,2	101,8	99,0	98,5	100,7	99,6	98,6
1978	99,3	100,6	101,7	98,4	100,1	103,7	102,1	99,8	101,4	103,7	101,7
1979	99,3	96,3	97,6	93,8	99,2	99,6	100,7	101,8	99,1	108,0	100,8
1980	95,3	90,2	92,0	95,5	92,4	92,8	97,3	98,7	97,3	111,5	97,3
1981	91,6	88,0	88,7	89,6	88,2	91,4	91,7	96,1	96,2	116,0	94,8
1982	91,5	87,4	90,4	87,9	92,2	93,8	94,8	94,2	98,4	118,1	97,1
(1983)	91,8	88,3	91,7	90,1	95,1	95,3	96,2	94,0	97,5	114,9	98,0

Table 22

Compensation per employee; total economy

(national currency, annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1961	3,2	12,9	10,2	6,5	10,6	9,5	8,2	2,8	7,4	6,7	8,4
1962	7,2	11,1	9,1	6,9	11,6	9,3	13,5	4,8	6,8	4,6	8,8
1963	8,0	4,6	6,1	7,5	11,4	6,1	19,7	8,1	9,3	4,9	9,1
1964	9,7	10,7	8,2	13,1	9,2	14,2	11,6	13,3	16,5	7,0	9,4
1965	9,5	13,8	9,5	12,6	6,5	3,2	8,2	4,2	11,7	6,8	8,4
1966	8,6	9,6	7,6	12,7	6,0	8,5	8,0	5,0	11,1	6,4	7,3
1967	7,4	10,9	3,3	9,2	6,9	8,0	8,3	2,8	9,3	6,2	6,2
1968	6,3	9,6	6,7	9,6	11,2	10,6	7,6	5,9	8,6	7,8	8,2
1969	8,4	11,4	9,5	10,2	11,1	13,9	7,6	5,6	13,2	7,1	9,4
1970	9,4	11,0	16,0	9,6	9,8	16,8	13,6	14,8	12,6	13,0	13,2
1961-70	7,8	10,5	8,6	9,8	9,4	9,9	10,6	6,7	10,6	7,1	8,8
1971	11,7	11,7	12,6	9,2	11,5	14,0	13,1	9,3	13,4	11,4	12,2
1972	14,0	7,9	9,1	12,4	10,3	16,9	11,1	8,8	12,9	13,0	11,1
1973	13,0	13,1	12,1	17,6	12,8	19,8	19,6	12,8	15,1	13,1	14,2
1974	18,2	18,4	11,5	18,7	17,6	18,6	22,1	21,3	15,8	18,8	17,4
1975	16,5	14,0	7,2	19,7	18,6	27,0	21,0	11,3	13,3	30,9	18,1
1976	16,1	11,7	7,9	23,9	14,7	19,3	20,9	13,2	10,9	14,6	13,7
1977	8,9	9,7	6,6	22,3	12,6	13,8	21,4	9,4	8,1	10,4	11,2
1978	7,6	9,2	5,6	23,1	12,5	14,8	16,2	5,6	7,2	13,8	10,8
1979	5,4	9,4	5,9	21,9	13,1	18,1	17,9	6,0	6,0	16,4	11,3
1980	8,8	9,9	6,8	14,8	14,8	19,5	22,2	7,8	5,5	20,2	12,9
1971-80	12,0	11,5	8,5	18,3	13,8	18,1	18,5	10,5	10,8	16,1	13,3
1981	7,3	10,2	5,3	23,9	14,5	18,5	22,0	7,7	3,3	14,7	11,5
1982	8,0	11,1	4,4	26,2	14,5	14,9	17,1	6,9	5,7	8,8	9,6
(1983)	6,0	7,5	3,8	17,3	9,7	12,2	15,6	7,1	3,2	7,9	7,2

Table 23

Real compensation per employee; total economy

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1961	0,5	8,9	6,4	5,4	7,0	6,9	6,2	2,3	5,2	3,7	5,4
1962	6,1	4,6	5,7	5,6	6,9	5,4	7,8	3,9	4,0	0,7	4,6
1963	4,1	−1,0	2,9	4,1	5,3	3,8	11,8	5,0	5,3	2,9	4,8
1964	5,4	6,4	5,8	10,7	5,6	6,3	6,2	9,9	9,0	3,3	5,4
1965	4,7	7,3	5,9	7,7	3,8	−1,8	4,4	0,9	7,3	1,8	4,1
1966	4,3	9,2	4,0	8,9	2,8	5,5	5,0	1,5	5,3	2,3	3,7
1967	4,8	3,9	1,7	7,2	3,7	4,7	5,1	0,5	6,0	3,5	3,6
1968	3,3	1,8	4,9	8,8	5,8	5,9	6,0	3,3	5,7	3,2	4,8
1969	5,3	6,4	6,9	7,0	3,7	6,3	4,6	3,7	6,6	1,5	4,5
1970	5,6	3,7	11,4	6,2	4,6	8,0	8,2	10,5	8,0	6,6	7,8
1961-70	4,4	5,1	5,5	7,1	4,9	5,1	6,5	4,1	6,2	2,9	4,9
1971	6,2	3,4	6,1	6,1	5,7	4,2	7,1	4,4	4,6	2,6	5,2
1972	8,1	−0,2	3,3	8,5	4,2	6,6	4,4	3,5	3,7	6,1	4,4
1973	6,6	2,0	4,3	2,2	5,6	7,4	6,4	7,5	5,4	4,2	5,0
1974	5,2	3,2	3,9	−4,0	3,8	2,4	1,0	10,3	5,2	1,3	2,8
1975	3,6	3,5	1,3	6,0	6,5	3,8	2,9	1,0	2,4	6,0	3,9
1976	7,9	2,4	3,5	9,0	4,4	0,4	2,4	3,4	1,9	−0,8	2,6
1977	1,8	−0,7	2,8	9,2	3,1	0,8	2,7	3,4	2,1	−4,2	1,2
1978	3,3	0,0	2,8	9,3	3,3	6,6	3,0	2,0	2,7	4,4	3,3
1979	1,6	−0,7	1,6	3,7	2,3	3,4	2,6	0,1	1,9	2,8	2,2
1980	1,6	−1,2	1,4	−6,1	1,4	1,6	1,6	0,1	−1,1	3,2	1,5
1971-80	4,6	1,2	3,1	4,3	4,0	3,7	3,4	3,5	2,9	2,5	3,2
1981	−1,5	−1,5	−0,3	−0,4	1,5	−0,9	2,5	−0,0	−2,8	3,3	1,3
1982	0,5	1,2	−0,8	4,2	3,3	−1,9	0,4	−2,8	0,0	0,7	0,9
(1983)	−1,7	0,9	0,8	−2,6	0,6	1,1	0,5	−1,2	0,4	2,0	0,8

Table 24

Real product wage; total economy

(as % of GDP at factor cost)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1960	69,2	72,2	70,5	102,8	72,6	86,5	81,6	66,4	64,2	72,4	74,6
1961	68,4	73,2	72,1	98,4	73,5	87,0	79,8	65,6	66,5	73,0	75,1
1962	69,7	73,9	72,5	98,6	73,5	88,1	79,4	68,7	67,3	73,7	75,2
1963	70,4	74,3	72,6	94,4	74,0	88,0	81,5	68,4	68,8	72,8	75,3
1964	70,0	73,5	71,4	94,3	73,9	89,2	82,8	69,1	69,3	72,6	75,0
1965	70,2	76,2	71,6	92,5	73,2	86,5	81,5	69,3	70,0	73,2	74,8
1966	71,8	76,6	72,2	93,3	72,2	89,9	79,8	69,7	72,2	73,9	74,7
1967	72,2	77,4	71,5	93,8	71,2	87,9	79,9	69,0	71,8	73,3	74,2
1968	71,3	77,9	70,0	94,7	72,1	86,4	78,7	66,4	71,4	72,9	73,6
1969	70,7	77,1	70,5	91,6	71,8	86,2	76,7	62,0	71,9	74,2	73,5
1970	68,9	78,1	72,1	88,3	70,8	88,6	78,3	64,1	73,1	76,0	74,3
1961-70	70,4	75,8	71,6	94,0	72,6	87,8	79,8	67,2	70,2	73,6	74,6
1971	70,9	79,4	73,2	85,2	70,9	88,6	80,8	70,5	74,2	73,4	74,6
1972	71,3	76,0	72,8	84,3	69,9	85,0	80,0	71,2	73,4	74,2	74,2
1973	71,5	75,2	73,6	76,7	70,1	84,5	80,6	66,4	73,3	73,8	74,3
1974	73,3	78,0	75,1	76,8	72,1	90,3	81,1	66,7	74,5	75,9	75,9
1975	75,9	79,0	75,0	79,2	74,2	90,0	85,0	83,2	76,3	78,2	77,8
1976	77,4	77,6	73,5	80,9	74,4	89,4	83,8	80,1	73,6	75,3	76,5
1977	77,9	78,0	73,2	84,5	74,6	83,0	85,0	86,6	73,8	73,1	76,1
1978	78,2	77,9	72,4	87,8	74,6	81,3	84,6	83,3	73,9	72,5	75,8
1979	78,1	78,3	71,9	88,7	74,4	85,2	82,3	80,7	74,2	74,1	75,6
1980	79,2	79,4	72,9	85,0	75,7	90,8	81,5	81,1	74,1	75,7	76,4
1971-80	75,4	77,9	73,4	82,9	73,1	86,8	82,5	77,0	74,1	74,6	75,7
1981	80,6	76,9	73,1	86,5	76,6	91,0	84,9	83,1	72,3	75,9	77,2
1982	79,2	74,6	72,1	87,9	75,8	88,1	84,7	84,1	71,3	74,7	76,4
(1983)	77,5	72,6	70,8	86,8	74,9	87,6	88,0	84,6	70,7	73,9	76,2

Table 25

Relative unit labour costs in a common currency; manufacturing industry

(1972 = 100)

	B/L	DK	D	GR	F	IRL	I	NL	UK	EC 9
1960	92,4	91,1	71,6	116,9	119,9	80,2	80,8	75,8	103,8	80,7
1961	86,4	92,7	76,8	107,9	120,2	79,4	78,5	81,4	107,8	84,8
1962	86,0	93,1	79,6	108,3	122,0	81,9	80,8	81,8	107,8	86,4
1963	87,8	95,5	79,0	105,8	123,6	83,8	93,6	85,6	104,5	89,5
1964	90,5	95,5	77,4	109,5	122,7	88,2	97,8	90,7	103,3	90,4
1965	93,6	98,5	78,0	110,9	120,1	86,5	92,1	94,5	107,5	90,4
1966	95,3	101,9	79,6	115,2	114,4	88,8	86,3	96,9	109,0	90,1
1967	96,4	101,9	77,7	118,2	111,3	88,3	87,8	100,7	105,0	88,5
1968	97,4	98,5	77,5	122,5	116,0	85,5	87,1	101,5	91,2	84,8
1969	98,5	103,2	79,3	121,0	110,3	89,6	89,1	98,3	94,2	85,5
1970	95,0	101,3	91,0	115,0	100,2	91,1	93,8	94,0	98,6	90,9
1971	96,1	101,2	95,4	107,5	97,4	95,1	98,0	95,8	102,2	95,2
1972	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0
1973	98,5	110,9	112,2	99,2	103,9	99,4	97,4	105,4	89,3	105,9
1974	104,5	113,3	111,1	112,4	91,6	97,0	91,5	108,7	92,5	100,5
1975	104,7	106,9	100,9	98,8	107,1	99,4	102,0	109,9	97,5	107,4
1976	106,1	105,9	102,4	101,9	105,8	94,5	89,2	107,2	89,7	99,9
1977	108,8	105,6	107,8	110,0	102,2	93,1	91,2	110,9	87,0	102,5
1978	106,4	111,7	112,1	106,6	103,2	94,4	89,9	109,9	92,4	107,6
1979	103,1	113,3	113,3	112,8	105,4	95,9	90,2	109,1	106,8	116,3
1980	100,5	100,1	109,8	110,9	107,9	102,4	89,9	102,9	132,4	122,5
1981	90,9	89,7	101,5	114,5	100,5	96,4	87,4	91,4	135,7	105,7
1982	78,2	88,2	102,3	98,7	94,8	97,2	89,1	94,7	126,4	99,3
(1983)	75,3	89,3	102,2	78,6	94,1	93,1	95,7	92,2	115,4	95,7

Table 26

Exports of goods and services at current prices

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	36,4	31,6	17,0	8,7	11,4	24,7	11,0	73,2	46,6	20,9	19,0
1959	35,1	30,9	17,5	7,8	12,9	24,2	11,5	74,9	47,8	20,4	19,7
1960	37,4	30,7	17,5	7,7	13,9	25,5	12,1	85,1	46,1	20,4	19,3
1961	38,7	28,3	16,7	7,7	13,4	28,2	12,4	81,2	43,8	20,0	18,7
1962	40,4	27,1	16,2	7,9	12,3	26,1	12,3	78,0	42,9	19,6	18,2
1963	41,5	28,8	16,5	8,0	12,0	27,3	11,8	74,9	42,8	19,4	18,1
1964	42,3	28,2	16,7	7,4	12,2	26,9	12,5	76,8	41,7	18,9	18,2
1965	41,7	27,6	16,8	7,2	12,7	27,7	13,9	78,6	41,1	18,9	18,5
1966	43,3	26,3	17,8	9,1	12,7	30,8	14,3	75,3	40,1	18,9	18,8
1967	42,3	25,0	19,0	8,9	12,6	31,6	14,2	75,1	39,1	18,6	18,9
1968	44,4	25,3	19,9	8,1	12,8	32,8	15,2	76,9	39,6	20,9	19,9
1969	48,3	25,3	20,3	8,0	13,6	31,9	15,9	81,2	41,4	21,7	20,7
1970	50,6	25,5	19,8	8,1	15,3	32,4	15,9	86,9	43,3	22,6	21,3
1961-70	43,3	26,7	18,0	8,0	12,9	29,6	13,8	78,5	41,6	20,0	19,1
1971	49,4	25,1	19,6	7,5	16,0	31,8	16,3	84,2	43,5	22,5	21,4
1972	49,9	24,5	19,5	8,6	16,2	31,4	16,9	79,5	43,1	21,3	21,3
1973	54,4	26,2	20,8	11,0	17,2	34,9	17,0	85,9	45,3	23,2	22,6
1974	60,1	29,3	25,2	13,1	20,5	39,1	20,7	99,3	52,0	27,3	26,8
1975	52,5	27,7	23,5	13,3	18,5	40,3	21,0	88,3	48,1	25,2	25,0
1976	55,9	26,5	24,8	13,3	19,1	44,1	22,9	84,2	49,4	27,4	26,4
1977	54,5	26,4	24,6	12,4	20,1	47,9	24,0	82,4	46,2	29,0	26,8
1978	52,7	25,5	24,0	12,5	19,9	49,1	24,3	79,1	43,6	27,5	26,2
1979	58,2	26,9	24,2	12,2	20,7	49,5	25,3	85,4	47,8	27,3	27,0
1980	61,9	30,5	25,6	15,4	21,0	50,0	22,7	81,4	51,3	26,7	27,3
1971-80	54,9	26,9	23,2	11,9	18,9	41,8	21,1	85,0	47,0	25,7	25,1
1981	67,1	33,2	28,0	14,4	22,2	50,1	24,7	79,4	56,8	26,1	28,9
1982	71,6	32,7	29,1	13,4	21,6	49,2	24,5	84,2	56,4	25,8	29,1
(1983)	71,6	32,6	28,3	13,7	22,1	51,4	24,0	80,5	57,5	25,6	28,9

Table 27

Exports of goods and services at 1975 prices

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	0,2	9,1	3,4	1,2	7,4	−1,7	12,6	:	6,1	−1,6	3,4
1959	6,6	5,6	12,0	2,0	13,5	1,7	17,7	:	10,0	2,7	9,1
1960	10,5	7,9	13,0	9,0	17,5	12,9	19,8	:	14,0	5,7	8,7
1961	9,1	4,2	4,3	12,0	5,1	17,2	16,1	3,2	2,1	3,3	5,6
1962	10,4	5,4	5,0	7,4	1,2	−1,0	11,2	−1,9	6,5	1,9	4,7
1963	8,1	10,4	7,3	2,3	7,5	9,6	7,3	3,5	5,6	4,5	6,5
1964	9,7	8,3	8,7	4,3	7,3	8,2	12,4	13,4	12,1	4,0	8,0
1965	6,0	8,1	7,0	11,6	11,0	8,9	20,3	6,2	7,7	4,9	8,6
1966	7,7	2,7	10,1	35,2	6,3	10,6	11,2	−0,3	6,0	3,9	7,4
1967	4,2	3,4	7,9	9,0	8,3	10,3	8,7	2,1	7,3	1,5	5,9
1968	12,2	10,1	13,9	−0,0	11,2	9,0	15,6	10,7	13,2	12,0	12,8
1969	15,4	5,5	9,4	12,7	16,1	4,6	12,3	13,8	16,0	8,7	11,5
1970	10,4	4,4	5,2	9,8	16,3	5,7	6,0	7,8	12,2	4,6	7,8
1961-70	9,3	6,2	7,9	10,1	8,9	8,2	12,0	5,7	8,8	4,9	7,9
1971	4,8	4,5	6,1	2,1	11,2	4,9	7,2	3,4	10,5	7,0	7,4
1972	11,3	5,3	7,2	24,6	13,4	6,1	11,5	4,0	10,8	0,5	8,0
1973	14,1	8,7	11,5	28,0	12,5	11,2	3,8	14,5	12,7	11,5	10,9
1974	3,8	4,7	12,6	4,8	10,8	0,5	9,9	14,1	2,8	6,5	8,3
1975	−7,9	−1,8	−6,8	7,2	−1,5	8,2	3,7	−16,1	−3,0	−3,3	−3,1
1976	13,6	4,8	11,5	12,7	9,6	8,9	13,2	1,7	10,6	7,9	10,5
1977	2,2	4,5	4,2	−0,7	8,6	13,7	6,7	1,4	−1,7	5,5	4,8
1978	3,2	2,3	3,3	14,6	6,0	12,6	10,1	3,5	3,6	2,2	4,8
1979	7,8	8,7	4,7	6,4	7,1	7,0	9,1	9,3	7,5	3,0	6,2
1980	4,6	5,2	5,5	9,8	3,0	7,4	−4,3	−1,1	1,4	0,8	2,0
1971-80	5,6	4,7	5,8	10,6	8,0	8,0	7,0	3,1	5,4	4,1	5,9
1981	2,4	5,4	7,7	5,4	4,6	2,0	6,0	2,0	0,8	−1,8	3,8
1982	2,0	2,1	3,5	−5,7	−3,7	4,0	1,2	0,3	−0,9	0,6	0,7
(1983)	1,0	4,6	−1,0	−2,8	−0,1	7,5	1,7	−3,3	2,9	0,3	0,6

Table 28

Intra-Community exports of goods at current prices

(as % of GDP)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1958	17,0	15,8	5,9	4,0	2,8	21,4	2,9	21,9	3,2	5,4
1959	17,5	15,2	6,0	3,2	3,7	19,5	3,3	22,9	3,2	5,8
1960	20,2	14,8	6,4	2,6	4,4	20,6	4,0	23,3	3,3	6,3
1961	20,8	13,4	6,7	2,3	4,8	23,0	4,4	23,2	3,6	6,6
1962	22,6	12,7	6,7	3,0	4,7	20,2	4,7	23,6	4,0	6,8
1963	25,1	13,4	7,4	2,7	4,8	21,4	4,4	24,5	4,2	7,1
1964	26,3	12,9	7,5	2,8	4,9	22,0	5,1	25,0	4,2	7,4
1965	27,3	12,1	7,3	2,7	5,2	20,4	5,9	24,6	4,0	7,5
1966	27,4	11,3	7,8	2,7	5,4	20,9	6,1	23,5	4,0	7,7
1967	26,3	10,3	8,4	3,3	5,1	22,8	5,8	22,9	3,8	7,6
1968	27,8	9,7	8,7	3,2	5,2	22,2	6,1	23,6	4,2	8,0
1969	32,0	9,3	9,3	3,2	6,1	20,8	6,5	25,4	4,6	8,9
1970	33,3	9,2	9,0	3,4	7,1	21,7	6,6	27,1	4,8	9,3
1961-70	26,9	11,4	7,9	2,9	5,3	21,5	5,6	24,3	4,1	7,7
1971	31,8	8,7	9,1	3,2	7,3	21,9	7,0	27,9	4,8	9,4
1972	32,9	8,7	8,7	3,6	7,6	22,6	7,5	27,5	4,7	9,6
1973	35,1	10,1	9,4	4,9	8,1	24,5	7,5	29,1	5,7	10,4
1974	36,0	10,6	10,7	5,4	9,3	28,3	8,4	33,3	6,8	11,9
1975	31,9	10,5	9,7	5,5	7,7	30,9	8,5	30,7	6,2	10,8
1976	35,1	10,1	10,7	5,7	8,2	30,9	9,8	32,3	7,5	12,0
1977	33,5	9,7	10,5	5,0	8,5	35,3	10,1	27,7	8,5	12,0
1978	32,8	10,1	10,4	5,4	8,6	35,6	10,6	26,0	8,7	11,9
1979	36,5	11,1	11,2	5,0	9,2	36,6	11,3	29,6	9,4	12,8
1980	38,1	12,9	11,6	6,2	8,9	35,4	9,7	31,5	9,3	12,7
1971-80	34,4	10,2	10,2	5,0	8,3	30,2	9,0	29,6	7,2	11,4
1981	39,2	13,0	12,0	5,1	8,6	32,6	9,3	34,7	8,7	12,6
1982	42,6	13,4	12,9	5,2	8,3	32,7	9,7	35,0	8,8	13,0

Table 29

Extra-Community exports of goods at current prices

(as % of GDP)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1958	14,5	11,3	10,5	4,0	6,9	2,6	5,7	15,9	12,7	9,8
1959	14,3	11,2	10,3	3,4	7,4	3,1	5,5	15,9	12,0	9,8
1960	13,8	11,4	10,2	3,5	7,6	3,2	6,2	14,9	12,0	9,8
1961	12,9	11,2	9,8	3,7	7,0	3,4	6,2	14,3	11,4	9,3
1962	12,1	11,0	9,0	3,4	6,1	3,5	5,8	13,2	10,9	8,6
1963	11,1	11,9	8,9	3,9	5,8	3,7	5,6	12,2	10,8	8,3
1964	11,0	11,8	9,0	3,4	5,6	3,1	5,7	11,4	10,6	8,2
1965	11,9	11,9	9,3	3,2	5,7	2,9	6,2	11,5	10,8	8,5
1966	11,7	11,7	9,8	3,8	5,6	3,9	6,3	11,5	10,8	8,6
1967	11,2	11,4	10,3	4,0	5,4	5,9	6,5	11,3	10,1	8,5
1968	11,4	11,5	10,4	3,0	5,3	6,3	6,7	10,5	11,0	8,6
1969	11,3	11,8	10,2	3,2	5,2	6,6	6,8	10,4	11,4	8,7
1970	11,5	12,1	9,9	3,1	5,8	6,4	6,7	10,4	11,3	8,8
1961-70	11,6	11,6	9,6	3,5	5,8	4,6	6,3	11,7	10,9	8,6
1971	11,1	11,5	9,9	2,8	5,7	6,0	6,6	9,6	11,2	8,6
1972	11,1	11,3	9,3	3,3	5,7	5,4	6,8	8,9	10,6	8,3
1973	12,2	11,6	10,0	4,0	6,1	7,3	6,8	10,2	11,4	8,9
1974	14,8	13,6	12,6	5,4	7,9	9,3	9,2	12,4	13,0	11,1
1975	12,5	12,6	11,9	5,5	7,7	7,5	9,5	11,2	12,6	10,5
1976	11,9	11,8	12,1	5,7	7,7	9,2	9,8	11,2	13,1	10,7
1977	12,8	12,0	12,3	5,5	8,1	10,1	10,7	10,4	14,3	11,2
1978	12,4	10,7	11,7	5,2	7,5	9,7	10,5	9,7	13,9	10,7
1979	13,0	11,3	11,3	5,1	7,9	9,9	10,6	10,1	12,7	10,6
1980	14,6	12,6	11,9	6,7	8,2	11,3	9,8	11,2	12,4	10,8
1971-80	12,6	11,9	11,3	4,9	7,3	8,6	9,0	10,5	12,5	10,1
1981	16,3	14,8	13,5	6,6	9,2	13,5	12,0	12,9	12,4	12,1
1982	17,1	14,1	13,8	6,0	8,7	13,1	11,2	12,5	12,6	11,9

Table 30

Imports of goods and services at current prices

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	33,6	29,8	14,2	12,8	11,0	34,5	12,0	70,2	44,7	20,0	17,9
1959	35,5	31,2	14,7	12,5	10,5	34,5	11,8	71,1	45,7	20,2	18,4
1960	37,8	32,3	15,3	16,2	11,3	34,9	13,9	72,1	45,2	21,6	19,0
1961	39,3	30,2	14,6	15,9	11,1	37,4	13,9	74,8	44,5	20,0	18,2
1962	40,2	30,3	14,8	16,4	11,0	36,3	14,3	77,4	43,5	19,5	18,1
1963	42,2	28,6	14,9	17,4	11,5	37,9	15,5	75,2	44,5	19,5	18,6
1964	42,4	30,5	15,2	18,3	12,1	38,1	13,7	76,7	44,5	20,2	18,7
1965	41,4	29,4	16,4	19,6	11,7	40,9	13,0	77,2	42,4	19,2	18,5
1966	43,7	28,3	16,0	18,1	12,3	40,1	14,0	72,8	41,8	18,6	18,5
1967	41,5	27,4	15,3	17,5	12,3	38,2	14,5	66,9	40,1	19,3	18,3
1968	43,6	27,1	16,3	17,8	12,6	42,3	14,2	66,8	39,5	21,5	19,2
1969	46,9	27,9	17,5	18,1	14,2	43,7	15,6	66,5	41,1	21,2	20,2
1970	47,8	29,2	17,4	17,8	15,0	42,5	16,6	74,5	44,6	21,7	20,9
1961-70	42,9	28,9	15,8	17,7	12,4	39,7	14,5	72,9	42,6	20,1	18,9
1971	46,6	27,7	17,3	17,7	15,1	41,1	16,4	81,8	43,6	21,1	20,6
1972	45,9	24,8	16,9	19,3	15,3	37,8	17,3	74,9	40,3	21,4	20,4
1973	51,4	28,7	17,1	24,5	16,6	42,6	20,2	74,3	42,0	25,7	22,7
1974	58,8	33,1	20,0	24,9	22,0	54,7	26,2	79,6	49,1	32,7	28,1
1975	51,4	29,3	19,8	26,1	17,8	46,1	22,2	85,3	44,3	27,2	24,6
1976	54,9	31,7	21,6	25,2	20,3	51,6	25,4	79,9	45,3	29,2	26,8
1977	54,5	30,5	21,2	24,6	20,4	56,8	24,5	80,3	44,0	29,2	26,4
1978	52,7	28,0	20,4	23,9	19,3	58,4	23,6	79,8	42,3	26,9	25,1
1979	58,9	29,8	22,4	24,5	20,8	65,6	26,0	83,4	47,0	27,5	27,1
1980	63,8	31,6	24,8	25,6	23,0	63,3	27,4	84,4	50,3	24,7	28,3
1971-80	53,9	29,5	20,2	23,6	19,1	51,8	22,9	80,4	44,8	26,5	25,0
1981	69,3	32,8	26,0	26,5	24,0	64,4	28,2	84,4	51,9	23,4	29,1
1982	75,8	32,6	25,6	28,1	24,3	56,6	27,2	90,3	51,3	23,7	29,0
(1983)	71,3	30,7	24,8	28,6	23,5	53,4	25,6	86,8	52,2	25,3	28,5

Table 31

Imports of goods and services at 1975 prices

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	−4,3	6,4	10,9	20,0	−0,8	10,8	3,5	:	−4,5	1,1	2,3
1959	11,2	21,2	15,2	24,2	−2,0	9,1	11,5	:	12,6	6,5	9,0
1960	12,9	9,5	18,4	27,6	16,9	5,2	37,7	:	16,6	12,0	16,5
1961	7,5	3,7	7,1	13,1	6,5	13,7	13,9	7,4	6,3	−0,8	5,2
1962	8,8	13,8	11,1	10,1	7,9	5,3	15,2	3,2	6,7	2,1	7,7
1963	8,4	−1,6	4,6	15,5	16,6	10,6	21,9	3,6	9,5	3,6	9,0
1964	9,3	21,1	9,7	14,4	15,7	12,9	−6,6	14,4	14,8	10,6	8,8
1965	6,4	6,8	14,8	21,6	2,0	11,0	2,0	4,3	5,8	0,5	5,4
1966	10,1	5,8	2,1	−0,3	11,1	3,5	14,3	−2,5	6,6	2,1	6,0
1967	1,4	4,7	−1,0	7,3	8,8	3,7	13,6	−4,8	6,1	8,6	6,3
1968	12,0	5,2	14,7	10,5	13,3	15,7	5,6	9,3	12,6	8,4	10,5
1969	15,5	13,1	16,7	15,6	22,4	13,4	19,3	11,3	13,9	2,5	13,4
1970	8,0	8,8	13,1	6,0	7,4	3,6	15,9	14,6	14,8	4,9	10,1
1961-70	8,7	8,0	9,1	11,2	11,0	9,3	11,2	5,9	9,6	4,2	8,2
1971	3,3	−0,7	8,9	6,9	7,8	5,0	2,4	8,4	6,1	5,2	5,6
1972	9,6	0,7	6,1	15,0	16,7	5,3	11,4	1,9	5,3	9,4	9,3
1973	18,4	15,3	2,6	34,0	15,4	19,2	10,5	10,9	11,3	11,8	11,3
1974	4,5	−3,6	0,6	−16,8	6,3	−2,5	2,2	7,4	−1,2	1,2	1,5
1975	−8,8	−5,0	2,2	6,0	−7,5	−12,7	−9,6	−9,9	−4,5	−7,6	−5,6
1976	13,0	17,2	12,3	6,3	18,7	15,2	15,4	2,0	10,2	4,7	11,9
1977	4,5	−0,6	2,9	8,3	1,5	13,2	−0,2	0,5	2,7	0,9	2,2
1978	3,0	0,3	6,3	6,5	5,2	15,2	8,1	8,5	6,0	3,1	5,4
1979	9,3	4,8	9,6	6,5	10,5	14,4	13,8	8,0	6,6	10,8	10,3
1980	2,2	−7,8	3,8	−7,1	4,6	−4,4	8,3	1,8	−0,7	−4,6	1,7
1971-80	5,7	1,8	5,5	5,8	7,6	6,3	6,0	3,8	4,1	3,3	5,2
1981	−1,4	−1,5	−0,5	9,0	−1,5	2,1	−5,4	1,8	−7,3	−0,9	−2,2
1982	0,2	2,1	−0,1	5,9	4,8	−4,4	2,1	−0,9	1,1	5,0	2,4
(1983)	−0,9	0,0	0,5	−1,3	−2,7	−1,5	−0,8	−3,0	1,7	4,8	0,5

Table 32

Intra-Community imports of goods at current prices

(as % of GDP)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1958	17,9	17,2	4,7	10,4	2,8	27,1	3,2	21,6	3,7	5,5
1959	18,8	18,2	5,3	9,3	3,2	25,8	3,6	22,7	3,6	5,9
1960	20,0	17,1	5,6	9,4	3,7	24,0	4,7	23,2	3,9	6,3
1961	21,3	16,3	5,6	9,5	4,0	26,7	4,9	25,8	3,8	6,5
1962	22,0	15,9	5,9	10,1	4,3	26,4	5,4	25,4	3,8	6,8
1963	23,6	14,5	6,0	9,4	4,9	28,1	6,2	26,8	3,9	7,1
1964	24,5	15,3	6,3	9,7	5,2	27,9	5,3	26,9	4,3	7,4
1965	24,7	14,5	7,4	10,4	5,1	27,8	4,7	26,0	4,1	7,5
1966	26,5	13,8	7,2	10,2	5,6	26,2	5,2	25,7	4,3	7,8
1967	24,5	12,8	6,9	9,6	5,7	25,2	5,7	24,2	4,6	7,7
1968	25,5	12,3	7,4	9,9	6,1	28,3	5,5	23,8	4,9	8,1
1969	28,2	12,9	8,4	9,5	7,3	29,2	6,3	25,3	4,8	9,0
1970	28,9	13,4	8,3	10,0	7,5	29,6	7,0	27,1	4,9	9,3
1961-70	25,0	14,2	6,9	9,9	5,6	27,5	5,6	25,7	4,3	7,7
1971	30,6	11,7	8,8	9,6	7,4	27,3	6,8	25,3	5,1	9,4
1972	30,2	10,7	8,5	10,2	7,7	26,1	7,5	23,7	5,6	9,5
1973	33,1	12,5	8,4	10,6	8,2	30,3	8,9	24,8	7,2	10,4
1974	35,8	14,3	8,9	10,1	10,0	37,3	10,3	27,0	8,4	11,9
1975	32,3	12,7	9,1	10,9	7,9	31,7	8,8	24,3	7,5	10,7
1976	34,7	14,1	9,7	10,7	9,2	35,6	10,3	24,5	8,1	11,8
1977	34,1	13,7	9,8	11,1	9,1	38,4	9,7	22,5	9,8	12,0
1978	34,1	12,8	9,7	10,7	8,9	40,5	9,8	22,2	9,5	11,8
1979	34,5	14,4	10,5	10,9	9,7	46,3	10,7	24,2	10,3	12,6
1980	37,3	14,5	11,0	10,5	9,6	46,2	11,2	24,3	8,8	12,5
1971-80	33,7	13,1	9,4	10,5	8,8	36,0	9,4	23,5	8,0	11,3
1981	37,1	14,6	11,5	12,2	10,2	47,2	10,6	24,6	8,4	12,6
1982	40,6	14,8	11,5	12,1	10,8	41,0	10,4	24,7	9,0	12,8

Table 33

Extra-Community imports of goods at current prices

(as % of GDP)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1958	14,8	12,0	9,0	9,1	7,8	11,2	7,7	21,4	14,3	10,7
1959	14,7	12,5	8,8	9,0	6,9	12,6	6,8	20,1	14,0	10,3
1960	15,9	14,9	9,2	11,7	7,3	12,6	8,7	20,2	14,9	11,1
1961	15,0	14,0	8,6	9,7	6,9	13,0	8,6	19,2	13,4	10,3
1962	14,9	14,8	8,7	7,8	6,7	12,1	8,5	18,1	13,0	10,0
1963	14,9	14,2	8,6	8,9	6,5	12,3	9,0	18,0	13,1	10,0
1964	15,3	15,7	8,5	8,3	6,7	12,5	8,0	17,8	14,2	10,2
1965	14,6	15,1	8,9	9,8	6,2	12,7	7,9	16,6	13,2	9,9
1966	14,8	14,8	8,6	9,4	6,4	12,5	8,3	16,4	12,5	9,7
1967	13,9	14,6	8,0	7,9	5,8	12,4	8,3	15,4	12,5	9,3
1968	14,8	14,1	8,1	8,4	5,4	12,6	7,5	14,7	13,8	9,3
1969	15,0	14,3	8,4	8,8	5,7	12,6	7,9	14,7	13,5	9,5
1970	15,2	15,0	8,2	10,1	6,3	11,6	8,2	16,2	13,2	9,6
1961-70	14,8	14,7	8,5	8,9	6,3	12,4	8,2	16,7	13,2	9,8
1971	13,0	14,0	7,9	9,3	6,0	12,2	7,6	16,0	12,0	9,0
1972	12,1	12,6	7,1	8,4	6,0	10,8	7,5	14,2	12,0	8,6
1973	13,6	14,7	7,4	10,6	6,5	11,3	9,1	15,6	14,5	9,6
1974	18,2	17,0	9,3	13,3	9,9	16,5	13,8	19,9	19,0	12,9
1975	15,6	14,9	8,9	14,7	8,1	13,5	11,3	18,2	15,1	11,2
1976	16,5	15,7	10,1	16,2	9,2	15,0	13,1	19,6	16,4	12,4
1977	16,1	14,9	9,8	15,0	9,2	17,1	12,6	18,2	15,2	12,0
1978	15,1	12,9	9,3	14,1	8,3	16,5	11,8	16,3	15,3	11,3
1979	19,0	14,1	10,4	14,1	8,8	17,6	13,2	18,4	14,7	12,2
1980	21,7	15,0	12,0	15,9	11,0	15,4	14,0	21,1	13,9	13,5
1971-80	16,1	14,6	9,2	13,2	8,3	14,6	11,4	17,8	14,8	11,3
1981	25,4	15,9	12,4	12,1	10,9	15,6	15,4	22,3	12,9	13,8
1982	25,9	15,5	12,0	14,0	10,5	14,2	14,4	21,1	13,0	13,4

Table 34

Current account of balance of payments

(as % of GDP)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1958	3,9	2,9	2,5	:	−0,4	−1,6	2,0	4,5	1,7	1,7
1959	0,7	0,4	1,6	:	1,5	−6,4	2,5	4,8	0,7	1,5
1960	0,7	−1,6	1,6	−2,9	1,5	−0,1	0,8	3,0	−1,0	0,7
1961	0,3	−2,0	1,0	−2,2	1,1	0,2	1,2	1,4	0,0	0,7
1962	0,7	−3,4	−0,1	−1,6	1,0	−1,8	0,6	1,1	0,4	0,4
1963	−0,4	0,1	0,2	−2,2	0,3	−2,8	−1,4	0,7	0,3	−0,0
1964	0,2	−2,4	0,2	−4,3	−0,3	−3,5	1,1	−1,1	−1,3	−0,3
1965	0,6	−1,8	−1,3	−5,8	0,8	−4,4	3,6	0,1	−0,2	0,2
1966	−0,1	−1,9	0,3	−2,0	0,1	−1,6	3,2	−1,0	0,1	0,4
1967	1,2	−2,4	2,2	−2,2	0,0	1,4	2,2	−0,3	−0,9	0,7
1968	1,4	−1,7	2,3	−3,6	−0,5	−1,3	3,3	0,3	−0,8	0,8
1969	1,8	−2,8	1,4	−4,0	−1,1	−4,8	2,7	0,3	0,7	0,6
1970	3,2	−3,9	0,6	−3,1	0,1	−4,0	1,2	−1,5	1,3	0,5
1961-70	0,9	−2,2	0,7	−3,1	0,2	−2,3	1,8	0,0	−0,0	0,4
1971	2,3	−2,4	0,4	−1,5	0,6	−3,8	1,8	−0,3	1,8	0,8
1972	3,9	−0,4	0,4	−1,3	0,5	−2,2	1,6	3,0	0,2	0,8
1973	2,8	−1,7	1,3	−3,8	−0,2	−3,5	−1,8	4,0	−2,0	0,0
1974	1,7	−3,1	2,7	−3,3	−2,3	−9,9	−4,7	3,2	−4,6	−1,0
1975	0,7	−1,5	1,0	−4,2	−0,0	−0,5	−0,2	2,5	−2,0	−0,0
1976	1,0	−4,9	0,9	−2,6	−1,5	−3,9	−1,5	3,2	−1,7	−0,5
1977	−0,4	−4,0	0,8	−2,7	−0,7	−3,5	1,2	0,8	−0,1	0,1
1978	−0,5	−2,7	1,4	−2,3	0,6	−4,0	2,4	−0,8	0,5	0,8
1979	−1,6	−4,7	−0,8	−2,9	−0,0	−11,2	1,7	−1,2	−0,0	−0,4
1980	−3,6	−3,7	−1,9	−0,9	−1,4	−10,0	−2,5	−1,5	1,6	−1,3
1971-80	0,6	−2,9	0,6	−2,6	−0,4	−5,3	−0,2	1,3	−0,6	−0,1
1981	−4,1	−3,1	−1,1	−2,2	−1,4	−13,8	−2,3	2,4	2,4	−0,7
1982	−2,0	−4,2	0,5	−3,8	−2,9	−8,3	−1,6	2,7	1,5	−0,6
(1983)	−0,9	−2,2	0,9	−5,0	−1,8	−2,6	−0,4	3,3	0,2	−0,2

Table 35

Structure of EC exports by country and region, 1958 and 1982

(as % of total exports)

Exports of / to	BLEU		DK		D		GR		F		IRL		I		NL		UK		EC	
	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982
BLEU	—	—	1,2	1,8	6,6	7,3	1,0	1,7	6,3	8,6	0,8	4,5	2,3	2,9	15,0	14,2	1,9	4,4	4,9	6,4
DK	1,6	1,0	—	—	3,0	2,0	0,2	0,8	0,8	0,7	0,1	0,7	0,8	0,7	2,6	1,7	2,4	1,9	2,0	1,4
D	11,6	20,5	20,1	17,5	—	—	20,5	19,0	10,4	14,8	2,2	9,4	14,3	15,6	19,0	29,5	4,2	9,5	7,4	11,7
GR	0,7	0,5	0,4	0,8	1,4	1,1	—	—	0,7	1,0	0,1	0,4	2,1	1,8	0,9	1,1	0,7	0,5	1,0	1,0
F	10,6	19,4	3,0	5,6	7,6	14,0	12,9	6,9	—	—	0,8	8,7	5,3	15,2	4,9	10,4	2,4	8,0	4,6	10,7
IRL	0,4	0,4	0,3	0,5	0,3	0,4	0,4	0,2	0,2	0,5	—	—	0,1	0,3	0,5	0,5	3,5	5,1	1,1	1,2
I	2,3	5,0	5,3	4,9	5,0	7,3	6,0	8,8	3,4	11,3	0,4	2,9	—	—	2,7	5,5	2,1	3,5	3,1	5,9
NL	20,7	14,2	2,2	3,5	8,1	8,5	2,0	4,1	2,0	4,6	0,5	5,2	2,1	3,1	—	—	3,1	8,1	5,4	6,5
UK	5,7	9,7	25,9	14,0	4,0	7,6	7,6	4,8	4,9	7,2	78,8	58,8	6,8	6,3	11,9	9,3	—	—	5,5	6,9
Total intra-Community trade	53,5	70,6	58,3	48,6	35,9	48,1	50,5	46,4	28,6	48,7	83,6	70,6	33,8	45,9	57,5	72,2	20,3	41,0	34,9	51,7
Other European OECD countries	10,4	8,5	17,2	25,7	23,7	19,0	6,7	6,8	10,5	11,8	1,8	5,8	16,6	12,9	12,3	8,3	9,6	13,1	16,4	13,9
USA	9,4	4,4	9,3	6,1	7,3	6,6	13,6	8,9	5,9	5,7	5,9	7,1	9,7	7,1	5,6	3,2	8,8	13,6	7,8	7,1
Canada	1,1	0,4	0,7	0,7	1,2	0,6	0,3	0,3	0,8	0,8	0,7	1,2	1,2	0,8	0,8	0,3	5,8	1,5	2,3	0,7
Japan	0,6	0,6	0,2	1,6	1,0	1,2	1,4	0,6	0,3	1,2	0,1	1,3	0,3	1,1	0,4	0,5	0,6	1,2	0,6	1,0
Australia	0,6	0,2	0,3	0,5	1,0	0,7	0,1	0,5	0,4	0,5	0,1	1,1	1,0	0,7	0,7	0,3	7,1	1,8	2,5	0,8
Developing countries of which:	18,8	11,6	9,7	13,6	22,3	17,0	7,2	28,0	48,4	27,0	1,6	10,0	27,9	25,7	18,1	11,1	33,8	23,2	27,9	19,5
OPEC	3,3	4,4	2,3	5,3	4,8	8,9	0,1	15,6	21,3	11,0	1,3	5,2	7,5	14,5	4,5	5,0	7,0	10,4	7,8	9,2
Other developing countries	15,5	7,2	7,3	8,3	17,5	8,1	7,1	12,4	27,1	16,0	1,3	4,8	20,4	11,2	13,7	6,1	26,8	12,8	20,1	10,3
Centrally-planned economies	3,8	2,2	3,8	2,6	5,0	4,8	16,3	8,4	3,7	3,6	0,2	1,2	4,7	3,8	2,0	1,7	3,1	1,8	3,9	3,3
Rest of world and unspecified	1,9	1,5	0,5	0,6	2,6	1,9	4,0	0,2	1,3	0,7	6,2	1,7	5,1	2,0	2,6	2,4	10,8	2,8	3,8	2,0
World (excl. EC)	46,5	29,4	41,7	51,4	64,1	51,9	49,5	53,6	71,4	51,3	16,4	29,4	66,2	54,1	42,5	27,8	79,7	59,0	65,1	48,3
World (incl. EC)	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Table 36

Structure of EC imports by country and region, 1958 and 1982

(as % of total imports)

Imports of / from	BLEU		DK		D		GR		F		IRL		I		NL		UK		EC	
	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982	1958	1982
BLEU	—	—	3,8	2,8	4,5	7,0	3,3	2,4	5,4	8,6	1,8	2,3	2,0	3,2	17,9	11,0	1,6	4,8	4,4	5,9
DK	0,5	0,5	—	—	3,4	1,8	0,7	1,0	0,6	0,8	0,7	0,8	2,2	0,9	0,7	1,0	3,1	2,2	2,0	1,3
D	17,2	19,9	19,8	20,5	—	—	20,3	17,1	11,6	17,9	4,0	7,3	12,1	16,1	19,5	22,2	3,6	12,3	8,2	12,7
GR	0,1	0,2	0,0	0,2	1,7	0,7	—	—	0,6	0,4	0,2	0,1	0,5	0,6	0,1	0,3	0,2	0,3	0,4	0,4
F	11,6	13,8	3,4	3,9	7,6	11,4	5,4	7,1	—	—	1,6	4,3	4,9	12,5	2,8	6,5	2,7	7,2	4,2	8,1
IRL	0,1	0,4	0,0	0,3	0,1	0,5	0,0	0,3	0,1	0,6	—	—	0,1	0,3	0,1	0,6	2,9	3,3	0,9	0,9
I	2,1	3,6	1,7	2,9	5,5	7,6	8,8	9,2	2,4	9,7	0,9	2,2	—	—	1,8	3,0	2,0	4,6	2,5	5,4
NL	15,7	17,2	7,3	7,6	8,0	12,8	4,8	5,4	2,5	6,4	2,9	4,6	2,6	4,3	—	—	4,2	6,1	6,4	8,0
UK	7,4	5,5	22,8	10,6	4,4	7,2	9,9	3,7	3,6	6,4	56,4	52,2	5,5	4,0	7,4	9,4	—	—	5,0	6,2
Total intra-Community trade	54,7	61,1	59,0	48,8	35,2	49,1	53,3	46,2	26,7	50,7	68,4	73,8	29,8	41,8	50,1	54,0	20,3	40,8	34,0	48,9
Other European OECD countries	8,1	6,8	19,5	25,2	15,8	14,9	9,5	7,1	8,0	9,3	4,3	5,1	12,0	9,9	7,7	7,7	13,9	14,9	12,0	11,7
USA	9,9	7,2	9,1	7,0	13,6	7,1	13,7	4,2	10,0	7,0	7,0	11,3	16,2	6,8	11,3	9,4	9,3	14,5	11,4	8,5
Canada	1,4	0,7	0,2	0,5	3,1	0,9	0,8	0,5	1,0	0,6	3,0	1,1	1,4	0,9	1,5	0,7	8,2	2,4	3,7	1,0
Japan	0,6	1,9	1,5	2,8	0,6	3,2	2,0	6,3	0,2	2,4	1,1	2,4	0,4	1,3	0,8	2,1	0,9	4,7	0,7	2,8
Australia	1,7	0,3	0,0	0,1	1,2	0,4	0,3	0,2	2,4	0,5	1,2	0,0	3,0	0,5	0,2	0,3	5,4	0,8	2,7	0,5
Developing countries of which:	19,7	15,6	6,1	9,8	24,4	17,8	9,6	28,6	46,7	25,0	9,7	4,0	31,2	30,2	25,0	19,8	35,0	16,6	30,3	20,4
OPEC	5,9	8,5	0,3	3,4	6,7	8,7	1,7	22,1	19,7	15,9	0,7	1,0	13,9	20,1	11,5	10,7	11,3	6,5	10,9	11,4
Other developing countries	13,8	7,1	5,8	6,4	17,7	9,1	7,8	6,5	27,0	9,1	9,0	3,0	17,3	10,1	13,5	9,1	23,7	10,1	19,4	9,0
Centrally-planned economies	2,0	3,5	4,6	4,5	5,3	5,6	8,1	5,4	3,3	3,6	1,2	1,5	3,6	6,6	2,6	5,7	3,2	2,6	3,5	4,6
Rest of world and unspecified	1,9	2,9	0,0	1,3	0,8	1,0	2,9	1,5	1,6	0,9	4,2	0,8	2,3	2,0	0,8	0,3	3,8	2,7	1,5	1,6
World (excl. EC)	45,3	38,9	41,0	51,2	64,8	50,9	46,7	53,8	73,3	51,3	31,6	26,2	70,2	58,2	49,9	46,0	79,7	59,2	66,0	51,1
World (incl. EC)	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Table 37

Money supply (M2/M3)

(annual percentage change)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1960	4,0	8,0	11,1	20,2	16,7	5,5	19,6	7,0	2,4	10,7
1961	10,1	9,8	12,9	17,0	17,2	7,3	14,9	5,4	3,2	11,0
1962	7,4	8,5	10,4	21,5	18,7	9,6	17,0	6,6	4,5	11,3
1963	10,9	12,5	9,9	21,4	14,1	5,8	13,5	9,7	7,0	10,8
1964	7,5	11,1	9,4	16,0	9,8	9,4	8,8	10,4	5,6	8,6
1965	8,9	9,7	10,6	12,9	10,9	6,7	15,4	6,2	7,6	10,4
1966	7,9	12,8	8,3	18,2	10,6	10,6	13,8	5,9	3,4	8,6
1967	6,8	9,8	12,0	16,1	13,1	12,7	13,3	10,9	9,3	11,6
1968	8,3	14,5	11,8	17,8	11,6	16,9	11,6	14,8	6,8	10,8
1969	6,8	10,2	9,4	16,2	6,1	11,2	11,4	10,2	2,4	7,6
1970	9,3	3,3	9,1	19,3	15,4	14,0	13,6	11,0	9,5	11,4
1961-70	8,4	10,2	10,4	17,6	12,7	10,4	13,3	9,1	5,9	10,2
1971	13,6	8,5	13,5	22,4	17,8	15,0	17,1	9,0	13,8	14,8
1972	17,2	15,0	14,4	23,6	18,5	14,1	18,3	11,9	24,0	18,1
1973	14,5	12,6	10,1	14,5	15,0	26,1	23,2	21,9	26,4	17,8
1974	11,0	8,9	8,5	20,9	15,9	20,6	15,5	20,0	10,2	12,7
1975	17,1	25,1	8,6	26,5	18,2	18,9	23,5	5,7	6,5	13,6
1976	13,7	10,9	8,4	26,8	12,9	14,4	22,8	22,7	9,5	13,5
1977	9,7	9,9	11,2	22,7	13,9	17,1	23,8	3,6	10,0	13,4
1978	9,7	8,7	11,0	26,0	12,2	28,9	24,2	4,2	15,0	14,2
1979	6,3	10,8	6,0	18,4	14,4	18,7	23,1	6,9	12,7	12,6
1980	2,6	8,1	6,2	24,7	9,8	17,7	17,3	4,4	18,6	11,5
1971-80	11,4	11,7	9,8	22,6	14,8	18,4	20,8	10,8	14,5	14,2
1981	5,9	9,1	5,0	34,7	11,4	17,4	16,0	5,3	13,5	10,8
1982	5,7	11,7	7,1	29,1	10,8	13,0	17,2	7,6	9,3	10,7

Table 38

Short-term interest rates

(%)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1958	:	:	3,6	10,0	6,5	:	3,9	3,0	:	:
1959	:	:	3,2	8,8	4,1	:	3,6	1,9	:	:
1960	:	:	5,1	8,0	4,1	:	3,6	2,1	:	:
1961	4,6	6,3	3,6	8,0	3,7	6,2	3,6	1,1	6,2	4,2
1962	3,4	6,5	3,4	8,0	3,6	5,0	3,6	1,9	5,0	3,9
1963	3,6	6,1	4,0	7,9	4,0	4,3	3,6	2,0	4,3	4,0
1964	4,9	6,2	4,1	7,8	4,7	5,5	3,6	3,5	5,5	4,6
1965	5,0	6,5	5,1	7,8	4,2	6,8	3,6	4,0	6,8	5,0
1966	5,6	6,5	6,6	8,0	4,8	7,0	3,6	4,9	7,0	5,7
1967	5,5	6,6	4,3	8,5	4,8	6,3	3,6	4,7	6,3	4,9
1968	4,5	6,6	3,8	8,3	6,2	7,9	3,6	4,6	7,9	5,3
1969	7,3	8,2	5,8	8,0	9,3	9,2	3,8	5,7	9,2	7,1
1970	8,1	9,0	9,4	8,0	8,6	7,0	5,3	6,2	8,1	8,0
1961-70	5,2	6,8	5,0	8,0	5,3	6,5	3,8	3,8	6,6	5,3
1971	5,4	7,6	7,2	8,0	6,0	6,6	5,7	4,5	6,2	6,3
1972	4,2	7,3	5,6	8,0	5,3	7,0	5,2	2,7	6,8	5,6
1973	6,6	7,6	12,1	9,0	9,3	12,2	7,0	7,5	11,8	9,9
1974	10,6	10,0	9,9	11,8	13,0	14,5	14,9	10,4	13,4	12,2
1975	7,0	8,0	5,0	11,9	7,6	10,9	10,4	5,3	10,6	7,9
1976	10,1	8,9	4,3	11,5	8,7	11,6	16,0	7,4	11,6	9,4
1977	7,3	14,5	4,4	12,0	9,1	8,4	14,0	4,8	8,0	8,3
1978	7,3	15,4	3,7	13,5	7,8	9,8	11,5	7,0	9,4	7,8
1979	10,9	12,5	6,7	16,7	9,7	16,0	12,0	9,6	13,9	10,4
1980	14,2	16,9	9,5	21,0	12,0	16,2	16,9	10,6	16,8	13,4
1971-80	8,3	10,8	6,8	12,3	8,8	11,3	11,3	6,9	10,8	9,1
1981	15,6	14,9	12,4	16,8	15,3	16,7	19,3	11,8	14,1	14,8
1982	14,1	16,4	8,8	18,9	14,6	17,5	19,9	8,2	12,2	13,3

Table 39

Long-term interest rates

(%)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1958	:	:	6,5	:	7,6	5,0	6,7	4,3	5,0	:
1959	:	:	5,8	:	6,3	4,8	5,7	4,1	4,8	:
1960	:	:	6,3	:	5,7	5,4	5,3	4,2	5,4	:
1961	5,9	6,6	5,9	:	5,5	6,2	5,2	3,9	6,3	5,5
1962	5,2	6,6	5,9	:	5,4	6,0	5,8	4,2	5,9	5,5
1963	5,0	6,5	6,1	:	5,3	5,6	6,1	4,2	5,4	5,5
1964	5,6	7,1	6,2	:	5,5	6,0	7,4	4,9	6,0	6,0
1965	6,4	8,6	7,1	6,2	6,2	6,4	6,9	5,2	6,6	6,5
1966	6,7	8,7	8,1	7,4	6,6	6,8	6,5	6,2	6,9	6,9
1967	6,7	9,1	7,0	7,4	6,7	6,7	6,5	6,0	6,8	6,6
1968	6,6	8,7	6,5	7,3	7,0	6,5	6,6	6,2	7,6	6,7
1969	7,3	9,7	6,8	7,1	7,9	7,3	6,7	7,0	9,1	7,5
1970	7,8	11,1	8,3	7,4	8,6	7,8	9,0	7,8	9,3	8,5
1961-70	6,3	8,3	6,8	7,1	6,5	6,5	6,7	5,6	7,0	6,5
1971	7,3	11,0	8,0	7,5	8,4	9,2	8,3	7,0	8,9	8,2
1972	7,0	11,0	7,9	7,8	8,0	9,1	7,5	6,7	9,0	7,9
1973	7,5	12,6	9,3	10,4	9,0	10,7	7,4	7,3	10,8	9,1
1974	8,8	15,9	10,4	9,6	11,0	14,6	9,9	10,7	15,0	11,5
1975	8,5	12,7	8,5	9,0	10,3	14,0	11,5	9,1	14,5	10,8
1976	9,1	14,9	7,8	10,0	10,5	14,6	13,1	9,2	14,6	11,0
1977	8,8	16,2	6,2	9,2	11,0	12,9	14,6	8,5	12,5	10,4
1978	8,5	16,8	5,7	9,3	10,6	12,8	13,7	8,1	12,6	10,1
1979	9,7	16,7	7,4	13,3	10,9	15,1	14,1	9,2	13,0	10,9
1980	12,2	18,7	8,5	18,8	13,7	15,4	16,1	10,7	13,9	12,6
1971-80	8,7	14,6	8,0	10,4	10,3	12,8	11,6	8,6	12,5	10,2
1981	13,8	19,3	10,4	16,3	17,7	17,3	20,6	12,2	14,8	15,0
1982	13,5	20,5	9,0	15,4	16,0	17,0	20,9	10,5	12,7	14,0

Table 40

Gross official reserves

(end year, '000 million ECU)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	EC
1958	1,47	0,22	5,57	0,16	0,99	0,29	2,16	1,48	2,91	15,25
1959	1,24	0,31	4,54	0,21	1,64	0,31	2,95	1,37	2,65	15,22
1960	1,43	0,27	6,66	0,23	2,15	0,31	3,08	1,76	3,52	19,41
1961	1,70	0,26	6,70	0,25	3,15	0,32	3,55	1,83	3,10	20,86
1962	1,64	0,24	6,50	0,27	3,79	0,34	3,80	1,82	3,09	21,49
1963	1,84	0,44	7,15	0,27	4,59	0,38	3,38	1,96	2,94	22,95
1964	2,08	0,60	7,37	0,26	5,35	0,42	3,57	2,19	2,16	24,00
1965	2,18	0,55	6,95	0,23	5,93	0,38	4,49	2,26	2,81	25,78
1966	2,20	0,56	7,51	0,26	6,29	0,46	4,59	2,29	2,90	27,06
1967	2,52	0,52	7,92	0,28	6,80	0,43	5,31	2,55	2,62	28,95
1968	2,33	0,45	10,28	0,33	4,60	0,54	5,58	2,62	2,55	29,28
1969	2,53	0,45	7,49	0,33	4,19	0,68	5,31	2,69	2,66	26,33
1970	2,82	0,48	13,42	0,31	4,95	0,68	5,31	3,22	2,80	33,98
1971	3,25	0,66	17,17	0,48	7,72	0,90	6,38	3,57	8,04	48,18
1972	4,30	0,81	23,73	1,00	10,93	1,03	7,03	5,33	5,51	59,65
1973	6,22	1,20	34,03	1,05	12,15	0,72	8,96	7,50	5,53	77,37
1974	8,61	0,92	40,16	1,08	16,50	0,78	12,02	10,91	6,47	97,46
1975	9,57	0,94	40,49	1,17	21,19	0,95	12,31	11,80	5,63	104,05
1976	8,34	0,95	43,90	1,09	16,12	0,90	10,81	11,13	4,01	97,25
1977	8,64	1,53	50,61	1,15	17,07	1,08	13,97	12,18	13,24	119,47
1978	8,18	2,55	52,84	1,25	21,03	2,00	19,70	11,11	13,90	132,57
1979	10,41	2,59	57,59	1,47	29,44	1,62	26,69	14,52	17,39	161,72
1980	20,54	3,28	76,56	2,49	57,10	2,25	45,94	27,50	23,69	259,34
1981	18,28	3,01	79,81	2,19	52,52	2,59	45,48	26,26	22,13	252,28
1982	16,24	2,94	82,14	2,31	46,30	2,84	39,02	26,52	19,71	238,01

Table 41

ECU exchange rates

(national units per ECU, annual average)

	BLEU	DK	D	GR	F	IRL	I	NL	UK	USA
1958	54,8350	7,57507	4,60614	32,9010	4,61264	0,391678	685,438	4,16745	0,391678	1,09670
1959	52,8101	7,29535	4,43605	31,6863	5,21454	0,377215	660,126	4,01357	0,377215	1,05621
1960	52,8101	7,29535	4,43605	31,6863	5,21454	0,377215	660,126	4,01357	0,377215	1,05621
1961	53,3667	7,37224	4,30742	32,0202	5,26950	0,381191	667,084	3,89854	0,381191	1,06734
1962	53,4901	7,38928	4,27921	32,0943	5,28168	0,382073	668,626	3,87268	0,382073	1,06981
1963	53,4901	7,38928	4,27921	32,0943	5,28168	0,382073	668,626	3,87268	0,382073	1,06981
1964	53,4901	7,38928	4,27921	32,0943	5,28168	0,382073	668,626	3,87268	0,382073	1,06981
1965	53,4901	7,38928	4,27921	32,0943	5,28168	0,382073	668,626	3,87268	0,382073	1,06981
1966	53,4901	7,38928	4,27921	32,0943	5,28168	0,382073	668,626	3,87268	0,382073	1,06981
1967	53,2404	7,42293	4,25924	31,9446	5,25703	0,387652	665,506	3,85461	0,387652	1,06482
1968	51,4442	7,71663	4,11554	30,8667	5,07967	0,428702	643,052	3,72456	0,428702	1,02889
1969	51,1093	7,66640	4,02622	30,6657	5,29027	0,425912	638,866	3,70032	0,425912	1,02219
1970	51,1116	7,66675	3,74138	30,6668	5,67767	0,425931	638,895	3,70049	0,425931	1,02223
1971	50,8663	7,75264	3,64566	31,4328	5,77214	0,428583	647,414	3,65750	0,428583	1,04776
1972	49,3611	7,78909	3,57681	33,6533	5,65717	0,448941	654,264	3,59991	0,448941	1,12178
1973	47,8009	7,41598	3,27644	36,9519	5,46775	0,502321	716,460	3,42853	0,502321	1,23173
1974	46,3994	7,25927	3,08352	35,7810	5,73386	0,509803	775,743	3,20224	0,509803	1,19270
1975	45,5690	7,12266	3,04939	39,9941	5,31923	0,560026	809,545	3,13490	0,560026	1,24077
1976	43,1654	6,76176	2,81545	40,8842	5,34486	0,621578	930,150	2,95515	0,621578	1,11805
1977	40,8826	6,85567	2,64831	42,0353	5,60607	0,653701	1 006,785	2,80010	0,653701	1,14112
1978	40,0611	7,01945	2,55607	46,7829	5,73983	0,663888	1 080,216	2,75409	0,663910	1,27410
1979	40,1651	7,20911	2,51087	50,7738	5,82945	0,669482	1 138,498	2,74864	0,646392	1,37065
1980	40,5979	7,82736	2,52421	59,3228	5,86895	0,675997	1 189,205	2,76027	0,598488	1,39233
1981	41,2946	7,92255	2,51390	61,6241	6,03992	0,691021	1 263,180	2,77510	0,553110	1,11645
1982	44,6988	8,15186	2,37541	65,3556	6,42534	0,690985	1 321,987	2,61232	0,563644	0,98208
(1983)	45,2484	8,13446	2,26873	77,6485	6,75035	0,716749	1 348,751	2,53684	0,592504	0,88979

Table 42

Central rates against the ECU

(national currency per ECU)

Date	BLEU	DK	D	GR [1]	F	IRL	I	NL	UK [1]
13. 3.1979	39,4582	7,08592	2,51064	:	5,79831	0,662638	1 148,15	2,72077	(0,663247)
24. 9.1979	39,8456	7,36594	2,48557	:	5,85522	0,669141	1 159,42	2,74748	(0,649821)
30.11.1979	39,7897	7,72336	2,48208	:	5,84700	0,668201	1 157,79	2,74362	(0,648910)
23. 3.1981	40,7985	7,91917	2,54502	:	5,99526	0,685145	1 262,92	2,81318	(0,542122)
5.10.1981	40,7572	7,91117	2,40989	:	6,17443	0,684452	1 300,67	2,66382	(0,601048)
22. 2.1982	44,6963	8,18382	2,41815	:	6,19564	0,686799	1 305,13	2,67296	(0,557037)
14. 6.1982	44,9704	8,2340	2,33379	:	6,61387	0,691911	1 350,27	2,57971	(0,560453)
21. 3.1983	44,3662	8,04412	2,21515	:	6,79271	0,717050	1 386,78	2,49587	(0,629848)
18. 5.1983	44,9008	8,14104	2,24184	:	6,87456	0,725690	1 403,49	2,52595	(0,587087)

[1] The drachma has not been integrated into the ECU; the pound sterling is represented in the ECU, but does not participate in the EMS exchange rate mechanism.

Table 43

Bilateral central rates since 20 March 1983

		BFR/LFR (Bruxelles)	DKR (København)	DM (Frankfurt)	FF (Paris)	IRL (Dublin)	LIT (Roma)	HFL (Amsterdam)	UKL [1] (London)
BFR/LFR 100	± 2,25	100	18,1312	4,99288	15,3106	1,61621	3 125,76	5,62561	—
DKR 100	± 2,25	551,536	100	27,5375	84,4432	8,91396	17 239,7	31,0273	—
DM 100	± 2,25	2 002,85	363,141	100	306,648	32,3703	62 604,3	112,673	—
FF 100	± 2,25	653,144	118,423	32,6107	100	10,5562	20 415,7	36,7434	—
IRL 1	± 2,25	61,8732	11,2184	3,08925	9,47313	1	1 934,01	3,48075	—
LIT 1 000	± 6,00	31,9922	5,80057	1,59733	4,89819	0,517061	1 000	1,79976	—
HFL 100	± 2,25	1 777,58	322,297	88,7526	272,158	28,7295	55 563,0	100	—
(UKL 1)	—	—	—	—	—	—	—	—	1

[1] The pound sterling does not participate in the EMS exchange rate mechanism.

Table 44

Effective exchange rates

(1972 = 100)

	B/L	DK	D	GR	F	IRL	I	NL	UK	EC 9
1960	96,7	106,6	79,3	107,4	111,9	109,4	101,1	92,0	120,3	99,3
1961	95,5	105,6	82,2	106,8	111,1	109,2	100,4	95,0	119,7	100,6
1962	95,6	105,6	82,6	106,8	111,1	109,5	100,4	95,7	120,1	101,0
1963	95,3	105,7	82,9	106,8	111,4	109,4	100,3	95,8	119,9	101,1
1964	95,6	105,5	83,2	106,9	111,2	109,3	99,8	95,6	119,5	101,1
1965	95,9	105,6	82,7	106,9	111,3	109,4	99,8	95,9	119,7	101,1
1966	95,7	105,7	82,7	107,0	111,9	109,3	99,9	95,4	119,6	101,2
1967	96,0	105,1	83,3	107,3	111,2	108,6	100,3	96,2	117,9	101,0
1968	97,0	101,4	84,8	109,3	113,1	102,0	102,5	97,9	103,9	98,8
1969	97,2	101,0	87,0	109,7	107,5	102,1	102,2	98,1	104,0	98,1
1970	97,3	100,2	94,4	108,9	99,5	101,8	101,3	97,1	103,6	97,9
1971	97,2	99,3	97,3	106,7	97,4	102,0	100,5	98,2	103,7	98,7
1972	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0
1973	101,4	106,1	110,2	92,9	104,1	93,5	90,5	104,2	89,7	101,8
1974	102,8	106,5	116,5	93,4	97,4	91,1	81,5	110,0	86,4	99,1
1975	104,3	110,2	118,4	84,1	107,1	86,2	78,4	113,0	79,7	101,5
1976	106,8	112,7	125,3	80,1	103,4	77,5	64,8	116,4	68,0	92,9
1977	112,9	112,2	135,5	78,2	99,0	74,8	59,9	123,3	64,7	93,8
1978	116,2	112,1	143,5	71,4	98,0	75,3	56,2	126,8	65,0	96,5
1979	117,6	111,2	150,4	67,5	98,9	75,5	54,4	129,1	69,0	102,2
1980	117,0	102,5	151,0	58,4	99,3	73,9	52,4	129,2	75,9	104,4
1981	110,7	95,5	143,2	52,9	90,7	67,8	46,0	122,8	76,8	88,8
1982	100,5	91,6	150,4	49,1	83,4	67,1	42,9	129,5	73,2	84,2
(1983)	98,6	91,7	157,1	40,7	78,3	64,8	41,5	132,7	68,1	80,2

Table 45

Current receipts of general government (taxation, social security contributions and other)

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	25,7	27,7	35,9	19,4	35,8	25,5	28,3	32,6	33,0	32,2	32,9
1959	26,2	28,0	36,4	19,7	36,6	25,8	29,1	31,2	33,3	32,0	33,2
1960	27,6	28,1	35,2	20,0	35,5	25,4	29,1	32,3	34,0	31,6	32,7
1961	28,6	27,4	36,3	22,0	36,7	26,3	28,4	33,0	35,0	32,6	33,6
1962	29,4	28,7	36,6	23,2	36,9	25,7	29,3	33,0	34,5	34,2	34,3
1963	29,5	30,4	36,9	23,2	37,7	26,7	29,8	32,9	35,7	32,8	34,3
1964	30,2	30,3	36,5	24,0	38,7	27,5	30,8	33,0	35,8	32,7	34,6
1965	30,9	31,7	35,8	23,7	39,1	28,6	30,4	34,6	37,4	34,4	35,0
1966	32,7	33,9	36,3	25,3	39,1	30,6	30,4	35,3	39,3	35,5	35,6
1967	33,4	34,3	36,8	26,2	39,0	31,3	31,3	35,1	40,7	37,5	36,4
1968	34,0	36,8	36,7	27,3	39,5	31,7	31,8	39,0	41,9	38,9	37,1
1969	34,5	37,1	38,7	27,2	40,6	32,3	30,9	38,6	42,7	40,9	38,1
1970	35,4	46,1	37,9	26,8	39,8	36,1	30,6	36,3	43,9	42,0	38,2
1961-70	31,9	33,7	36,9	24,9	38,7	29,7	30,4	35,1	38,7	36,2	35,7
1971	35,9	48,1	38,8	26,6	39,1	36,7	31,3	39,0	46,1	39,6	38,2
1972	35,8	48,3	39,2	26,6	39,0	35,4	31,1	39,8	47,2	38,3	38,1
1973	36,6	48,6	41,7	25,4	39,4	35,1	30,6	39,5	48,9	37,8	39,1
1974	37,9	50,3	42,0	27,0	40,3	36,1	30,8	41,0	49,5	41,6	40,2
1975	40,7	47,5	41,3	27,4	41,3	36,2	31,6	50,2	51,9	42,7	40,8
1976	40,5	46,9	42,8	29,5	43,7	39,4	33,3	51,0	52,2	41,8	42,0
1977	42,0	47,6	44,1	29,9	43,7	38,9	34,3	55,0	53,0	41,8	42,7
1978	43,0	49,7	43,9	30,2	43,3	36,0	36,2	55,9	53,7	38,4	42,4
1979	44,7	51,2	43,3	30,6	44,7	38,7	36,2	53,5	56,1	39,0	42,8
1980	44,8	52,5	43,5	30,2	46,6	42,0	37,8	55,7	54,2	40,7	43,6
1971-80	40,2	49,1	42,1	28,3	42,1	37,5	33,3	48,1	51,3	40,2	41,0
1981	45,2	51,9	45,5	30,1	47,3	41,4	39,5	54,6	53,8	42,4	44,6
1982	47,0	51,2	46,0	33,5	47,9	43,7	41,8	56,9	54,6	43,5	45,7
(1983)	46,7	52,4	46,1	35,7	48,9	45,7	44,7	58,4	56,8	43,0	46,6

Table 46

Expenditure of general government

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	27,9	26,3	34,3	22,0	34,9	27,3	29,7	33,5	34,7	31,7	32,5
1959	29,6	25,7	34,3	23,5	35,4	26,6	30,6	34,6	32,8	31,9	32,7
1960	30,5	25,5	32,0	23,8	34,6	26,7	29,9	29,3	33,2	32,6	32,1
1961	29,9	28,1	33,4	24,2	35,7	28,4	29,1	28,5	34,9	33,3	32,9
1962	30,6	29,1	35,2	25,7	37,0	28,3	30,2	30,8	35,1	34,2	34,2
1963	31,5	29,1	35,9	24,1	37,8	29,4	30,8	31,4	37,1	35,6	35,0
1964	30,8	29,4	35,7	27,7	38,0	30,7	31,5	30,9	37,3	33,8	34,8
1965	32,2	30,3	36,3	27,5	38,4	31,9	34,0	31,8	38,2	36,3	36,1
1966	33,5	32,3	36,5	27,6	38,5	32,4	34,0	34,0	40,2	35,6	36,1
1967	34,6	34,9	38,2	29,8	39,0	33,5	33,3	35,7	42,0	38,5	37,5
1968	36,2	36,9	37,6	29,2	40,3	33,9	34,4	41,4	42,8	39,7	38,2
1969	36,1	36,8	37,6	29,5	39,6	35,4	33,8	38,0	43,2	41,6	38,3
1970	36,5	43,1	37,6	29,1	38,9	40,1	33,4	33,4	44,7	39,4	37,9
1961-70	33,2	33,0	36,4	27,4	38,3	32,4	32,5	33,6	39,6	36,8	36,1
1971	38,1	44,5	38,9	30,6	38,3	40,5	35,8	36,6	46,6	38,5	38,6
1972	39,1	43,7	39,7	30,5	38,3	39,0	37,6	37,6	47,2	40,1	39,5
1973	39,4	42,7	40,5	28,9	38,5	39,2	36,5	36,0	47,8	41,2	39,8
1974	39,7	48,5	43,4	31,7	39,7	43,7	36,2	36,0	49,6	45,7	42,1
1975	44,7	49,5	47,1	32,5	43,5	47,8	44,9	49,0	54,6	47,7	46,2
1976	45,3	47,7	46,4	33,0	44,2	47,5	42,3	49,4	54,5	46,8	45,7
1977	47,0	49,3	46,7	34,0	44,9	46,4	43,3	52,9	54,6	45,3	46,0
1978	48,4	52,0	46,7	35,3	45,6	46,5	46,7	52,6	55,8	42,4	46,4
1979	51,6	54,3	46,3	35,2	45,5	50,5	45,6	53,4	58,1	42,3	46,4
1980	53,9	58,6	46,9	29,8	46,2	55,2	45,6	57,0	57,9	44,3	47,1
1971-80	44,7	49,1	44,3	32,2	42,5	45,6	41,5	46,1	52,7	43,4	43,8
1981	57,9	58,9	49,3	40,2	49,1	57,2	51,2	56,9	59,0	45,3	49,9
1982	58,9	60,3	49,5	39,9	50,6	59,9	53,7	58,9	61,5	45,6	50,9
(1983)	58,9	61,2	49,4	42,0	52,0	59,1	56,6	61,3	63,6	45,1	52,0

Table 47

Net lending or net borrowing of general government

(as % of GDP)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EC
1958	−2,2	1,4	1,6	−2,6	0,9	−0,8	−1,3	−0,9	−1,6	0,5	0,4
1959	−3,4	2,3	2,1	−3,8	1,2	−0,7	−1,5	−3,4	0,5	0,1	0,5
1960	−2,9	2,6	3,1	−3,7	0,9	−1,3	−0,8	3,0	0,8	−1,0	0,6
1961	−1,3	−0,7	2,9	−2,2	1,0	−2,1	−0,7	4,5	0,1	−0,7	0,6
1962	−1,2	−0,4	1,5	−2,5	−0,1	−2,6	−0,9	2,2	−0,6	−0,0	0,1
1963	−2,0	1,3	1,0	−0,8	−0,1	−2,6	−1,0	2,5	−1,3	−2,8	−0,7
1964	−0,6	0,9	0,7	−3,7	0,7	−3,2	−0,7	2,1	−1,5	−1,1	−0,1
1965	−1,4	1,5	−0,6	−3,8	0,7	−3,3	−3,6	2,8	−0,8	−2,0	−1,1
1966	−0,8	1,6	−0,2	−2,4	0,6	−1,8	−3,6	1,3	−0,9	−0,0	−0,5
1967	−1,2	−0,6	−1,4	−3,6	0,0	−2,2	−2,0	−0,7	−1,3	−1,0	−1,1
1968	−2,2	−0,1	−0,8	−1,9	−0,8	−2,3	−2,6	−2,4	−0,9	−0,8	−1,2
1969	−1,6	0,3	1,1	−2,3	0,9	−3,1	−2,9	0,6	−0,5	−0,7	−0,2
1970	−1,1	3,0	0,3	−2,3	0,9	−4,0	−2,8	2,9	−0,8	2,6	0,3
1961-70	−1,3	0,7	0,5	−2,6	0,4	−2,7	−2,3	1,6	−0,9	−0,7	−0,4
1971	−2,1	3,6	−0,2	−4,0	0,7	−3,8	−4,6	2,4	−0,5	1,2	−0,5
1972	−3,3	4,6	−0,5	−3,8	0,8	−3,5	−6,5	2,2	−0,0	−1,9	−1,4
1973	−2,7	5,9	1,2	−3,5	0,9	−4,1	−5,8	3,5	1,1	−3,4	−0,8
1974	−1,8	1,8	−1,4	−4,7	0,6	−7,5	−5,4	5,1	−0,1	−4,1	−1,9
1975	−4,1	−2,0	−5,8	−5,1	−2,2	−11,6	−13,3	1,2	−2,7	−5,0	−5,5
1976	−4,8	−0,8	−3,6	−3,6	−0,5	−8,1	−9,0	1,6	−2,4	−5,0	−3,7
1977	−4,9	−1,7	−2,6	−4,2	−1,3	−7,6	−9,0	2,1	−1,5	−3,4	−3,3
1978	−5,5	−2,2	−2,8	−5,1	−2,3	−10,4	−10,5	3,3	−2,1	−4,0	−4,0
1979	−6,9	−3,1	−3,0	−4,6	−0,8	−11,9	−9,4	0,1	−2,0	−3,3	−3,6
1980	−9,4	−5,9	−3,5	0,4	0,0	−12,8	−8,4	−1,8	−3,4	−3,5	−3,5
1971-80	−4,6	0,0	−2,2	−3,9	−0,1	−8,1	−8,0	2,0	−1,4	−3,2	−2,8
1981	−12,6	−7,0	−3,9	−10,1	−1,8	−15,8	−11,7	−2,3	−5,2	−2,9	−5,2
1982	−11,9	−9,1	−3,5	−6,4	−2,7	−16,2	−11,9	−2,0	−6,9	−2,1	−5,2
(1983)	−12,2	−8,8	−3,3	−6,3	−3,1	−13,4	−11,9	−2,9	−6,7	−2,2	−5,4

Table 48

Budgetary expenditure of the European Communities (a)

(million ua/EUA/ECU)

	ECSC operational budget	European Development Fund	Euratom (b)	EC general budget						Total
				EAGGF (c)	Social Fund	Regional Fund	Industry Energy Research	Adm. and others (d)	Total EC	
1958	21,7	—	7,9	—	—	—	—	5,9	5,9	35,5
1959	30,7	51,2	39,1	—	—	—	—	25,2	25,2	146,2
1960	23,5	63,2	20,0	—	—	—	—	28,3	28,3	135,0
1961	26,5	172,0	72,5	—	8,6	—	—	25,4	34,0	305,0
1962	13,6	162,3	88,6	—	11,3	—	—	81,0	92,3	356,8
1963	21,9	55,5	106,4	—	4,6	—	—	79,5	84,1	267,9
1964	18,7	35,0	124,4	—	7,2	—	—	85,9	93,1	271,1
1965	37,3	248,8	120,0	102,7	42,9	—	—	55,5	201,1	607,2
1966	28,1	157,8	129,2	310,3	26,2	—	—	65,8	402,2	717,3
1967	10,4	105,8	158,5	562,0	35,6	—	—	77,5	675,1	949,8
1968	21,2	121,0	73,4	2 250,4	43,0	—	—	115,3	2 408,6	2 624,2
1969	40,7	104,8	59,2	3 818,0	50,5	—	—	182,7	4 051,2	4 255,9
1970	56,2	10,5	63,4	5 228,3	64,0	—	—	156,1	5 448,4	5 578,5
1971	37,4	236,1	—	1 883,6	56,5	—	65,0	284,3	2 289,3	2 562,8
1972	43,7	212,7	—	2 477,6	97,5	—	75,1	424,3	3 074,5	3 330,9
1973	86,9	210,0	—	3 768,8	269,2	—	69,1	533,8	4 641,0	4 937,9
1974	92,0	157,0	—	3 651,3	292,1	—	82,8	1 011,9	5 038,2	5 287,2
1975	127,4	71,0	—	4 586,6	360,2	150,0	99,0	1 017,8	6 213,6	6 412,0
1976	94,0	320,0	—	6 033,3	176,7	300,0	113,3	1 329,2	7 952,6	8 366,6
1977 (e)	93,0	800,0	—	6 667,6	55,3	400,0	167,0	1 303,9	8 483,2	9 376,2
1978	159,1	394,5	—	9 552,3	256,5	254,9	266,8	1 430,8	11 884,2	12 190,8
1979	173,9	480,0	—	10 765,0	527,0	499,0	288,0	2 368,0	14 602,5	15 256,4
1980	175,7	508,5	—	11 596,1	502,0	751,8	212,8	2 994,9 (f)	16 057,5	16 741,7
1981	261,0	658,0	—	11 443,0	547,0	547,0	232,0	4 060,0	18 546,0 (g)	19 465,0
1982	243,0	750,0	—	12 792,0	910,0	2 766,0 (h)	346,0	4 613,0	21 427,0 (i)	22 420,0
1983	:	:	—	16 611,0	1 497,0	2 432,0	1 454,0	3 282,0	25 276,0 (j)	:
1984	:	:	—	16 992,0	1 446,0	1 335,0	1 307,0	3 768,0	24 848,0 (k)	:

Table 49

Budgetary receipts of the European Communities (a)

(million ua/EUA/ECU)

	ECSC levies and other	European Dev. Fund contributions	Euratom contributions (research only)	EC budget					Total
				Miscellan. and contributions under special keys	Own resources			Total EC	
					Miscellaneous	Agricultural levies	Import duties	GNP contributions or VAT (b) (c)		
1958	44,0	116,0	7,9	0,02	—	—	—	5,9	5,9	173,8
1959	49,6	116,0	39,1	0,1	—	—	—	25,1	25,2	229,9
1960	53,3	116,0	20,0	0,2	—	—	—	28,1	28,3	217,6
1961	53,1	116,0	72,5	2,8	—	—	—	31,2	34,0	275,6
1962	45,3	116,0	88,6	2,1	—	—	—	90,2	92,3	342,2
1963	47,1	—	106,4	6,7	—	—	—	77,4	84,1	237,5
1964	61,3	—	124,4	2,9	—	—	—	90,1	93,1	278,7
1965	66,1	—	98,8	3,5	—	—	—	197,6	201,1	366,0
1966	71,2	—	116,5	3,9	—	—	—	398,3	402,2	590,0
1967	40,3	40,0	158,5	4,2	—	—	—	670,9	675,1	913,9
1968	85,4	90,0	82,0	—	—	—	—	—	2 408,6	2 666,0
1969	106,8	110,0	62,7	78,6	—	—	—	3 972,6	4 051,2	4 330,7
1970	100,0	130,0	67,7	121,1	—	—	—	5 327,3	5 448,4	5 746,1
1971	57,9	170,0	—	—	69,5	713,8	582,2	923,8	2 289,3	2 517,2
1972	61,1	170,0	—	—	80,9	799,6	957,4	1 236,6	3 074,5	3 305,6
1973	120,3	150,0	—	—	511,0	478,0	1 564,7	2 087,3	4 641,0	4 911,3
1974	124,6	150,0	—	—	65,3	323,6	2 684,4	1 964,8	5 038,2	5 312,8
1975	189,5	220,0	—	—	320,5	590,0	3 151,0	2 152,0	6 213,6	6 623,1
1976 (d)	129,6	311,0	—	—	282,8	1 163,7	4 064,6	2 482,1	7 993,1	8 433,7
1977	123,0	410,0	—	—	283,0	1 778,5	3 927,2	2 494,5	8 483,2	9 016,2
1978	164,9	147,5	—	—	217,2	2 283,3	4 407,9	4 975,8	11 884,2	12 196,6
1979	168,4	480,0	—	—	230,3	2 143,4	5 189,1	7 039,8	14 602,5	15 251,0
1980	226,2	555,0	—	—	1 055,9 (e)	2 002,3	5 905,8	7 093,5	16 057,5 (f)	16 838,7
1981	264,0	658,0	—	—	1 219,0	1 747,0	6 392,0	9 188,0	18 546,0 (g)	19 468,0
1982	243,0	750,0	—	—	187,0	2 228,0	6 815,0	12 197,0	21 427,0	22 420,0
1983	:	:	—	—	1 294,0	2 461,0	7 574,0	13 947,0	25 276,0 (h)	:
1984	:	:	—	—	222,0	2 950,0	7 623,0	14 053,0	24 848,0 (i)	:

Table 50

Borrowing operations of the European Communities and of the European Investment Bank

(million ua/EUA/ECU)

	ECSC	EIB	Euratom	EEC(b)	EEC-NCI(c)	Total
1958	50	—	—	—	—	50
1959	—	—	—	—	—	—
1960	35	—	—	—	—	35
1961	23	21	—	—	—	44
1962	70	32	—	—	—	102
1963	33	35	5(d)	—	—	73
1964	128	67	8(d)	—	—	203
1965	54	65	11(d)	—	—	130
1966	103	139	14(d)	—	—	256
1967	58	195	3(d)	—	—	256
1968	108	213	—	—	—	321
1969	52	146	—	—	—	198
1970	60	169	—	—	—	229
1971	102	413	1(d)	—	—	516
1972	230	462	—	—	—	692
1973	263	608	—	—	—	871
1974	528	826	—	—	—	1 354
1975	731	814	—	—	—	1 545
1976	956	732	—	1 249	—	2 937
1977	729	1 030	99	571	—	2 429
1978	981	1 863	72	—	—	2 916
1979	837	2 437	153	—	178	3 605
1980	1 004	2 384	181	—	305	3 874
1981	325	2 243	373	—	339	3 280
1982	712	3 146	363	—	773	4 994

Table 51

Net outstanding borrowing of the European Communities and of the European Investment Bank

(million ua/EUA/ECU) (a)

	ECSC	EIB	Euratom	EEC(b)	EEC-NCI(c)	Total
1958	212	—	—	—	—	212
1959	209	—	—	—	—	209
1960	236	—	—	—	—	236
1961	248	21	—	—	—	269
1962	304	54	—	—	—	358
1963	322	88	—	—	—	410
1964	436	154	—	—	—	590
1965	475	217	—	—	—	692
1966	560	355	—	—	—	915
1967	601	548	—	—	—	1 149
1968	686	737	—	—	—	1 423
1969	719	883	—	—	—	1 602
1970	741	1 020	—	—	—	1 761
1971	802	1 423	—	—	—	2 225
1972	963	1 784	—	—	—	2 747
1973	1 157	2 287	—	—	—	3 444
1974	1 615	3 124	—	—	—	4 739
1975	2 391	3 926	—	—	—	6 317
1976	3 478	4 732	—	1 161	—	9 371
1977	3 955	5 421	99	1 500	—	10 975
1978	4 416	6 715	172	1 361	—	12 664
1979	4 675	8 541	323	965	178	14 682
1980	5 406	10 604	502	1 016	402	18 019
1981	5 884	13 482	902	1 062	894	22 224
1982	6 178	16 570	1 272	591	1 747	26 358

Notes on the tables

Tables 1 and 2:

Source: Eurostat, National Accounts 1972 (Greece (1958-60) OECD National Accounts) and National Accounts ESA 1982 (Cronos data bank, SEC 1).

Table 3:

Source: Eurostat, Cronos data bank (SOEC definition).

Tables 4 to 8:

Source: As for Tables 1 and 2.

Table 8:

Coverage: Not including construction.
Source: Eurostat, Cronos data bank.

Tables 10 to 23:

Sources: As for Tables 1 and 2.

Table 22:

Source: As for Tables 1 and 2.

Table 23

Definition: Compensation per employee deflated by the price index of private consumption.
Source: Commission departments.

Table 24

Definition: Compensation of employees adjusted for the share of self-employed in total employment, as per cent of GDP at factor cost.

Table 25

Source: For a detailed commentary on the method used see *European Economy* No 8, March 1981.

Tables 28 and 29:

Source: Eurostat, Foreign Trade (monthly bulletin), special number July 1981, and National Accounts as for Tables 1 and 2.

Tables 30 and 31:

Source: As for Tables 1 and 2.

Tables 32 and 33:

Source: As for Tables 28 and 29.

Table 34:

Definition: Net lending or borrowing of the nation minus net capital transfers to the rest of the world.
Source: As for Tables 1 and 2.

Tables 35 and 36:

Source: As for Tables 28 and 29.

Table 37:

Definitions: B: up to 1964, monetary claims on the main monetary institutions; from 1965, M2H. DK: up to 1975, M2; from 1976, M2H. D: M3. GR: M3. F: up to 1981, total M2; from 1982 residents M2. IRL: M3. I: up to 1975, M2; from 1976, M3. NL: M2. UK: sterling M3. EC: rate of growth of the geometrical average, weighted by GDP at current prices and purchasing power parities, of the money stock indices of the countries (1975 = 100). The weight of Luxembourg has been added to the weight of Belgium.

Table 38:

Definitions: DK: Discount rate until 1976, day-to-day rate since 1977. D: 3-month inter-bank rate. GR: Interest rates on credit for working capital to industry until 1980; from 1981, rate on inter-bank sight deposits. F: Day-to-day rate until 1968, 1-month commercial paper rate since 1969. IRL: Up to 1970: 3-month inter-bank loans in London; from 1971: 3-month inter-bank loans in Dublin. I: 12-month Treasury bill rate until 1970, inter-bank rate since 1971. NL: Treasury bill 3-months up to 1972; inter-bank loans 3-months from 1973. B: Rate on 4-month certificates of Fonds des Routes. UK: 3-month Treasury bill rate until September 1964, 3-month inter-bank rate since October 1964. EC: Weighted average with GDP at purchasing power parity 1975.

Table 39:

Definitions: DK: Yield on first-class mortgage loans. D: Average yield on all public sector bonds. GR: Weighted average yield of government bonds. F: Yield on public sector bonds. IRL: Up to 1970: yield on government securities with maturity 20 years in London. From 1971: yield on government securities with maturity 15 years in Dublin. I: Yield on Crediop public bonds. NL: OECD, yield of government bonds 3,25% up to 1973. Private loan to public utilities from 1974. B: Yield on 5-year government bonds. UK: Yield on 20-year government securities. EC: Weighted average with GDP at purchasing power parity 1975, up to 1964 without Greece.

Table 40:

Source: IMF International Financial Statistics and Commission departments. Gold is valued at market related prices.

Tables 41 and 44:

Source: Commission departments; for 1982 average to September 1982.

Tables 45 to 47:

Sources: Member countries' national accounts and OECD National Accounts.

Table 48:

Source: 1958-81: Management accounts. (a) u.a. until 1977. EUA/ECU 1978 onwards. (b) Incorporated in the EC budget from 1971. (c) This column includes, for the years to 1970, substantial amounts carried forward to following years. (d) Including the European Parliament, the Council, the Court of Justice, the Court of Auditors and the administrative part of the ECSC budget. (e) In 1977 appropriations for the Social Fund carried forward from 1976 and subsequently cancelled amounted to 227 716 611 u.a., while total expenditure for 1977 amounted to only 172 439 999 u.a. giving the net figure shown here. (f) Including surplus of 82,4 million ECU carried forward to 1981. (g) Including 1 173 million ECU carried forward to 1982. (h) Including 1 819 million ECU UK special measures. (i) Including 2 211 million ECU carried forward to 1983. (j) Preliminary draft supplementary budget No 2/1983. (k) Draft budget established by the Council 22 July 1983.

Table 49:

Source: 1958-81: Management accounts. (a) u.a. until 1977, EUA/ECU 1978 onwards. (b) GNP until 1978, VAT from 1979 onward. (c) This column includes for the years to 1970 surplus revenue from previous years carried forward to following years. (d) As a result of the calculations to establish the relative shares of the Member States in the 1976 budget, an excess of revenue over expenditure occurred amounting to 40 543 573 u.a. This

was carried forward to 1977. (c) Including surplus brought forward from 1979 and balance of 1979 VAT and financial contributions. (f) Including surplus of 82,4 million ECU carried forward to 1981. (g) Including surplus of 661 million ECU. (h) Preliminary draft supplementary budget No 2/1983. (i) Draft budget established by the Council 22 July 1983.

Tables 50 and 51:

Source: European Economy No 6; 'Borrowing and lending instruments looked at in the context of the Community's financial instruments', No 8, 'The Community's borrowing and lending operations: recent developments affecting certain instruments', and No 13, September 1982, 'The borrowing and lending activities of the Community'. (a) ECSC: 1958-74, u.a.; 1975-82, EUA/ECU. EIB: 1961-73, u.a.; 1974-82, EUA/ECU. Euratom: 1963-71 u.a.; 1977-82, EUA/ECU. (b) EEC balance of payments financing. (c) EEC New Community Instrument (for investment). (d) Drawings under credit lines opened with Eximbank (USA).

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