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Supplement A – No 3 – March 1989

In this number: The March Communication from the Commission to the Council[1]

Recent economic trends

On 22 February 1989, the Commission of the European Communities adopted its yearly March Communication to the Council concerning the current economic situation. The complete text is as follows.

SAFEGUARDING THE CONDITIONS FOR A SUCCESSFUL 1992

The economic outlook and policy problems for 1989 and 1990

Communication from the Commission to the Council conforming to the convergence decision of 18.2.1974 (74/120/EEC)

SUMMARY

This Communication updates the Annual Economic Report adopted by the Commission last October. As required by the Convergence Decision of 1974, it discusses whether the policy guidelines laid down in the October Report are still valid in the light of the current economic situation and outlook.

The document takes as a starting point the results of the most recent round of economic forecasts produced by the Commission's services which include the year 1990 for the first time.

The completion of the internal market, the strengthening of the economic and social cohesion of the Community and the progressive reduction of unemployment are all objectives requiring a prolonged and determined effort. The analysis therefore focuses on Community-wide trends and puts them into a perspective going beyond the short-term.

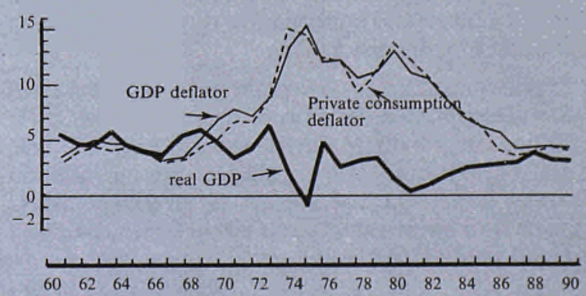
1. 1988 has been a very good year for the economy of the Community as it was for the world economy. The outlook for 1989 and 1990 is also favourable. The policies implemented over the last years are bearing fruit and the Community seems to have increased its trend rate of growth from 2 ½ to 3 %. The very good investment and employment performance is expected to continue. Growth is now more employment-creating than ever: on present trends job creation will accomodate a significant increase of the labour force and bring unemployment well below 10 % in 1992 .

[1] The Communication is based on forecasts established by the Commission services on 26 January 1989 and published in Supplement A, No 2 of February 1989.

CHART 1: **GDP and employment growth in the Community, annual percentage growth rate**

[1] Forecasts.
Source: Commission services.

CHART 2: **Real GDP and inflation in the Community, annual percentage changes**



1989-90: Forecasts.
Source: Commission services.

Against this positive background and the perspectives opened up by the completion of the internal market, the achievement of a sustained medium-term growth trend of around 3 ½ % a year appears within reach. This would be in line with the path outlined in the 'Cooperative Growth Strategy' and would open up the possibility of reducing unemployment significantly.

2. The present economic situation owes much to the favourable prospects created by the completion of the internal market. In the second half of the 1980s, given the need to re-equilibrate the international imbalances, the Community had to rely on its own economy to regain dynamism. The 1992 project was therefore 'the right idea at the right time'. The expectations thus created must not be disappointed and the momentum must be maintained.

At the same time, the policies aimed at further strengthening the conditions for growth presented in the *Annual Economic Report for 1988/89* must continue to be implemented. These policies are necessary to maintain the strong investment and employment performances and a healthy rate of growth. A buoyant economy will facilitate budgetary consolidation and the structural adjustment needed to reap the benefits of the completion of the internal market. Strong growth in the Community also helps the cohesion process as well as the reduction of unemployment.

3. Although the economic outlook for the Community is basically favourable, disequilibria and uncertainties are building up at the macroeconomic level. Three possible sources can be identified.

(a) The current account gap between surplus and deficit countries is increasing.

(b) Public debt/GDP ratios are still growing and fiscal deficits are not being reduced sufficiently in those countries where they are particularly high.

(c) Disinflation has stopped throughout the Community; in a number of countries inflation is actually increasing and even in countries where price pressure is, statistically, still low there are signs of inflationary expectations building up.

Authorities must act to correct these growing imbalances at an early stage. The credibility they have built up in the successful twin process of the 1980s - growth with disinflation - must be preserved. Appropriate action now will save possibly painful interventions later. This is all the more important as the international adjustment process is slowing down.

Hence, the guidelines laid down in the Annual Economic Report for 1988/1989 aimed at improving the conditions for growth remain entirely valid.

— The remaining decisions on the completion of the internal market must be taken and implemented rapidly to maintain the momentum already generated.

— Economic policy must act to correct the growing imbalances before they affect private sector confidence and through it the foundations of growth. Maintenance of strong economic growth and of continued downward pressure on inflation are necessary if the internal market is to deliver all its promises and if its implementation is not to be slowed down by social and political frictions.

It is disappointing to observe that the current period of growth is not being better exploited to undertake the necessary structural adjustments which many economies still need.

SAFEGUARDING THE CONDITIONS FOR A SUCCESSFUL 1992

1. INTRODUCTION

1988 has been a very positive year for the *world economy*. Activity has grown strongly, mainly in investment, entailing robust trade buoyancy. The outlook for 1989 and 1990 continues to be favourable. Although the good results of 1988 may not be fully repeated the overall trend remains positive.

In the *Community*, the economic performance of 1988 - the most favourable since 1976 - can largely be attributed to the policies that have been implemented over the last years and of the prospects opened up by the completion of the internal market. For the first time, the pattern of growth in 1988, with investment as the most dynamic component, broadly corresponded to that aimed at under the 'Cooperative Growth Strategy' and to that needed for relentless progress towards the objective 1992. In 1989 and 1990 growth is expected to remain strong and to continue at rates of around 3 %.

2. ECONOMIC OUTLOOK FOR 1989 AND 1990: GROWTH CONTINUES

The Community, with around one quarter of world GDP, has a sufficiently large economic base to act as a buffer against external shocks. However, in a world increasingly more integrated, the economic outlook still depends to a large extent on an international environment free of financial upheavals.

2.1 The Community's external environment

Growth of economic activity in the OECD region is expected to be just over 3 % in 1989 and to fall slightly below this figure in 1990. However the international adjustment process is likely to slow down in 1989 and could come to a halt in 1990 as the demand differentials among the major economic zones narrow considerably (see chart 3).

TABLE 1: **Growth of real GDP**

	1985	1986	1987	1988	1989	1990
EC	2,5	2,6	2,8	3,7	3	3
USA	3,8	3,0	3,6	3,8	2 ¾	2
Japan	4,7	2,4	4,3	5,6	4	3 ½
OECD	3,4	2,7	3,3	4,0	3	2 ¾
Growth gap EC/Rest of OECD	−1,5	−0,2	−0,9	−0,6	−¼	+½

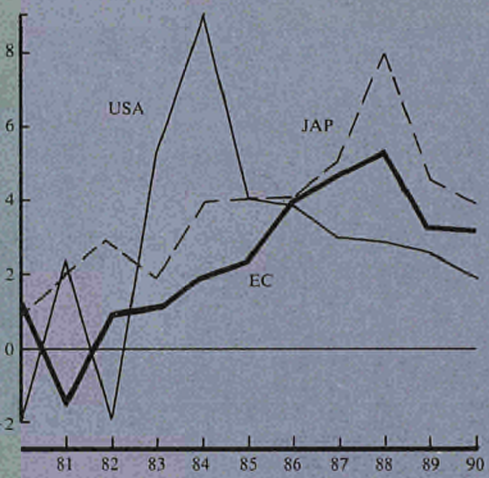
Source: Commission's services (1989/90: forecasts) GNP in USA and Japan

In the *United States*, GNP growth reached almost 4 % in 1988. Business investment was vigorous, and still is. But, of late, export growth - though still strong - has started to decelerate: that may be problematic for the adjustment process. After six years of uninterrupted expansion, supply conditions have become fairly tight: unemployment is low, sectoral capacity constraints are developing and inflationary pressure is building up.

In 1989, export growth is expected to decrease further (plus 10 % against more than 18 % in 1988) while domestic demand is likely to grow moderately (+ 2 ½ %). Depending on the strength of demand, inflation could become a major concern. Even in the case of the expected easing of demand pressures, a new monetary tightening may still be required unless the budget deficit is reduced further. Either outcome could induce a further slowdown in 1990 (+ 2 % for real GNP). With the export boom losing momentum, the trade balance is expected to improve only marginally. But the current account may begin to deteriorate again because of foreign debt service charges.

The economy of *Japan* experienced an exceptionally strong expansion in 1988 (real GNP: +5.6 %), led by buoyant domestic demand (+7.9 %). Substantial wage increases and higher employment provided the base for a strong rise in private consumption (+5.3 %). Higher rates of return on fixed capital have constituted an important stimulus for private enterprise-investment (+15.5 %). These features, together with the flexibility of the labour and product markets, enabled the Japanese economy to adjust successfully to the appreciation of the yen. The surpluses of both the trade and current accounts have fallen by about half a percentage point of GDP, while remaining broadly at the same level in USD terms. In spite of a strong increase in the money supply consumer prices remained remarkably stable (+0.3 %).

CHART 3: **Growth of internal demand in EC, USA, JAP.**



Real annual percentage change.
Source: Commission's services.
1989-90: forecasts.

For 1989 and 1990, the expected growth performance will entail a lower, but still considerable expansion of domestic demand. However, the Japanese economy is expected to contribute little to the absorption of worldwide imbalances.

In the *developing world,* except for some countries confronted with setbacks in their adjustment plans, growth has been sustained in 1988, boosted also by real and nominal growth of export earnings. In 1989 and 1990, growth may slow down slightly, except for a recovery in the larger Latin American economies, depending on whether inflation can be reduced and more normal growth conditions restored. OPEC countries are expected to benefit from the firming of oil prices. Even if the rates of growth of the four Asian NIEs are expected to fall slightly their economic performance should remain strong.

The volume of *world trade*, in line with a somewhat slower growth of activity, should expand at a rate of 7 % in 1989 and by 6 % in 1990. Imports by the OECD countries will grow by 6 ½ % in 1989 and by 5 ¾ % in 1990 in real terms. Trade flows with Asian NIEs will also remain buoyant. However, import volume growth will be sluggish in OPEC, sustained only in a few large economies.

The outlook to 1990 shows that important uncertainties still characterize the international economic environment. A dynamic Community will be better able to contribute to their reduction.

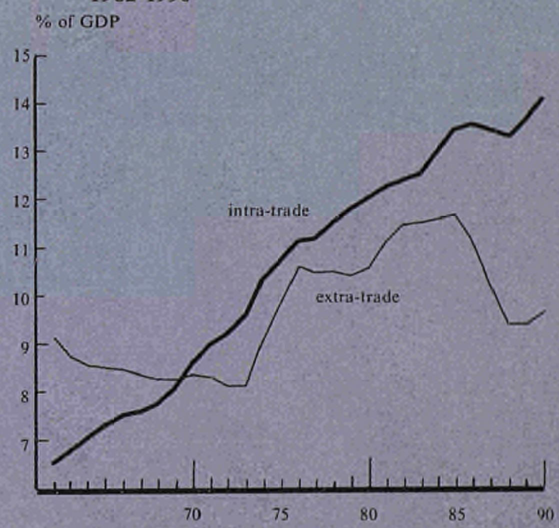
2.2 *The economy of the European Community*

Robust economic growth, notably since mid-1987, is due to continue in 1989 and 1990: output is expected to increase by 3 % in both 1989 and in 1990. Much improved supply-side conditions are providing a better base for growth. Demand prospects remain good and confidence is supported by the prospects opened up by the completion of the internal market. As a result, the growth trend of around 2 ½ % recorded since 1983 has now been transformed into a growth path of around 3 %.

The buoyancy of the EC economy is reflected in strong growth of intra-Community trade which has now reached a level equal to almost 15 per cent of Community GDP whereas extra-Community trade barely reaches 10 per cent. Intra-Community trade shows a clearly rising trend which reflects the increasing integration within the Community, the successive enlargements and, more recently, the effects of the progressive completion of the internal market. The trend of the Community's extra-trade is less clear cut, affected as it is by the very large swings in commodity and oil prices as well as by the girations of the dollar.

Internal demand in the Community, with an expected rate of increase of 3 ¼ in real terms this year and in 1990, should continue to grow faster than GDP implying some further positive contribution to the international adjustment process. Exports to the rest of the world are expected to recover gradually, but imports should still grow faster. The current account should still show a surplus (a quarter of a point of GDP in 1990 against half a point in 1988). Between 1987 and 1990,

CHART 4: **Intra and extra-EC trade as % of GDP, 1962-1990**



Three-year moving averages centred on the last year, current values; trade is defined as the average of import and export figures for goods.
Source: Commission's services.
1989-90: forecasts.

TABLE 2: **The EC economy – Use and supply of goods and services**

	1985	1986	1987	1988	1989	1990
Private consumption	2,6	3,9	3,8	3,7	2 ¾	3
Government consumption	2,0	2,5	2,3	1,9	1 ¾	1 ¾
Gross fixed capital formation	2,5	3,4	4,8	7,3	5 ¾	5
Domestic demand (including stocks)	2,3	3,9	4,1	4,7	3 ¼	3 ¼
Exports of goods and services*	2,5	0,7	2,2	4,7	5 ¼	5
Total demand	2,4	3,5	3,8	4,7	3 ½	3 ½
Imports of goods and services*	1,3	10,9	11,8	11,4	7	6 ¼
GROSS DOMESTIC PRODUCT	2,5	2,6	2,8	3,7	3	3

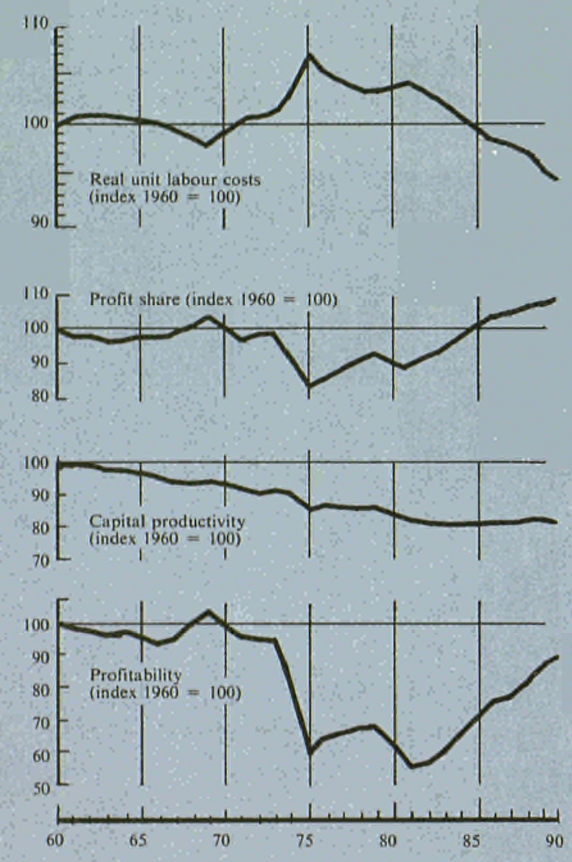
Source: Commission's services (1989/90: fore casts).
* Extra-Community trade only; estimates of the Commission's services.

the Community's contribution to the adjustment of the international payments imbalances will amount to 38 bn. ecus (1987 prices) equal to one point of its GDP.

2.3 Investment and job creation in a growing internal market

Two aspects of the economic outlook for the Community are particularly interesting in the perspective of the completion of the internal market: the *growth of investment* and the *growth-employment-unemployment* relationship. A closer look at them throws light on the extent of the improvement in the supply conditions which has already taken place and shows how far there is still to go.

CHART 5: **Determinants of the profitability of capital in the EC**



Source: Commission services.
1989-90: forecasts.

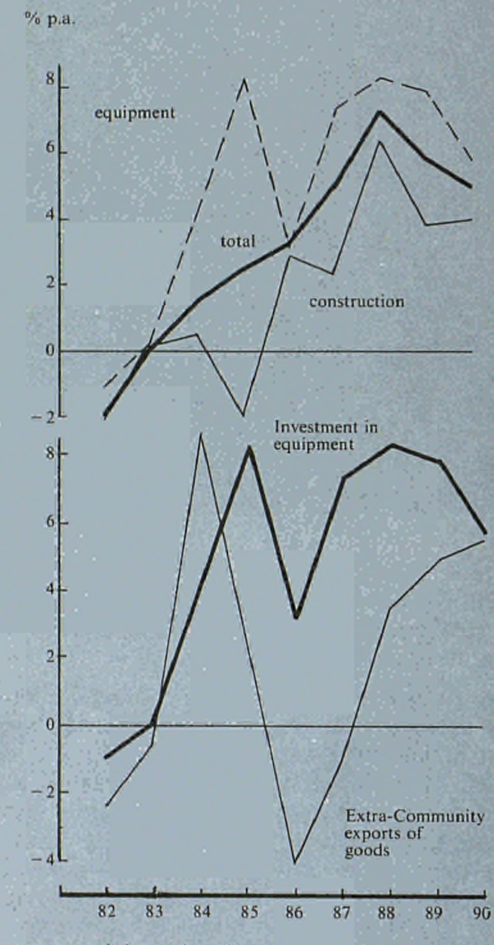
2.3.1 Investment

Gross fixed capital formation has been, and remains, the most buoyant factor behind the current expansion phase of output in the Community. Its present strength can largely be explained by the improvement in the attractiveness of investment which has taken place over the last years. Chart 5 shows how the *profitability of capital* has continued to increase since the beginning of the 1980s. This is due to two factors. First, protracted *wage moderation* helped by the marked improvement in the terms of trade (drop in oil prices and depreciation of the dollar) has induced a steady and pronounced increase in the *profit share* since 1981. In addition, *capital productivity* has stopped falling since 1984 and has even started to improve again thanks also to a strong rise in capacity utilization (see charts 5 and 7).

Investment is now fully responding to the improvement in profitability which has mitigated the negative effects of the high level of real interest rates. However, until mid-1987, the recorded expansion of total investment had been moderate. This had cast doubt on the reaction of the behaviour of firms to the improvement in fundamental conditions. Now it is possible to show that the extent of the recovery had been masked by two particular factors.

In 1985, investment in equipment grew strongly, but construction was depressed by a very severe winter (see chart 6). In 1986 and at the beginning of 1987, investment in equipment was hit by the marked change in the sectoral composition of global demand due to the shift from exports to internal demand which had taken place in 1985-1986 following the depreciation of the dollar and the fall in oil prices (see bottom of chart 6).

CHART 6: **Components of investment; investment in equipment and Community exports**



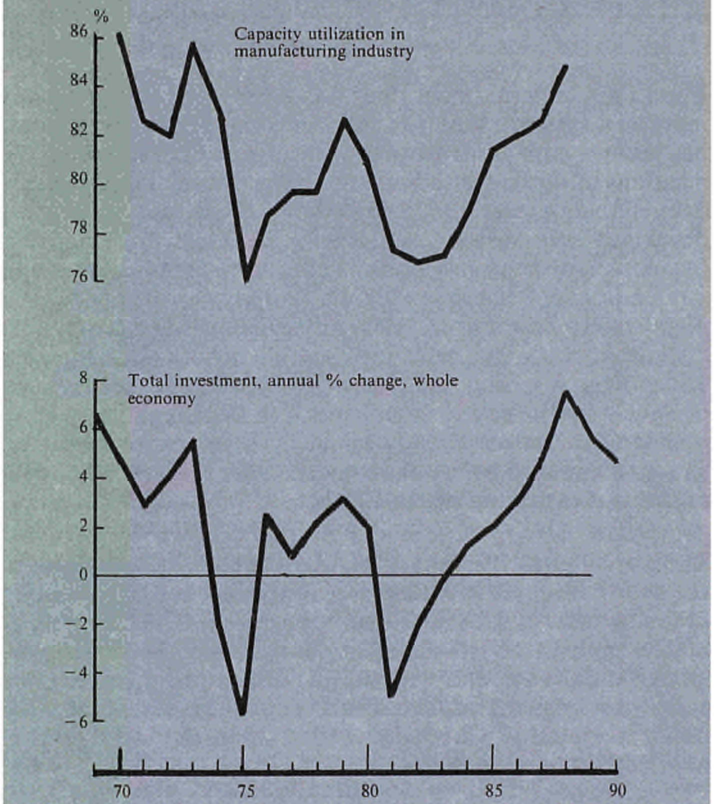
Percentage annual changes in real terms.
Source: Commission's services.
1989-90: forecasts.

Besides the improvement in profitability, the recent upturn in investment is due to the fact that demand has been, and is expected to remain, relatively strong inside and outside the Community (see table 2) and the rate of capacity utilization is now reaching record levels in many countries.

Moreover, it appears that rising expectations in the business sector in relation to 1992 are beginning to have a positive influence on investment trends. With the higher investment, increasing technical progress is being incorporated into the productive system. This could further promote the recovery of capital productivity.

The existing evidence points to a stronger increase of capital widening rather than capital deepening investment. The high rate of capacity utilization combined with the improvement in profitability and a sound economic and monetary environment should ensure a continuation of the expansion of investment and of capacity.

CHART 7: **Capacity utilization and investment (EC)**



Source: Commission's services.
1989-90: forecasts.

Most recent survey evidence points to a considerable increase of available capacity: firms interviewed report high rates of capacity utilization, but do not foresee any significant capacity constraints in the near future. This suggests that the present high investment activity is having an effect on available capacity.

2.3.2 Economic Growth-Employment-Unemployment

A second noteworthy phenomenon is the current *job creation*. In the Community, growth is now more employment creating than ever. This is very important at a time when fears are being expressed that the adjustment required by the completion of the internal market might create transitional job losses. If these jobs losses are indeed occurring, they appear to be more than offset by the current rates of job creation.

The relative cost of labour has come down and this has been accompanied by a slowdown in the substitution of capital for labour and the rate of increase of capital intensity (see chart 8).

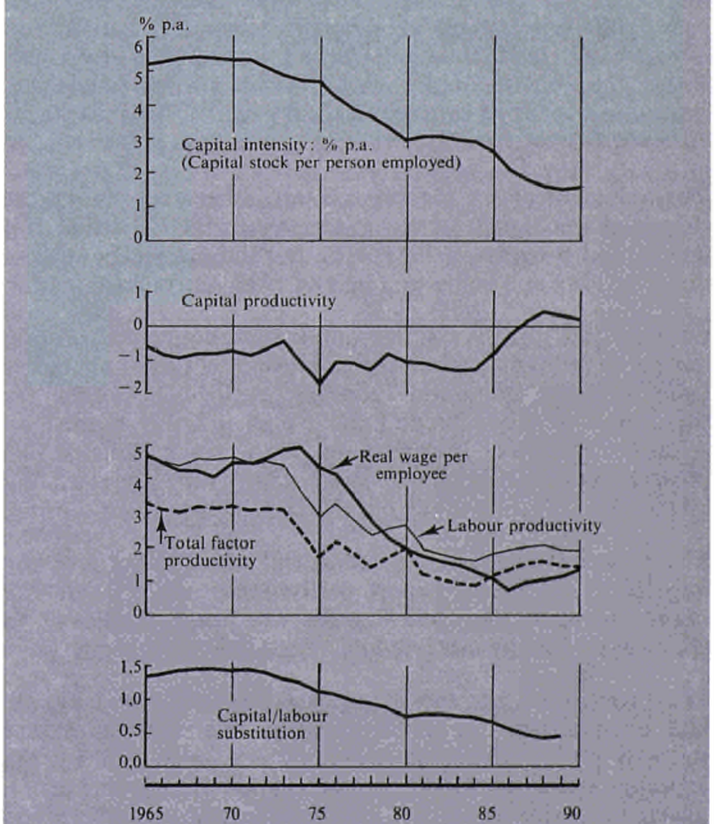
Several factors have played a role in this development. The service sector, with a notoriously low increase of labour productivity, has increased its weight in the economy and contributed strongly to employment. The reduction in individual working time may also have played a role.

Part-time jobs, reflecting the greater flexibility in the labour market, are perhaps the single most important factor explaining the higher employment content of growth. This form of employment accounts in fact for the larger part of the total job creation of the last few years especially in the service sector. Survey results show that part-time employment corresponds to the preference of around two thirds of those so employed.

Employment in the manufacturing sector in 1988 has risen, albeit very slowly, after many years where rationalization had led to large scale shedding of labour.

In 1989 and 1990, *employment* is expected to continue to grow strongly, but unemployment will still be at around 10 ½ % in 1990. This is more than one point below the peak of 1986 (11.7 %) and corresponds roughly to the level of 1983. Besides the increase in the population of working age, the divergence between the performance of employment and the slow reduction of unemployment is explained by an increasing participation rate. At the beginning of the 1980s, in a period of bleak employment prospects, the growth of the labour force in the

CHART 8: **Factors explaining the higher job content of growth**



5 year moving averages centred on last year.
Source: Commission services.

TABLE 3: **Job creation in the Community 1981-90**

In the period	
1981-85	were lost 2,4 mio jobs
1986-90	will be created 6,0 mio jobs
Of these 6 million jobs:	
4 ¾	*will be absorbed by the increase in active population due:*
– 2 ¾	*to demographic factors*
– 2	*to the increase in the participation rate*
1 ¼	*will be utilized to reduce unemployment*

Source: Commission's services (1989/90: forecasts).

TABLE 4: **Current account balances**

	1985	1986	1987	1988	1989	1990
			a) in billion US$			
EC	19,3	47,5	32,6	21,2	13,1	14,5
USA	– 116,4	– 138,3	– 154,0	– 132,7	– 135,0	– 139,1
Japan	49,2	85,9	87,0	84,5	83,7	83,4
			b) as % of GDP			
EC	0,7	1,4	0,9	0,5	0,2	0,2
USA	– 2,9	– 3,4	– 3,6	– 2,7	– 2,6	– 2,5
Japan	3,7	4,3	3,7	3,0	2,7	2,5

Source: Commission's services (1989/90: forecasts).

Community was slightly lower than the growth of the population of working age with the participation rate declining by three quarters of a point between 1980 and 1984. Since 1985, the trend of the labour force has been determined by two opposing factors: the growth of the population of working age has decelerated further, but the participation rate has started to increase significantly.

A certain increase in the participation rate is normal in a period of higher growth, but the nature of the new jobs offered has probably also contributed to the recent increase. In fact, many new jobs, not suitable for the typical registered unemployed, are now taken up by persons, often women, who were previously outside the labour force. In 1989, the participation rate may return to its 1980 level and is expected to go on increasing in 1990. Even then its level will, however, still be significantly below the participation rates of the United States and Japan.

3. ECONOMIC POLICY PROBLEMS

3.1 International issues

The reduction of the current account imbalances among the three major economic zones, and especially the US deficit, has made good progress in 1988. However, adjustment may slow down in 1989 and come to a halt in 1990 (see table 4).

Over the last three years, international economic cooperation has been remarkably successful in preventing these imbalances from affecting the world economic performance. But, the persistence of large disequilibria places a heavy burden on economic policies. Furthermore, large trade deficits fuel protectionnist tendencies that could endanger the liberal trading system on which the industrial world has built its prosperity.

The present strength of the dollar, will certainly not give any impulse to the fading export performance. As a result, the improvement in the trade balance will not be sufficient to compensate for the increase in external debt service charge.

The interest rates increases of the last few months have certainly had an impact on the dollar exchange rate. But the present strength of the dollar is probably also explained by the expectation that the US authorities will take appropriate action on the fiscal side to redirect activity from the domestic to the export sector. Failure to reduce sufficiently the budget deficit might place too heavy a burden on monetary policy. In such circumstances monetary policy would be confronted with the difficult task of trying to control inflationary pressures without inducing a further appreciation of the dollar which would damage the adjustment process.

The LDCs' external debt does not seem to be perceived any more as a systemic threat to the world financial system, but it has become a major constraint to their growth. Aside from the decisions of the Toronto Summit on the poorest countries, the debt situation and the development prospects of the less developed countries are not improving. Growth of activity, balance of payments prospects and of course the social situation remain fragile. Policies in the OECD countries leading to even higher interest rates would place an extra burden on the debtors adding to debt fatigue, which is being felt on both sides. Member States may find that their quest for global partnership can become a useful way to complement, at the Community level, unilateral initiatives already taken by other major creditors. Trade liberalization would significantly improve the debt repayment capability of the LDCs.

The present phase of expansion in the Community owes much to the improvement in private sector confidence resulting, among other factors, from international cooperation. The Community has to intensify efforts aimed at strengthening policy cooperation within itself, and with all its partners, to guarantee the stability of financial markets. Further strengthening of intra-EC policy cooperation will maximize the Community's influence on international developments.

3.2 Community issues.

Within the Community, the underlying structural improvement makes it possible to aim for a sustained medium-term growth path of around 3 ½ % a year. This would enable employment in the Community as a whole to rise by an average of some 1 ½ % a year, thereby opening up the possibility of reducing the unemployment rate significantly.

To achieve this goal, Member States must pursue the policies set out in the*Annual Economic Report for 1988/1989* that the Council has adopted last December. In particular, the remaining decisions on the completion of internal market must be taken and implemented rapidly to maintain the present momentum.

On the other hand, the present growth dynamism helps the internal market process as it facilitates sectoral adjustment. A reduction of the growth momentum of the Community provoked by growing macro-economic imbalances, besides having negative consequences on employment and welfare, would also affect adversely the internal market process. If all the benefits of the completion of the internal market are to be reaped and the economic and social cohesion strengthened, growth conditions must remain sound. Belated corrective actions could endanger the achievement of the objectives of the Community.

Economic policy in the 1980s fought a hard and long disinflation battle with the EMS playing a key role. In the process, a considerable improvement in the fundamental growth factors and in the behaviour of economic agents has been put in motion. Enterprises must be able to count on a sound and stable economic environment: it takes a long time to dampen inflationary expectations. They can quickly be rekindled. The credibility capital gained thus far should not be wasted. In this context, a stronger EMS would be a very useful instrument.

The economic outlook for the Community presented in Section 2 shows that the present dynamism could be at risk if policy does not address rapidly three concerns:

(a) the persistence of external disequilibria among Member States;

(b) the fact that certain Member States are not exploiting the opportunity offered by the stronger growth to take sufficient action to control the still growing debt/GDP ratios;

(c) the reappearance of inflationary pressures.

These three problem areas are closely interlinked. Inflationary expectations are in most cases fuelled by high wage claims or excessive budget deficits. The external imbalances are almost always explained by a loss of competitiveness due to a poor relative price performance or by an inappropriate level of internal demand often attributable to an unsatisfactory budgetary policy. A budgetary policy more oriented towards improving growth conditions finds serious obstacles in too high debt/GDP ratios.

Monetary policy, as the recent coordinated tightening of monetary conditions shows, is called upon almost everywhere to fight inflation or prevent inflationary expectations building up. But excessive reliance on monetary policy makes the reduction of budget deficits more difficult and adversely affects investment and the current account. Budgetary policy could and should play an important role more often. In particular it could help to prevent inflationary expectations building up. It could also be useful in re-establishing saving/investment balances more in line with a sustainable balance of payments configuration. The correction of the disequilibria that are appearing in the Community economy requires a well balanced policy mix that safeguards the objective of improving further supply-side conditions.

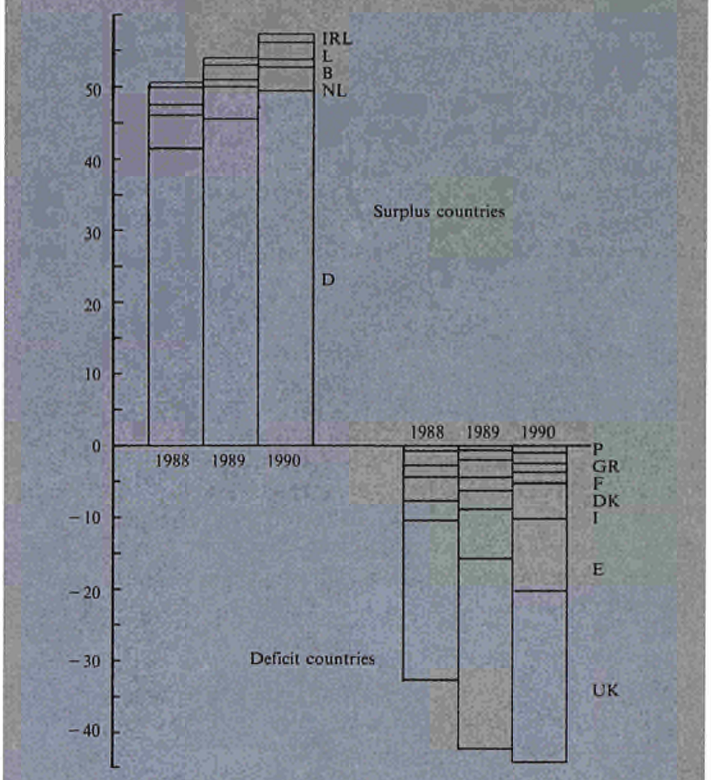
3.2.1 Payments imbalances

The divergences between the external balances of the countries participating in the EMS exchange rate mechanism and the others are increasing. Furthermore, within the EMS, the gap between the surplus and deficit countries is growing particularly as the German surplus is not declining. The polarization of the situation is brought out clearly by chart 9.

To the extent that the surpluses find their counterpart in the deficit of the less favoured countries, the imbalances can be seen as contributing to the catching-up process of the latter where there is a need for increasing investment. Yet, external imbalances in these countries are sustainable in the medium term on condition that the deficit of the current balance corresponds to a strengthening of the domestic productive base and goes hand in hand with sound spontaneous external financing.

This has been the case in Spain and Portugal where the deterioration in current transactions has accompanied a strong uptake in productive investment financed by private capital inflows and increasing interventions of the Community's structural funds and financial instruments. In view of these considerations, the deficits of these countries do not appear very worrying as long as overheating is avoided and the situation remains healthy in respect to the external financing.

CHART 9: **Balance on current account in Ecu billions** [1]



[1] 1989-1990: forecasts.

But these considerations do not justify the full size of the continuing German surplus. The strength of the dollar, monetary cooperation within the EMS, but also various occasional factors, have induced, until now, large capital outflows from Germany sufficient to prevent the appearance of strains within the EMS. However, the situation shows an underlying fragility. Furthermore, the persistence of such a large surplus is leading to a productive sector that is becoming more and more export oriented. Such a trend hinders the structural change towards a relatively larger service sector and reduces the employment intensity of growth.

In Italy and France, the size of the deficits is small. But the situation requires caution as both countries present a certain fragility in their external accounts. In Italy the situation could be severely affected by an increase in oil prices while in France the trade account is very sensitive to any acceleration of internal demand. This fragility is being progressively reduced as growth conditions improve and competitiveness of the enterprise sector increases. Efforts in this direction must continue.

TABLE 5: **Convergence of current account balances** (as % of GDP)

	1984	1987	1988	1989	1990
EC	0,3	0,9	0,5	0,2	0,2
Surplus ([1])	1,6	3,5	3,7	3,9	4,1
– of which Germany	1,3	4,0	4,1	4,3	4,3
Deficit ([2])	−0,3	−0,4	−1,2	−1,5	−1,5
– of which UK	−0,2	−0,6	−3,2	−3,4	−2,8
E+P	0,9	0,2	−0,9	−2,0	−2,8

([1]) Surplus countries: B, D, IRL, L, NL
([2]) Deficit countries: UK, E, P, F, I, DK, GR
Source: Commission's services (1989/90: forecasts).

The same efforts must also continue in Denmark and in Greece where the continuing high external deficits represent a severe constraint on growth.

The very large deficit of the United Kingdom reflects an inappropriate saving/investment pattern. The private sector shows a large borrowing requirement while the public sector has a small financial surplus. The correction of the deficit therefore requires above all an increase in national savings since a reduction of the investment propensity would be unwelcome. An increase in savings could be brought about by various measures including appropriate budgetary policy measures and a more moderate development of wage costs.

3.2.2 Public deficits

Stronger GDP growth has had a positive effect on public deficits. The average general government borrowing requirement, measured as a percentage of GDP is expected to drop by one point between 1987 and 1989. This reduction is larger than the one experienced between 1983 and 1987 in spite of all the efforts aimed at reducing deficits which had taken place in those years. Budgetary consolidation can more easily be achieved in a dynamic context.

TABLE 6: **Convergence of net general government borrowing or lending** (as % of GDP)

	1984	1987	1988	1989	1990
EC	−5,1	−4,2	−3,6	−3,1	−3,1
High deficit (1)	−11,6	−9,2	−8,8	−8,6	−8,7
United Kingdom + DK	−3,9	−1,1	+0,2	+1,2	+1,5
Others (D, E, F, IRL, L)	−1,6	−2,5	−2,1	−1,6	−1,6

(1) Italy, Greece, Belgium, Netherlands, Portugal
(−) borrowing or (+) lending
Source: Commission's services (1989/90: forecasts).

The reduction of the deficits has been achieved through a tighter control on expenditure. Public expenditure, measured as a percentage of GDP, has decreased throughout the 1980s. In the countries where the budget deficit was not excessively high, the margin for manoeuvre on the receipt side has been used to reduce taxes thus improving supply conditions.

However, this positive global picture masks worrying situations in certain countries. Concern must be expressed at the fact that, on the basis of present policies, in 1990 the budget deficits are expected to remain high or even increase in those countries where they are highest and where action to reduce them is most needed (Greece, Italy, Belgium, Portugal, the Netherlands). Furthermore, the divergence among Member countries is increasing. Even if these differences in the level of budget deficits are accompanied by different household saving behaviour, they nevertheless complicate the task of monetary policy in the pursuit of the objectives of internal and external stability.

Budgetary consolidation should remain an important medium term aim for economic policy. Efforts in this direction should be intensified in the countries where the debt/GDP ratio is worrying. The available room for manoevre opened up by higher growth should be used to reform the structure of government receipts and expenditure in a way that will contribute to improving the conditions of supply and demand.

It is disappointing to observe that the current period of expansion is not better exploited to operate the necessary structural adjustments which many economies still need. Reducing the subsidies to unproductive sectors, re-orient public expenditure and re-equilibrate unbalanced public finances are painful operations at all times, but the transitional costs that they entail are minimized in a period of rapid growth. Member States must seize this opportunity.

3.2.3 Inflation

Inflation in the Community is accelerating again. The average increase of the private consumption deflators is forecast to be around 4 ¼ % this year and 4 % in 1990 compared with 3.7 % in 1988. This could negatively affect expectations. The increase results largely from higher import prices (higher oil and raw material prices compounded by an appreciating dollar), but also internal factors are not developing in a satisfactory way in some countries.

In a first group of countries (Belgium, Germany, France, Ireland, Luxembourg and the Netherlands) where, on the whole, inflation has been reduced to very low levels, consumer prices are expected to increase slightly faster this year. This has to be seen as a sort of normalization once import prices do not decrease any more, but, on the contrary, increase once again. Besides, indirect tax increases will add once and for all around one third of a point to the rate for 1989 and explain half of the acceleration experienced by this group of countries between 1988 and 1989. Even if the situation here does not give rise to special concern, care will have to be taken to prevent inflationary expectations building up. They could notably hinder the continuation of a wage behaviour favourable to investment and growth.

TABLE 7: **Rates of inflation** (Weighted average of deflator of private consumption)

	1985	1986	1987	1988	1989	1990
B-NL-L F-D-IRL	3,8	1,1	1,7	2,0	2¾	2½
I-UK-E-DK	7,4	5,6	4,5	5,0	5½	5
P-GR	18,9	17,1	13,0	11,6	10¾	9½
COMMUNITY	5,9	3,8	3,4	3,7	4¼	4

Source: Commission's services (1989/90: forecasts).

A second group is made up of countries (Italy, Spain, the United Kingdom and Denmark) where the rate of inflation, at around five percent, is double that of the previous group. In the first three of these countries, the disinflation process is either progressing very slowly or has actually been reversed. These countries have in common a very high level of internal demand fuelled by either too high nominal wage increases or public expenditure flows which are not yet under control. Monetary policy is particularly tight in these countries, but action will have to taken on the fundamental causes of the disequilibria.

Finally, in the third group (Portugal and Greece) the rate of inflation is still at an unsustainably high level and the expected improvement is insufficient especially in the case of Greece. Unfavourable developments in public finances and wages are at the origin of these inflationary pressures. The implementation by Greece of a medium-term fiscal consolidation strategy along the lines of the financial adjustment programme announced already by Portugal would contribute to a smoother disinflation process.

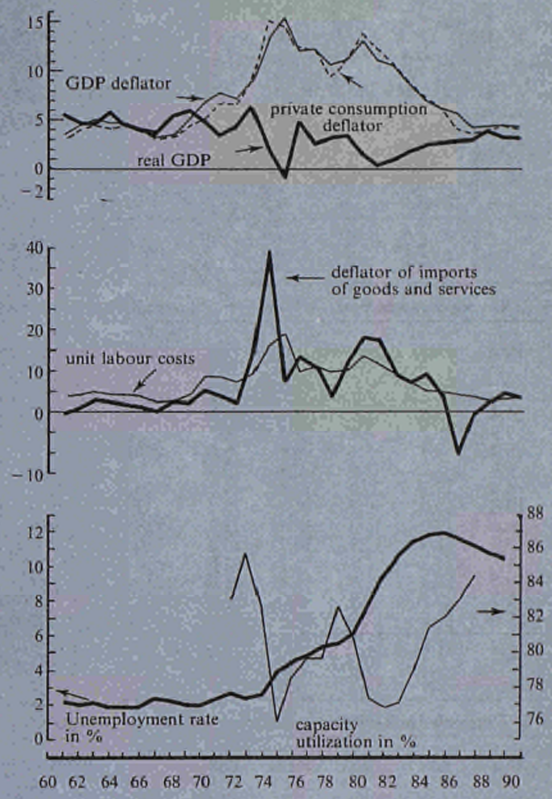
All the countries in the last two groups are experiencing balance of payments problems to different degrees. Wage moderation is therefore even more important to restore international competitiveness and maintain, via strong exports, an acceptable level of activity considering the adverse effects that the other measures aimed at containing inflation will inevitably have.

Finally, wage increases should remain moderate throughout the Community, to allow a continuation of the recovery of profitability which is still below the levels achieved in the quasi full employment period of the 1960s. A further improvement in profitability is needed to maintain and strengthen investment and make it more employment creating.

The success and the speed of the disinflation process has constituted one of the striking aspects of the present phase of expansion. In the process, the authorities have gained credibility. Monetary policy, which had become more accomodating following the financial crisis of the end of 1987, has been tightened across the Community since mid-1988 as soon as inflationary pressures were perceived. With monetary expansion still leaving ample room for growth, the further tightening of monetary conditions of January 1989 helped to prevent a new appreciation of the dollar and to dampen rising inflationary expectations. However, a spiralling increase of interest rates amongst the major economic zones must be prevented. This would, among other negative effects, increase the burden of the debt of the LDCs and increase the deficits in the Member States where debt/GDP rates are high. The future of world interest rates depends to a large extent on the budgetary policy decisions of the new US administration.

Also in the Community, it is necessary that the task of monetary policy be eased by having other policies playing their role. Monetary policy is nowadays being more and more called upon to attain three objectives simultaneously: an internal one, to allow non inflationary growth; a Community one, to provide exchange rate stability within the internal market; an international one, to achieve an exchange rate configuration that allows an orderly continuation of the adjustment process. A continuing favourable wage behaviour and budgetary policy in particular should help, but developments in these areas give cause for concern.

CHART 10: **Inflation in the Community; factors influencing inflation (annual percentage changes)**



1989-90: forecasts.
Source: Commission services.

TABLE A.1: **Industrial production** (a) — Percentage change on preceding period (s.a.)

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 June	July	Aug.	Sept.	Oct.	Nov.	Dec.	Change over 12 months (%) (b)
B	2,5	2,5	0,8	2,1	:	0,1	3,7	0,6	1,2	:	2,2	2,4	−3,8	2,0	1,1	1,0	:	7,9
DK	9,7	4,2	4,2	−3,1	0,9	0,4	1,2	1,6	−4,2	2,2	6,3	−11,2	6,4	−2,3	−2,5	6,5	−0,1	−1,6
D	3,2	5,3	1,9	0,2	:	0,8	0,8	0,8	2,3	0,5	2,8	−3,4	6,6	−1,8	−1,3	−0,6	1,5	5,6
GR	1,6	3,4	−0,2	−1,7	:	2,4	5,4	−0,4	0,2	:	1,8	−2,7	2,0	−2,3	−1,3	3,0	:	4,4
E	0,8	2,0	3,1	4,6	3,0	−0,2	0,6	1,1	−0,8	1,1	0,7	−2,4	−1,2	3,3	−3,9	6,8	−3,4	2,6
F	2,0	1,0	1,0	2,0	:	0,8	0,9	1,0	1,8	0,5	1,8	0,7	0,0	−1,0	−1,2	4,0	−0,9	5,0
IRL	9,9	3,5	3,2	9,7	:	4,1	2,8	0,8	0,8	:	4,0	−3,9	0,7	2,5	5,6	:	:	13,4
I	3,4	1,3	2,7	3,9	:	2,2	2,4	0,1	3,0	1,3	0,9	2,8	2,3	−1,6	0,1	0,9	2,9	7,9
L	13,3	6,9	2,8	0,8	:	5,7	2,9	2,7	3,8	:	2,2	1,2	5,2	−6,4	3,4	1,9	:	15,8
NL	5,2	3,9	0,0	0,9	:	2,5	−3,1	−0,6	4,8	0,9	1,9	4,7	−3,6	2,8	1,8	−0,9	−2,7	0,9
P	−0,1	10,9	5,7	2,4	:	−1,1	3,4	1,2	−0,1	:	−3,2	1,4	−0,5	−1,1	2,7	:	:	8,7
UK	0,2	5,5	2,2	3,8	:	1,5	−0,3	1,6	1,5	−0,2	0,5	0,7	0,1	0,5	−0,4	−0,6	−1,8	1,4
EUR 12	2,1	3,4	2,0	2,2	:	1,4	0,8	0,8	(1,6)	:	1,6	−0,8	(0,9)	(1,5)	(−0,9)	:	:	(3,0)
USA	12,3	2,1	2,1	4,4	:	1,8	1,2	1,3	1,8	:	0,2	1,1	0,3	0,3	0,6	0,4	:	6,0
JAP	9,4	3,7	−0,2	3,0	(9,8)	3,5	3,2	−0,2	2,4	(2,4)	3,3	−0,9	2,7	0,5	−1,0	2,8	(0,9)	(8,3)

TABLE A.2: **Unemployment rate** — Number of unemployed as percentage of civilian labour force (s.a.)

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 July	Aug.	Sept.	Oct.	Nov.	Dec.	1989 Jan.	Change over 12 months (%) (b)
B (g)	14,4	13,6	12,5	12,1	11,1	11,8	11,6	11,3	11,1	10,6	11,4	11,1	10,9	10,7	10,6	10,5	10,4	−9,9
DK	9,9	8,7	7,5	7,5	8,3	7,5	7,7	8,2	8,6	8,9	8,5	8,5	8,6	8,9	8,9	9,0	8,9	17,2
D	8,4	8,4	8,1	8,1	8,0	8,1	8,0	8,2	8,1	7,9	8,2	8,1	8,1	8,0	7,9	7,8	7,4	−7,3
GR	1,8	2,2	2,8	2,8	2,8	2,7	2,8	2,7	2,8	2,7	2,8	2,9	2,8	2,8	2,8	2,7	2,6	−1,4
E	18,4	19,5	20,0	20,4	19,6	20,6	20,4	20,0	19,5	18,7	19,7	19,6	19,2	18,9	18,6	18,5	18,2	−9,7
F	10,0	10,5	10,7	11,1	10,9	11,0	10,9	10,8	10,9	10,7	11,0	11,0	10,8	10,8	10,6	10,7	10,7	−1,0
IRL	16,6	17,9	18,3	19,1	18,7	19,0	18,9	18,7	18,7	18,5	18,8	18,7	18,6	18,6	18,5	18,3	18,3	−2,7
I	12,0	12,9	13,7	14,2	16,2	14,6	15,6	16,3	16,6	16,5	16,6	16,8	16,6	16,5	16,5	16,4	16,0	4,8
L	1,8	1,7	1,5	1,7	1,5	1,7	1,7	1,6	1,6	1,4	1,6	1,5	1,5	1,4	1,4	1,4	1,3	−18,3
NL (g)	14,5	13,3	12,3	11,8	11,6	11,7	11,7	11,7	11,6	11,6	11,7	11,6	11,6	11,6	11,6	11,5	:	−1,0
P	6,7	7,7	8,3	7,0	6,7	6,5	6,7	6,6	6,6	6,6	6,6	6,6	6,6	6,5	6,6	6,7	6,9	3,3
UK	11,6	11,8	12,0	10,7	8,6	9,9	9,4	8,9	8,4	7,6	8,5	8,4	8,2	7,8	7,6	7,4	7,3	−23,8
EUR 12	11,2	11,6	11,7	11,6	11,4	11,5	11,5	11,5	11,4	11,1	11,5	11,5	11,3	11,2	11,1	11,0	(10,8)	(−5,6)
USA	7,5	7,2	7,0	6,2	:	5,9	5,7	5,4	5,5	:	5,4	5,6	5,4	5,3	5,4	:	:	−7,0
JAP (h)	2,7	2,6	2,8	2,8	2,5	2,7	2,7	2,5	2,5	2,4	2,5	2,6	2,5	2,4	2,4	2,2	:	−10,6

TABLE A.3: **Consumer price index** — Percentage change on preceding period

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 July	Aug.	Sept.	Oct.	Nov.	Dec.	1989 Jan.	Change over 12 months (%) (b)
B	6,4	4,9	1,3	1,6	1,2	−0,3	0,0	0,7	0,6	0,3	0,3	0,2	0,1	0,0	−0,1	0,4	0,4	2,4
DK	6,3	4,7	3,7	4,0	4,5	1,2	1,2	1,4	0,4	1,2	−0,4	0,7	0,5	0,2	0,7	0,0	0,5	4,6
D	2,4	2,2	−0,2	0,3	1,2	0,0	0,5	0,5	0,1	0,4	−0,1	0,1	0,0	0,1	0,2	0,2	1,1	2,6
GR	18,4	19,3	23,0	16,4	13,5	5,4	1,6	4,5	1,9	5,4	−0,3	0,3	3,0	2,5	0,7	1,1	−0,3	13,8
E	11,2	8,8	8,8	5,3	4,8	1,2	1,2	0,3	2,5	1,3	1,3	1,0	1,0	0,1	−0,1	0,8	1,0	6,3
F	7,3	5,9	2,7	3,1	2,7	0,5	0,5	1,0	0,9	0,6	0,3	0,3	0,2	0,2	0,1	0,2	0,4	3,3
IRL (i)	8,6	5,4	3,8	3,1	2,2	0,1	0,7	0,5	0,8	0,6	(0,3)	(0,3)	(0,2)	(0,2)	(0,2)	:	:	2,7
I	10,8	9,2	5,8	4,7	5,1	1,6	1,2	1,0	1,0	1,9	0,2	0,4	0,5	0,8	0,8	0,3	(0,8)	(5,7)
L	6,4	4,1	0,3	−0,1	1,4	0,4	0,4	0,2	0,7	0,6	0,4	0,1	0,1	0,2	0,3	0,0	0,7	2,5
NL	3,1	2,3	0,2	−0,4	0,9	0,8	−0,7	0,7	0,4	0,4	0,1	0,3	0,3	0,1	0,1	−0,1	(−0,9)	(0,9)
P	29,3	19,3	11,7	9,4	9,6	2,5	3,1	1,7	2,6	(3,6)	0,8	1,4	1,1	0,9	1,5	(1,2)	(1,3)	12,2
UK	5,0	6,1	3,4	4,1	4,9	1,1	0,5	2,4	1,4	2,1	0,1	1,1	0,5	1,0	0,5	0,3	0,6	7,5
EUR 12	(7,4)	(6,1)	(3,6)	(3,3)	(3,6)	(0,9)	(0,7)	(1,2)	(1,0)	(1,2)	(0,2)	(0,5)	(0,4)	(0,4)	(0,3)	(0,3)	(0,7)	(4,8)
USA	4,3	3,6	1,9	3,7	4,1	0,8	0,6	1,3	1,3	1,0	0,4	0,4	0,7	0,3	0,1	0,2	0,5	4,7
JAP	2,3	2,2	0,7	0,1	0,7	0,3	−0,5	0,7	0,2	0,8	−0,2	0,3	0,8	0,5	−0,4	−0,3	(0,1)	(1,4)

TABLE A.4: **Visible trade balance** — fob/cif, million ECU (s.a.)

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 June	July	Aug.	Sept.	Oct.	Nov.	Dec.	Change over 12 months (%) (c)
B/L	−4897	−3514	146	−580	:	−510	−396	−813	−987	:	−392	−284	−407	−296	−67	:	:	205
DK	−1108	−1538	−1714	96	1066	5	444	102	166	400	−58	107	63	−4	154	45	201	204
D	24136	32986	53044	56960	60936	14738	12908	15782	15407	15.870	6626	5075	5365	4968	(4511)	5756	5603	19
GR	−6048	−7266	−5809	−5694	:	−1257	:	:	:	:	:	:	:	:	:	:	:	−333
E	−4711	−5582	−6306	−8749	−12000	−2431	−2347	−2830	−2916	−3603	−986	−801	−1247	−868	−1087	−1108	−1407	−874
F	−13130	−13428	−9699	−12473	−11968	−3232	−2405	−2969	−3264	−3420	−811	−814	−1617	−833	−942	−1349	−1128	−129
IRL	81	430	983	2047	2740	670	649	721	740	684	244	275	216	249	264	229	191	−1
I	−13849	−16130	−2459	−7427	−8390	−1830	−2804	−757	−3230	−2165	−525	−620	−1157	−1453	−885	−550	−729	−54
NL	4740	3874	4161	1088	:	664	62	−531	582	:	−283	−6	448	139	301	(549)	:	(386)
P	−3467	−2735	−1297	−2955	:	−705	−734	−829	−896	:	−248	−251	−357	−287	−312	:	:	−28
UK	−14005	−11540	−19868	−20890	−42385	−6618	−8685	−9928	−10856	−13031	−3496	−4466	(−3655)	−2735	−5062	−4220	−3749	−1409
EUR 12 (j)	−32256	−24653	11053	757	:	−844	(−4937)	(−4019)	(−7645)	:	(−656)	(−2766)	(−3024)	(−1855)	(−3871)	(−1916)	:	(−2301)
USA (k)	−154992	−194856	−157829	−147830	−116231	−35521	−30343	−27411	−29128	−29349	−11159	−8403	−11115	−9610	−8999	−10308	−10042	76
JAP	42599	60497	84010	69636	65349	15396	16861	13700	15997	18791	4383	5518	5002	5477	6310	6436	6045	702

TABLE A.5: **Money stock** (l) — Percentage change on preceding period (s.a.)

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 July	Aug.	Sept.	Oct.	Nov.	Dec.	1989 Jan.	Change over 12 months (%) (d)
B (M2)	5,9	7,6	11,5	10,5	:	2,4	2,2	1,5	1,8	:	:	:	:	:	:	:	:	8,1
DK (M2)	17,8	15,8	8,4	4,4	3,5	1,8	−2,1	3,0	2,1	0,4	1,7	−1,0	1,5	−0,4	−0,9	1,6	0,7	4,8
D (M3)	4,7	5,1	6,8	6,0	6,8	1,4	1,9	1,8	1,5	1,4	0,1	0,7	0,8	0,4	0,7	0,3	0,8	6,9
GR (M3)	29,4	26,8	19,0	24,8	22,8	6,0	7,0	5,1	5,1	4,9	1,7	1,7	1,7	1,2	1,7	1,9	:	22,8
E (ALP)	13,2	12,8	11,4	14,0	11,0	3,5	2,5	2,7	2,5	2,8	0,8	0,9	0,8	0,9	0,9	0,9	:	11,0
F (M2)	9,8	6,0	4,1	4,3	3,1	1,4	−0,8	2,1	0,8	1,1	2,1	−0,5	−0,8	1,6	−0,1	−0,4	:	3,1
IRL (M3)	10,1	5,3	−1,0	10,9	6,3	1,6	2,3	1,8	2,1	0,3	0,9	0,3	0,9	−2,1	0,5	2,0	1,3	8,4
I (M2)	12,1	10,8	9,4	8,3	7,7	1,8	0,7	3,0	2,9	1,1	1,4	0,4	1,0	0,9	0,0	0,2	:	7,7
NL (M2)	(6,8)	(10,5)	4,5	3,9	:	1,5	1,1	3,5	3,0	:	1,0	1,4	0,6	1,5	1,0	:	:	10,6
P (L)	24,6	28,9	25,9	16,8	:	1,9	5,4	3,5	(4,3)	:	2,3	(−0,1)	(2,1)	(−0,3)	(3,0)	:	:	(15,0)
UK (LM3)	10,1	13,4	19,1	22,9	20,5	5,2	4,1	4,5	6,5	4,1	2,9	0,9	2,6	0,7	1,0	2,4	1,3	21,7
EUR 12 (m)	(9,8)	(9,6)	9,7	10,1	(9,6)	2,4	1,6	2,8	2,8	(2,1)	1,4	0,5	0,9	(0,8)	(0,5)	(0,7)	:	(9,6)
USA (M2)	8,2	8,1	9,1	3,4	5,8	0,9	2,3	1,7	0,6	1,3	0,3	0,2	0,1	0,1	0,7	0,4	−0,1	5,0
JAP (M2)	7,8	8,7	9,2	10,8	10,2	(3,0)	(2,7)	2,5	2,7	1,9	2,0	−0,2	0,9	1,0	0,2	0,6	:	7,5

TABLE A.6: **Short-term interest rates** (n)

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 Aug.	1988 Sept.	1988 Oct.	1988 Nov.	1988 Dec.	1989 Janu.	1989 Febru.	Change over 12 months % (e)
B	11,5	9,6	8,1	7,1	6,7	6,8	6,1	6,1	7,4	7,5	7,5	7,4	7,3	7,2	7,5	7,7	8,0	1,8
DK	11,5	10,0	9,1	9,9	8,3	9,3	8,7	8,4	7,8	8,0	7,9	7,8	7,8	7,8	8,0	8,0	7,8	–0,8
D	6,0	5,4	4,6	4,0	4,3	3,5	3,4	4,4	4,9	5,3	5,3	4,9	4,8	4,9	5,3	5,8	6,1	2,8
GR	15,7	17,0	19,8	14,9	14,3	16,7	14,4	16,4	13,8	11,7	11,4	13,8	11,7	11,7	11,7	0,0	0,0	–5,0
E	14,9	12,2	11,7	15,8	11,6	13,1	10,7	10,7	12,5	14,0	10,7	12,5	12,3	12,6	14,0	14,4	14,4	2,6
F	11,7	10,0	7,7	8,3	7,9	8,6	8,3	7,3	7,9	8,6	8,0	7,9	8,1	8,1	8,6	8,8	8,9	1,4
IRL	13,2	12,0	12,4	11,1	8,1	8,8	8,3	7,8	7,6	8,4	8,1	7,6	7,6	8,0	8,4	8,2	8,3	–0,6
I	17,3	15,0	12,8	11,4	11,3	11,5	11,1	11,1	11,4	11,8	11,1	11,4	11,5	11,8	11,8	12,4	12,5	1,4
NL	6,1	6,3	5,7	5,4	4,8	4,6	4,0	4,4	5,6	5,8	5,4	5,6	5,3	5,4	5,8	6,3	6,6	2,6
P	22,5	21,0	15,6	13,9	13,0	14,0	13,0	12,7	12,8	12,8	13,0	12,8	12,8	12,8	12,8	12,5	12,5	–0,6
UK	10,0	12,2	10,9	9,7	10,3	8,9	8,6	9,9	11,9	13,2	12,3	11,9	12,0	13,2	13,2	13,0	13,0	3,6
EUR 12 (o)	11,2	10,4	9,0	8,8	8,5	8,3	7,8	8,1	8,9	9,6	8,9	8,9	8,9	9,2	9,6	9,6	9,8	1,9
USA	9,5	7,5	6,0	5,9	6,9	5,9	5,9	6,8	7,5	8,4	7,5	7,5	7,6	8,2	8,4	8,7	8,9	3,1
JAP	6,3	6,5	5,0	3,9	4,0	3,9	3,9	4,0	4,3	4,7	4,1	4,3	4,3	4,5	4,7	4,6	4,6	0,8

TABLE A.7: **Long-term interest rates** (p)

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 Aug.	1988 Sept.	1988 Oct.	1988 Nov.	1988 Dec.	1989 Janu.	1989 Febru.	Change over 12 months % (e)
B	12,0	10,6	7,9	7,8	7,9	8,0	7,7	7,8	8,1	8,1	8,3	8,1	8,0	8,1	8,1	8,2	8,5	1,1
DK	14,0	11,6	10,5	11,9	10,6	11,7	11,1	10,6	10,1	9,8	10,5	10,1	10,0	10,0	9,8	9,9	10,1	–0,7
D	7,8	6,9	5,9	5,8	6,1	6,0	5,7	6,1	6,3	6,3	6,5	6,3	6,2	6,1	6,3	6,5	6,9	1,1
GR	18,5	15,8	15,8	17,4	16,9	19,1	19,1	15,2	14,9	13,9	14,1	14,9	15,3	12,8	13,9	0,0	0,0	12,8
E	16,5	13,4	11,4	12,8	11,8	13,1	11,8	11,3	11,4	12,8	11,1	11,4	12,1	12,5	12,8	13,2	13,4	1,5
F	12,5	10,9	8,4	9,4	9,0	10,0	9,4	8,8	8,8	8,5	9,4	8,8	8,6	8,7	8,5	8,6	9,3	0,2
IRL	14,6	12,7	11,1	11,3	9,4	10,5	10,1	9,6	8,8	8,3	9,1	8,8	8,2	8,4	8,3	8,6	8,8	–1,6
I	15,0	14,3	11,7	11,3	12,1	12,5	12,1	12,1	12,3	12,3	12,1	12,3	12,1	12,0	12,3	12,3	12,7	0,6
L	10,3	9,5	8,7	8,0	7,1	7,0	7,7	6,5	7,5	6,1	7,3	7,5	7,7	7,0	6,1	7,5	7,6	–0,2
NL	8,6	7,3	6,4	6,4	6,3	6,3	6,0	6,3	6,4	6,4	6,6	6,4	6,2	6,3	6,4	6,6	7,0	0,9
P	32,5	25,4	17,9	15,4	14,1	15,2	14,1	14,0	14,1	14,4	13,8	14,1	13,8	14,1	14,4	14,1	13,9	–0,6
UK	10,7	10,6	9,8	9,5	9,3	9,5	9,0	9,6	9,4	9,5	9,7	9,4	9,2	9,4	9,5	9,2	9,3	0,1
EUR 12 (o)	11,8	10,9	9,2	9,4	9,4	9,8	9,3	9,3	9,3	9,4	9,5	9,3	9,2	9,3	9,4	9,5	9,8	0,4
USA	12,0	10,8	8,1	8,7	9,0	9,1	8,6	9,0	9,1	9,1	9,3	9,1	8,9	9,1	9,1	9,1	9,2	0,8
JAP	7,3	6,5	5,2	4,7	4,7	4,7	4,5	4,7	5,2	4,5	5,2	5,2	4,8	4,6	4,5	4,6	4,9	0,6

TABLE A.8: **Value of ECU** = ... units of national currency or SDR

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 Aug.	1988 Sept.	1988 Oct.	1988 Nov.	1988 Dec.	1989 Jan.	1989 Febru.	Change over 12 months % (b)
BFR/LFR	45,44	44,91	43,80	43,04	43,43	43,19	43,23	43,44	43,54	43,49	43,63	43,48	43,46	43,45	43,56	43,65	43,67	1,1
DKR	8,15	8,02	7,94	7,88	7,95	7,96	7,92	7,94	7,94	8,00	7,96	7,96	7,99	8,00	8,02	8,07	8,11	2,6
DM	2,24	2,23	2,13	2,07	2,07	2,07	2,07	2,08	2,08	2,08	2,08	2,07	2,07	2,07	2,08	2,08	2,08	0,9
DR	88,4	104,8	137,4	156,1	167,5	161,9	165,2	166,4	167,2	171,4	167,1	168,1	169,6	171,7	173,0	173,1	173,9	5,4
PTA	126,5	129,0	137,5	142,2	137,6	138,4	139,4	137,5	137,5	136,0	136,9	138,0	137,0	136,4	134,6	130,6	130,1	–6,6
FF	6,87	6,80	6,80	6,93	7,04	6,98	6,99	7,03	7,04	7,09	7,05	7,05	7,07	7,08	7,10	7,10	7,09	1,6
IRL	0,726	0,715	0,733	0,775	0,776	0,776	0,776	0,777	0,774	0,776	0,776	0,773	0,775	0,776	0,777	0,779	0,781	0,6
LIT	1381	1447	1462	1495	1537	1514	1524	1543	1543	1539	1541	1547	1545	1541	1533	1529	1525	0,3
HFL	2,52	2,51	2,40	2,33	2,34	2,33	2,32	2,33	2,35	2,34	2,35	2,34	2,34	2,34	2,35	2,35	2,35	1,4
ESC	115,6	130,0	146,9	162,5	170,1	166,6	169,1	169,7	169,8	171,7	169,4	170,8	171,1	172,0	172,0	170,9	171,0	1,3
UKL	0,591	0,589	0,670	0,705	0,664	0,692	0,687	0,661	0,657	0,653	0,650	0,659	0,656	0,656	0,648	0,641	0,641	–7,4
USD	0,788	0,759	0,983	1,154	1,183	1,213	1,234	1,218	1,114	1,170	1,104	1,111	1,140	1,185	1,184	1,138	1,125	–7,6
YEN	187,0	180,4	165,0	166,5	151,5	164,3	157,9	153,0	148,0	146,4	147,5	149,4	146,8	146,0	146,3	144,7	143,6	–8,7
DTS	0,833	0,767	0,749	0,838	0,892	0,895	0,889	0,902	0,890	0,859	0,893	0,879	0,864	0,854	0,859	0,864	0,874	–3,9

TABLE A.9: **Effective exchange rates: export aspect** (q) — Percentage change on preceding period

	1984	1985	1986	1987	1988	1987 IV	1988 I	1988 II	1988 III	1988 IV	1988 Aug.	1988 Sept.	1988 Oct.	1988 Nov.	1988 Dec.	1989 Jan.	1989 Febru.	Change over 12 months % (b)
B/L	–2,2	0,9	5,5	4,1	–1,3	0,6	–0,2	–0,9	–1,4	0,6	–0,5	0,6	0,2	0,4	–0,3	–0,9	–0,3	–2,8
DK	–3,7	1,2	6,3	4,2	–1,9	1,1	0,3	–1,3	–1,8	–0,2	–1,2	0,3	–0,2	0,5	–0,5	–1,6	–0,7	–5,6
D	–1,6	0,3	10,7	6,9	–0,8	1,8	–0,1	–1,3	–2,0	0,9	–0,7	0,8	0,3	0,6	–0,4	–1,3	–0,3	–3,7
GR	–14,4	–15,9	–21,3	–9,9	–7,2	–1,8	–2,1	–1,2	–2,0	–2,0	–0,8	–0,3	–0,7	–0,8	–0,8	–0,8	–0,7	–7,2
E	–2,4	–2,3	–1,5	0,2	3,1	3,0	–0,8	0,8	–1,8	1,9	0,2	–0,5	1,1	1,1	1,3	2,2	0,0	4,5
F	–4,8	1,1	4,5	1,1	–2,3	0,3	–0,3	–1,3	–1,8	–0,2	–1,1	0,3	–0,1	0,4	–0,4	–1,0	–0,1	–4,5
IRL	–4,2	1,2	3,7	–2,1	–1,4	1,0	–0,2	–1,3	–1,4	0,3	–0,9	0,8	0,0	0,4	–0,4	–1,3	–0,5	–4,0
I	–5,9	–5,2	3,7	1,1	–3,5	0,5	–0,8	–2,0	–1,9	1,0	–0,6	–0,1	0,4	0,9	0,5	–0,7	–0,1	–2,9
NL	–1,6	0,3	7,7	5,1	–0,4	1,3	0,1	–0,9	–1,8	0,6	–0,6	0,7	0,2	0,4	–0,4	–0,9	–0,2	–3,2
P	–17,4	–11,5	–7,8	–7,1	–5,1	–1,4	–1,5	–1,1	–1,3	–0,7	–0,6	–0,5	0,0	–0,1	–0,2	–0,2	–0,3	–3,6
UK	–4,7	–0,2	–7,3	–1,0	5,7	2,8	0,7	3,2	–1,8	1,5	1,3	–1,1	0,8	1,0	1,1	0,0	–0,4	4,8
EUR 12	–9,3	–1,9	9,6	7,0	–1,6	3,3	–0,5	–1,6	–4,7	1,8	–1,1	0,5	0,7	1,6	0,1	–2,0	–0,6	–5,7
USA	7,8	4,1	–19,1	–12,1	–6,1	–5,8	–2,9	–0,7	6,2	–4,5	1,4	0,0	–2,8	–3,1	–0,3	2,6	0,7	1,7
JAP	5,8	3,0	27,2	8,2	10,4	5,1	4,8	1,8	–2,4	4,3	0,5	–0,7	3,0	2,6	–0,4	–1,3	0,1	3,4

Sources: For Community countries: Eurostat, unless otherwise specified; for the USA and Japan: national sources.
(a) National sources, except for the Community, Denmark, Ireland, Belgium and Luxembourg. Because of differences in methods of seasonal adjustment, the change in the EUR index, adjusted by Eurostat and given in Table 1 may differ from the change in the EUR index obtained by aggregating national indices. Data are adjusted for working days. They do not include building.
(b) % change over 12 months on the basis of the non-adjusted nominal series of the most recent figure given.
(c) Change on corresponding month in previous year; seasonally adjusted.
(d) Change over 12 months in seasonally adjusted figures of the most recent figure given for each country.
(e) Difference in relation to the same month of the previous year.
(f) Number of registered unemployed according to national legislation. Annual average, quarterly average and end of month.
(g) Changes in the coverage of these series occurred in 1984 for the Netherlands and in 1985 for Belgium.
(h) As % of total labour force.
(i) Monthly series calculated by linear interpolation.
(j) The seasonally adjusted position for the Community does not correspond to the sum of other Member States; it is obtained by saisonal adjustment of the sum of gross figures for the various countries' exports and imports.
(k) Unadjusted figures.
(l) National sources for Belgium, Denmark, Germany, Spain, France, Portugal and the United Kingdom; seasonal adjustment by Eurostat for Greece, Ireland, Italy and the Netherlands.
(m) Average of monthly changes, seasonally adjusted, weighted by GDP at 1980 prices and purchasing power parities. The monthly change in Belgium is obtained by linear interpolation of quarterly data.
(n) National sources; three-month interbank rate except: Belgium: yield on issue of four-month *Fonds des Rentes* certificates; Denmark: daily money market rate (monthly average); Portugal, 6 month deposits; from 8/85, 3 month Treasury Bills (months average). Annual average, end quarter and end month.
(o) Average weighted by GDP at 1980 prices and purchasing power parities.
(p) Yield on public sector bonds. Annual average. Average for the last month of quarter and monthly average for Germany, Spain, Italy, Luxembourg, the Netherlands and Portugal. End quarter and end month for the other Member States.
(q) Weighting coefficients are calculated so as to allow not only for bilateral trade but also for competition on third markets and on the domestic market of the exporting country.
Note: (s.a.) = seasonally adjusted : = data not available ( ) = estimated.

Principal economic policy measures - February 1989

Community (EUR 12)

22.2 The Commission adopts its Communication to the Council 'Safeguarding the conditions for a successful 1992 - The economic outlook and policy problems for 1989 and 1990', prepared in accordance with Article 2 of the Council Decision of 18 February 1974 on convergence.

Belgium (B)

22.2 The central bank raises the rates for one-, two- and three-month Treasury certificates in five stages, taking the one-month rate from 7.40 % to 7.80 %.

Denmark (DK)

9.2 The Nationalbank lowers the limit for banks' drawing on current account without the provision of collateral from 15 % to 10 % of a bank's capital base.

Federal Republic of Germany (D)

None.

Greece (GR)

3.2 The issuing institution authorizes foreign banks in Greece to engage in swap operations in which foreign currencies are exchanged for drachmas. The foreign exchange directorate is given responsibility for setting the terms for these operations.

Spain (E)

31.1 The Bank of Spain raises the compulsory reserve ratio for financial institutions by 1.5 of a percentage point. On 14 January, the Government approves the progressive reduction of the compulsory investment ratio for financial institutions with a view to bringing it to an end on 1 January 1993. In addition, firms which borrow abroad are required to make a prior deposit of 30 % of the sum involved, while banks are required to deposit 20 %.

2.2 The Treasury raises by half a point the interest rate on issues of its twelve-month securities.

3.2 The Bank of Spain raises its money market intervention rates by 1 percentage point for overnight loans to the bank and by 0.5 of a percentage point for three month 'repurchase' operations on Treasury paper.

France (F)

6.2 The Government freezes FF 10 billion in budget appropriations. This measure will have the effect of freezing 5 % of the programme authorizations opened by the Finance Law for 1989, the corresponding payment appropriations and all administrative and intervention appropriations, except for appropriations for assessment, appropriations earmarked for the public debt, for allocations to the public authorities and for staff expenditure. The procedure also excludes appropriations for the national education system, official development assistance and the commitments entered into by the State in connection with planning agreements.

Ireland (IRL)

None.

Italy (I)

3.2 Agreement between the Government and the trade unions on the amendment of the decree containing most of the tax measures in the 1989 Finance Law:

— protection against fiscal drag: with effect from January 1990, the Government has promised to adjust tax rates fully in line with inflation if it exceeds 2 % in any year, so that fiscal drag is completely neutralized;

— in exchange, the trade unions have conceded that the impact of the 2 %-4 % increase in VAT rates on 1 January 1989 should not be reflected in the wage indexation system;

— other points in the agreement: more effective measures against tax evasion and avoidance; a Government commitment to present proposals by May 1989 for the taxation of income from investment and financial assets (excluding Government securities); the reform of taxes on immovable property under the 1990 Finance Law; the reduction of deductible expenses.

17.2 The Minister for the Treasury decides that with effect from 1 March 1989 net increases in foreign currency deposits with banks will be subject to a 25 % compulsory reserve.

17.2 With effect from the end-February auction, the competitive auction method, which has been used for three-month securities since February 1988, will be extended to six— and twelve-month Treasury bills. It will now be up to the market to set the issue price for securities, with the Treasury intervening only if the rates offered prove genuinely incompatible with its policy for financing the Treasury.

Luxembourg (L)

27.1 The Government adopts a draft law increasing family allowances by between LFR 220 and LFR 966 a month, depending on the number of children.

16.2 Adoption of the law which increases private sector pensions by 3.55 %, with effect from 1 January 1989.

Netherlands (NL)

2.2 Parliament adopts the draft law simplifying the tax system and reducing the top rate of tax from 72 % to 60 %. The new system, which will enter into force on 1 January 1990, will consist of no more than three tax bands.

7.2 The Nederlandsche Bank raises the rate for special advances from 5.9 % to 6.25 % in two stages.

16.2 Entry into force of the law introducing penalties for insider dealing offences involving stock market operations.

Portugal (P)

16.2 The Government sets the conditions for the first partial privatization (49 % of the Unicer brewery), and enables workers and small savers to purchase shares on special terms.

United Kingdom (UK)

None.

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