ISSN 0379-0991

EUROPEAN ECONOMY

COMMISSION OF THE EUROPEAN COMMUNITIES • DIRECTORATE-GENERAL FOR ECONOMIC AND FINANCIAL AFFAIRS

Economic trends and prospects

Budgetary systems and procedures
Industrial labour costs
Greek capital markets

No 15 March 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 — 'Recent 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 September.

— Series C — 'Consumer survey results' reports on the consumer survey, which is carried out thrice yearly (in January, May and October) throughout the Community (except Greece and Luxembourg) and measures consumers' opinion on the economic situation and outlook.

Subscription terms are shown on the back cover and the addresses of the sales offices are shown on page 3 of the cover.

Unless otherwise indicated the texts are published on the responsibility of the Directorate-General for Economic and Financial Affairs of the Commission of the European Communities, rue de la Loi 200, 1049 Brussels, to which enquiries other than those related to sales and subscriptions should be addressed.

Commission of the European Communities
Commission des Communautés européennes

CORRIGENDUM

European Economy No 15 — March 1983

The economies of Member States — United Kingdom

page 78, The second line of the table relating to unemployment should read 'percentage of which:'

page 84, Graph 3: The words 'import' and 'export' on the graph itself should be disregarded.

Économie européenne n° 15 — mars 1983

Les économies des pays membres — Royaume-Uni

page 90, graphique 3: Les indications « import » et « export » sont sans objet.

Commission of the European Communities

EUROPEAN ECONOMY

March 1983

Number 15

The manuscript was completed in March 1983.

Printed in Belgium, 1983

Catalogue number: CB-AR-83-015-EN-C

Contents

Economic trends and prospects 5

The Community economy 9

The economies of Member States 21

Special studies

Budgetary systems and procedures for the central government budget in the Community Member States 87

Unit labour costs in manufacturing industry and in the economy as a whole 125

Financial markets and institutions in Greece 145

List of contents of European Economy Nos 1 to 14 157

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 countries of the European Community
EC 4	Federal Republic of Germany, France, Italy, United Kingdom
EC 9	European 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.

BIS	Bank for International Settlements
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)
GAB	General Agreement to Borrow
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
∅	Average

Economic trends and prospects

Contents

The Community economy 9

Introduction 9

World activity, trade and payments 9

The Community: trends and prospects 13

Problems of economic policy 16

— International debt and less developed countries 19

The economies of Member States 21

Belgium 21

— Wage moderation and reductions in working hours in the Benelux countries 26

Denmark 29

Federal Republic of Germany 34

— Growth potential and structural adjustment in the Federal Republic of Germany 40

Greece 44

France 48

Ireland 54

Italy 59

— Italian monetary policy: from the bypassing of the banks to the return to indirect credit controls 65

Luxembourg 68

The Netherlands 72

United Kingdom 77

— Price competitiveness and trade in manufactured goods 83

List of tables

1. Major supply and demand components, EC 4 9

2. World GDP and trade 11

3. World export price developments 11

4. EC 10: Supply and uses of goods and services together with main economic indicators, 1971-83 15

The Community economy

Introduction

A comprehensive review of the short-term and medium-term economic outlook drawn up by Commission departments in September and October 1982 was published in *European Economy* No 14. It was hoped at that time that the Community would emerge from the recession during the second half of 1982, but in fact a sharp contraction in world trade and a decline in business confidence led, in the third quarter of 1982, to a decline in output not only in the Community but also in most of the industrialized countries.

These developments are largely attributable to problems caused by the increasing debt of developing countries and the rapid reduction in the capacity of absorption of the OPEC countries; but they were also due to continuing high interest rates and to exchange rate instability.

As the data (still incomplete) for the fourth quarter of 1982 show (Table 1), Community gross domestic product has more or less stabilized; it is reasonable to expect that economic activity will return to a rising trend during the first half of 1983.

In this respect, the positive factors outweigh in both quantity and quality the negative factors. The former include the improved outlook for world trade, the decline in oil prices, continuing disinflation, the fairly low level of stocks, the improved balance of payments and the easier monetary situation; the latter include consumer and investor reticence, continuing high real interest rates, and constraints exercised by budget and balance-of-payments problems in some countries. All in all, the conditions are now more favourable for renewed expansion. Fears of a further flare-up in inflation, problems of global debt and structural imbalance in many countries may however attenuate or even seriously hamper the upswing.

The last section of the chapter on the Community, and the corresponding sections of the country chapters, highlight the problems to be solved and the obstacles to be overcome on the road to a more lasting and balanced growth in the Community.

World activity, trade and payments

1982 was to have been a year of economic recovery. At the beginning of the year, most international organizations were forecasting the growth of GDP in industrial countries at 1%, with a pick-up in the second half of the year and growth in the volume of world trade of the order of 3%. There was an improvement in business confidence; non-oil commodity prices were low; inflation was expected to drift downward under the influence of weak labour market conditions and

Table 1

Major supply and demand components, EC 4

(% change over preceding period, annual rates; seasonally adjusted)

		GDP [1]	Imports [2]	Exports [2]	Foreign balance [1, 2]	Domestic demand	Change in stocks [3]	Final domestic demand	Gross fixed investment	Government consumption	Private consumption
1980	I	3,8	10,4	12,1	0,4	3,4	−0,6	4,1	2,5	3,2	4,9
	II	−5,0	−6,5	−10,6	−1,1	−3,9	0,3	−4,3	−7,0	1,7	−5,0
	III	−2,7	−5,9	−5,8	0,1	−2,7	−4,5	1,9	−1,9	2,5	3,0
	IV	1,3	−1,9	0,9	0,8	0,5	−0,2	0,8	0,8	0,1	1,0
1981	I	0,9	−0,7	8,1	2,3	−1,3	−0,2	−0,2	−10,0	5,6	0,0
	II	−2,0	−1,8	12,3	3,7	−5,5	−4,2	−1,4	−0,3	−4,6	−0,8
	III	−0,8	11,9	12,6	0,3	−1,1	−2,8	1,8	−1,2	4,3	2,1
	IV	4,5	3,0	10,8	2,2	2,4	3,0	−0,7	−4,5	−1,5	0,9
1982	I	0,8	7,8	−4,8	−3,5	4,5	4,4	0,0	−7,4	4,8	1,1
	II	−0,9	0,2	−5,4	−1,6	0,8	1,4	−0,6	2,5	−1,2	−1,4
	III	−4,6	−12,2	−8,0	1,2	−5,8	−6,0	0,2	−2,7	2,3	0,5

1 Federal Republic of Germany: GNP.
2 Goods and services; including intra-Community trade; FR of Germany: including factor incomes.
3 Change over previous period as % of previous period's GDP.

Source: Estimates by the Commission services based on national accounts data for the Federal Republic of Germany, France, Italy and the United Kingdom.

firm monetary policies. By mid-year, expectations had to be revised. In the first half of the year commodity prices had declined further and exports of oil from OPEC countries continued to fall. Interest rates remained high, however, and contributed to the liquidity crisis which became acute in early summer, when certain major finance houses failed, to be followed in July by Mexico's request for a moratorium on interest payments on its external debt. Thereafter, as fears for the world financial system induced a mood of caution in the banks faced with lending requests from developing countries, the request for renegotiation came in from Argentina, Brazil, Yugoslavia and Romania. Meanwhile, the exports of industrial countries to the developing countries had begun to decline.

Internal demand remained weak on both sides of the Atlantic until the end of the year. The downward trend in world trade continued almost to the end of 1982, and first estimates indicate a year-on-year fall in merchandise trade of the order of 7% in US dollar value, and 2% in volume.

The present situation has encouraging factors but gives no grounds for optimism. By comparison with the beginning of 1982, nominal interest rates and commodity prices are now lower, and oil prices fell appreciably in February 1983. Stocks are low in industrial countries and consumption has been under restraint for some time past. Although nominal interest rates receded in the second half of 1982, inflationary expectations have declined also, so that real interest rates now remain considerably above the level at which previous recoveries have commenced. Some of the debt problems of developing countries have been eased by the intervention of the International Monetary Fund and by the efforts of central banks in organizing the continuation and extension of syndicated lending, but the conditions under which agreements have been reached will inevitably limit the market opportunities of exporting countries in Latin America, in Eastern Europe, and in many parts of the developing world. In both the Community and the United States the unemployment rate stands at 10% or more, so that uncertainty in both the labour market and the financial market is retarding a return of consumer confidence. Furthermore, many of the problems of European countries are due to structural imbalances in public finance and industrial organization for which long-term corrective measures, often painful, are required. Countries which have already set a programme of structural change in motion find difficulty in modifying it. Thus, although 1983 may produce the long-awaited recovery, the process of recovery itself is likely to be cautious and tentative.

In 1983 the major sources of uncertainty are the prospects for oil prices, shifts in the economic policy of major countries, and problems arising from global indebtedness.

Substitution, energy-saving measures and, more recently, the weakening of activity in industrial countries, have led to the appearance of excess supply conditions on the world oil market. In 1982 the downward trend in consumption was reinforced by a large reduction in stocks. World demand for oil declined, on average, by 4,5% per year from 52,1 million barrels per day (mbd) in 1979 to 45,4 mbd in 1982. However, as non-OPEC countries have increased supply in response to higher prices, the demand for oil from OPEC members has fallen even more precipitously, from 31,4 mbd to 19,3 mbd over the same period, an average of 15% per year. Although OPEC attempted to maintain the general level of its prices by assigning output quotas, not all OPEC member countries have respected them. Oil prices have therefore fallen as a result of selective changes in official prices, discounts and lower spot prices. The combined effect of lower volumes and falling prices on OPEC members' export earnings caused many of them to review their development plans and to introduce measures designed to curtail their imports. Nevertheless, OPEC's current account surplus (which reached USD 115 000 million in 1980) disappeared in 1982. During the year, a conflict arose within OPEC between the low absorbers of imports (Saudi Arabia and the Gulf States) and the high absorbers (Venezuela, Iran, Libya, Nigeria, etc.), the former being determined to maintain the market price of USD 34 per barrel, and the latter to maintain oil revenue, if necessary by cutting prices to improve their share of the export market. In effect, Saudi Arabia became the marginal producer, and the volume of its exports declined from 9 mbd to less than 6 mbd in consequence. Early in 1983, the delay in the recovery of industrial activity, the unusually mild winter and the failure of OPEC to agree on a credible pricing and output strategy, increased expectations of a further price cut. After North Sea producers and Nigeria had reacted to company pressure and lowered their prices, Saudi Arabia initiated discussions with other OPEC members and non-OPEC producers in an attempt to prevent a price-cutting war. Agreement was eventually reached on a new marker price for Arabian light of USD 29 per barrel together with a revised scale of differentials and a set of output quotas.

The prices of primary commodities, the principal source of export earnings for many developing countries, have declined since the beginning of 1981, as the recession has gathered force in industrial countries. Thus both oil-producing countries and non-oil primary producers suffered a cut-back in export earnings. Non-oil developing countries, faced with deteriorating terms of trade and substantially higher debt servicing costs have been obliged to reduce their imports, including imports of capital goods, with damaging consequences for their long-term rates of growth. Thus the deterioration in the OPEC external position was partly offset by improvements in the situation of the non-oil developing countries, with the balance of industrial countries remaining

Table 2

World GDP and trade

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

	1978	1979	1980	1981	1982	1983 [2]	1980	1981		1982		1983 [2]	
							II	I	II	I	II	I	II
GDP or GNP, OECD total	3,8	3,2	1,3	−1,4	−0,3	1,2	−0,3	1,8	0,5	−0,8	0,0	1,3	2,4
Imports of goods (volume)													
World	6,9	7,0	2,2	2,0	−2,1	0,4	−2,9	3,0	3,0	−3,1	−5,0	1,6	3,5
EC 10 [1]	5,8	10,6	1,9	−2,8	1,4	0,8	−7,8	−6,0	4,0	4,5	−7,0	3,1	4,0
World excluding EC	7,6	5,0	2,4	4,7	−3,9	0,2	−0,1	8,2	2,4	−6,9	−3,9	0,8	3,2
of which:													
OECD excluding EC	7,2	6,5	−1,5	0,8	−2,8	2,1	−5,3	4,9	2,3	−6,4	−0,7	2,4	4,5
OPEC	5,0	−12,0	12,0	27,4	−1,1	−4,5	13,0	37,6	20,2	−5,9	−9,7	−4,0	0,0
Other developing countries	8,0	11,0	6,0	5,5	−7,5	−2,9	4,4	7,7	−1,7	−9,7	−8,7	−2,3	2,1
Other countries	10,0	2,0	3,8	1,5	−3,8	2,1	2,5	2,0	−3,0	−5,3	−1,6	3,3	3,4
Exports of goods													
EC total [1]	5,0	7,4	2,7	3,5	0,8	1,5	−5,2	6,3	9,0	−0,7	−2,0	2,7	4,3

[1] Including intra-EC trade.
[2] Forecasts.
Source: OECD, IMF and Commission services.

Table 3

World export price developments

(% change over previous period, annual rate - USD)

	1978	1979	1980	1981	1982	1980	1981		1982	
						II	I	II	I	II
Fuel	0,6	39,7	67,7	10,7	−3,8	13,0	14,9	0,9	−6,8	−2,4
Food	1,3	12,9	16,8	−11,1	−10,8	11,9	−17,2	−18,8	−3,7	−15,5
Other primary products	4,8	21,7	8,6	−8,3	−9,4	2,3	−10,4	−14,3	−5,8	−11,4
Total primary products (excluding fuels)	3,0	17,1	12,7	−9,8	−10,1	7,2	−14,0	−16,7	−4,8	−13,5
Total primary products (including fuels)	1,9	27,5	40,5	2,6	−6,0	10,7	3,0	−5,6	−6,1	−6,2
Manufactured goods [1] (unit value)	13,6	11,8	9,6	5,2	2,7	11,8	3,5	2,4	6,6	−4,6

[1] Non-EC developed countries.
Source: United Nations and Commission services.

virtually unchanged.[1] The reaction of the major individual countries varied, however, with the current balance-of-payments position deteriorating in the United States, the United Kingdom and France, and improving in Japan, the Federal Republic of Germany, Italy and a number of smaller industrial countries.

In the United States, until mid-1982, a relaxed budgetary policy designed to promote growth and structural change was operated alongside a strict monetary policy based on money supply targets, conducted with the aim of reducing inflation. The resultant rise in interest rates attracted capital movements and obliged other countries to combat capital outflow by raising their interest rates in parallel. In the second half of 1982, after a period of falling inflation, low growth, and increasing liquidity problems among banks and industrial companies in the United States, the Federal Reserve Board signalled an easing of monetary policy; thus the Federal funds rate was reduced from 12% to 9% between July and October 1982. The Administration and Congress began to tighten budgetary policy by introducing measures to increase taxation. Nevertheless, the Federal deficit in the present fiscal year is expected to exceed USD 200 000 million (about 6% of GDP).

The prospects of a recovery of the United States economy in 1983 are more firmly based than in the 'false dawn' of 1982. Interest rates are lower, but owing to the fall in inflation, real interest rates—more than 4% on three-month Treasury Bills and 6,5% on long-term bonds, calculated on the basis of current inflation—need to fall even further if recovery is to be ensured. Attempts are being made to reduce the imbalance in public finance which showed signs of slipping out of control in 1982. The President's draft budget for the fiscal year commencing October 1983 contains proposals for the limitation of public expenditure and stand-by tax measures, to be triggered if the budget deficit continues above USD 160 000 million in the year commencing October 1985. It is now admitted, however, that the Federal deficit is largely structural and will not disappear automatically as economic activity increases. Thus further measures are likely to be required if the deficit is to be reduced and a low interest rate regime ensured. There are uncertain indications of a recovery of internal demand. In view of the low level of capacity utilization, less than 70%, and the high unemployment rate, over 10%, real activity can increase substantially before internal pressures start to push inflation higher. Nevertheless, short-term interest rates have begun to edge upwards, confidence remains low and there are still anxieties about parts of the banking system. For these reasons the recovery in GDP growth is expected to be slow, but to improve gradually to about 3½% at annual rates in the final quarter of 1983.

Japan has in the past relied on exports as the motor of economic growth, but in 1982 a fall of 4% in export volume occurred, notwithstanding the weakness of the yen. The Japanese authorities attempted to counterbalance the fall in external demand by encouraging an increase in private consumption, permitting a real wage increase in the private sector of the order of 3% in the spring of 1982, and by introducing a front-loaded programme of public works in April. At the same time current budgetary expenditure was strictly limited because of anxieties about the size of the budget deficit.

According to present estimates Japanese exports will not be particularly dynamic in 1983, given among other things the modest outlook for world trade and the appreciating trend of the yen. The room for manœuvre in public finance is very limited, as almost any increase in public expenditure has to be met by borrowing. Wage increases in 1983 are likely to be moderate, of the order of 5% nominal. GNP is expected to increase by 3 to 3½%, year on year.

The Western European countries outside the Community suffered a decline in exports in 1982, but whereas Switzerland and Austria have maintained low inflation and strong exchange rates at some sacrifice in short-term growth, most of the remaining countries in Scandinavia and Iberia have preferred more expansionary policies, compensating for the loss of competitiveness due to higher inflation by varying degrees of devaluation. Their prospects for 1983 depend largely on the degree of recovery within the Community itself.

The liquidity problems of a number of heavily indebted South American and East European countries (see box) dominated the world economic scene in the latter half of 1982, as their creditworthiness was sapped by a fall in the price of primary commodities, reduced world demand and high interest rates. The fears of a world economic crisis were for a time acute, but diminished as arrangements for rescuing individual countries, involving governments, central banks and commercial banks, were developed under the aegis of the International Monetary Fund. Nevertheless, as a substantial reduction of internal demand by the debtor nation is usually included in borrowing conditions, the continuance of indebtedness also implies a dampening of world trade.

For commercial banks this form of lending involves assuming a degree of exposure which would formerly not have been acceptable. Their acquiescence has only been obtained by the spreading of the risk, the guarantee of IMF supervision and the threat of increasing dangers for the stability of the world banking network.

[1] The statistical problem of reallocation of the fall in the OPEC external balance has not been fully solved. Thus the asymmetry in the world current balance table increased substantially between 1981 and 1982.

The constraints under which the world economic system is now working do not preclude all grounds for optimism. The drop in inflation and the swift reduction in interest rates will lighten the debt servicing problems of the indebted nations, although real interest rates remain too high to encourage rapid recovery in industrial countries.

For most of 1982, the interest rate differential between the United States and other countries was the dominating influence on the trend of exchange rates. After the fall in the United States short-term rate in the autumn, competitivity in world markets assumed greater importance; the yen appreciated strongly and the United States dollar and the pound sterling moved downwards against the main currencies of the European Monetary System. In the coming year it seems probable that the relationship between the dollar, the Deutschmark and the yen will be relatively stable.

All in all, world trade appears to have ceased to fall at the end of 1982, and imports are forecast to be increasing at a more normal annual rate of 6% in the USA and Japan and 4% in the Community by the second half of 1983. For certain developing countries the process of recovery is likely to be longer, because of the persistence of credit problems. The increase in demand from industrial countries should be enough to arrest the fall in the prices of primary commodities, other than oil, which should increase slightly well before the end of the year. Thus the balance-of-payments position of the developing countries should improve, together with those of the Community and Japan. On the other hand, the USA is expected to show a substantial increase in its balance-of-payments deficit.

The Community: trends and prospects

The recession in the Community economy which started in the spring of 1980 has, by early 1983, already persisted for almost three years. 1982 was a year of depressed output and steadily rising unemployment. Some tentative signs of a slight upturn in activity in the Community early in 1982 fed hopes that there would be a strengthening of this trend in the second half of the year. Instead the worsening world trade picture and a renewed weakening of business confidence and domestic demand led to a further fall in real output. National accounts data for the four largest Member States (the Federal Republic of Germany, France, Italy and the United Kingdom) show a decline in their real gross domestic product in the third quarter of 1982 of 4,6% (at a seasonally adjusted annual rate), bringing the level of real gross domestic product back once again to the low point previously reached in the third quarter of 1980. Detailed figures are not yet available for the fourth quarter of 1982, but it seems likely that, at best, output stagnated at this low level.

Commission estimates for the whole of the Community in the second half of 1982 suggest that real gross domestic product fell at an annual rate of 2,0% compared with the first half (see Table 4). A major contribution to this decline came from a large swing in stockbuilding; in the first half of the year there had been substantial (although in part, perhaps, involuntary) additions to stocks, while in the second half stocks were run down again to bring them closer into line with the depressed levels of output and demand. Fixed investment again declined sharply in the second half and there was a modest reduction in the volume of general government consumption. Private consumption was the only component of domestic demand not to fall in this period.

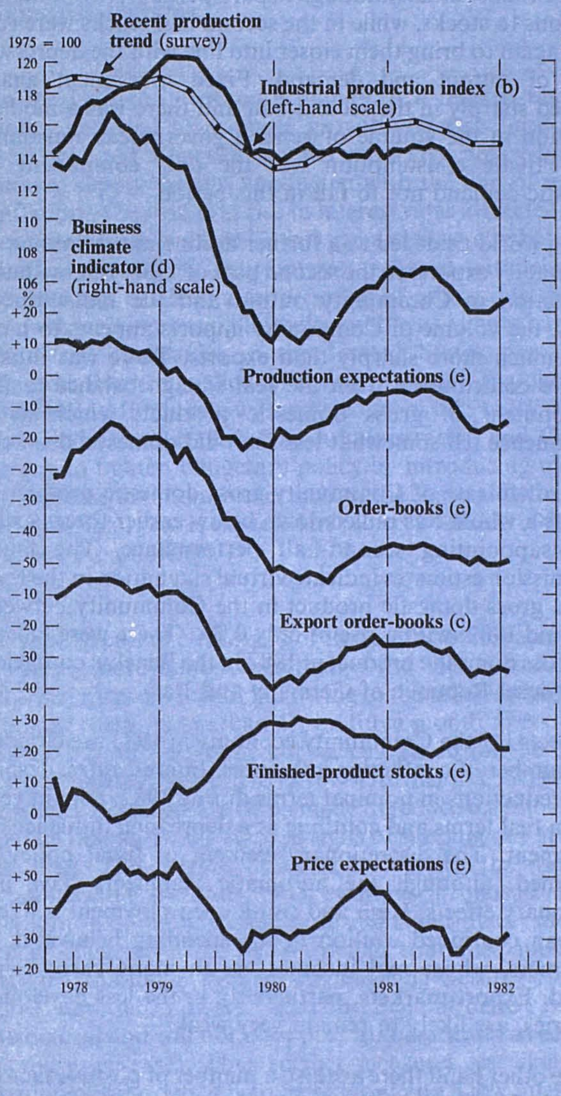
Falling world trade led to a further decline in the volume of Community exports in the second part of 1982. But, with the contraction in Community output and the reduction in stocks, the volume of Community imports appears to have fallen much more sharply than exports. There was thus a positive contribution from the real foreign balance to the development of gross domestic product, which as a consequence fell somewhat less than did domestic demand.

The growth rate of Community gross domestic product in 1982 as a whole was pulled down below earlier forecasts by the disappointing second-half performance. The latest Commission estimates indicate virtual stagnation in the level of real gross domestic product in the Community between 1981 and 1982, with a rise of only 0,2%. There were falls in real gross domestic product in 1982 in the Benelux countries, the Federal Republic of Germany and Italy.

Prospects for the Community economy in 1983 are clouded by a number of conflicting influences. Interest rates, despite some reductions in nominal terms during 1982, remain very high in real terms and continue as a depressing influence on investment. The discretionary element of fiscal policy is restrained, although the automatic stabilizers have expansionary effects. High and rising unemployment is likely to mean continued caution in the spending behaviour of consumers, whose real incomes are in many cases being eroded. Export markets, particularly in the less developed countries, are likely to remain very weak.

On the other hand there are also a number of positive factors at work. International prospects look generally somewhat brighter. Inflation is still coming down within the Community, and this achievement of greater stability may help to engender more confidence among both consumers and investors. The low level of investment and of consumption of durables in recent years will lead in due course to a rise in replacement demand, which could be encouraged if there are further falls in interest rates. Similarly, stock levels have declined substantially and will need to be rebuilt once recovery does get under way. Finally, the recent weakness of the price of oil should have a beneficial effect on both inflation and growth in the Community.

GRAPH: **Business survey indicators for manufacturing industry and the index of industrial production, EC 9** (a)



(a) Weighted total of available country data.
(b) Industrial production excluding building and construction and, in the case of France, the foodstuffs and beverages industry. Three-month moving average.
(c) The last section of this curve represents the recent production trend (in December 1981 and January 1982) in the Community with the exclusion of Denmark, Greece and the United Kingdom, for which data are not available.
(d) Composite indicator based on the replies to the questions on production expectations and stocks of finished products. The indicator is an average of the net balances, i.e. differences between the percentages of respondents giving positive and negative replies.
(e) Net balances, i.e. differences between the percentages of respondents giving positive and negative replies.

Source: European Community business surveys and Eurostat.

The latest evidence from the Commission's business surveys is mildly encouraging. After deteriorating sharply in the summer and early autumn of 1982 business sentiment stabilized in the final months of the year and then, according to first results for January 1983, started to improve. In January the production expectations of chief executives in industry became less pessimistic by 2% on balance, and there were signs of improvements in new orders and in expectations about export orders, especially in the Federal Republic of Germany. The economic sentiment indicator (a broad indicator of economic expectations in the Community based on the surveys of consumers, heads of business enterprises in industry and construction and on stock exchange prices) improved by 0,5% in January 1983, following three months of stability at a very low level.

On balance it is expected that positive factors will become progressively dominant, and the growth of activity in the Community should gradually resume during 1983. The latest Commission forecasts show Community real gross domestic product rising in the second half of 1983 at an annual rate of a little over 2% (see Table 4). The year-on-year growth in 1983 is likely to remain very modest, however, because of the fall in output in the second half of 1982; a rise of only 0,4% is forecast for 1983 as a whole. All the countries of the Community are expected to be showing some growth in real output by the second half of 1983, but year-on-year growth could be marginally negative in Belgium, the Federal Republic of Germany, Italy and Luxembourg. Only the United Kingdom and Ireland are forecast to have a positive annual growth rate above 1%.

Among the components of demand in the Community, private consumption is expected to remain almost flat throughout 1983, since, despite falling inflation rates, real disposable incomes are likely to show only small gains and household savings ratios will remain high while labour market conditions remain difficult. Real government consumption expenditures will also rise only very slowly, and will not give much of a stimulus to the growth of demand. After very steep falls in 1981 and 1982, fixed investment is expected to stabilize in the first half of 1983 and then to start growing slowly, although residential construction investment is likely to remain weak in most countries. Comparing 1983 as a whole with 1982 the level of real fixed investment is still expected to show a slight fall. The reduction of stocks is likely to come to an end early in 1983, and additions to stocks in the second half should make a noticeable contribution to the growth of output.

The gradual recovery which is expected in the volume of world trade should allow Community exports to expand at a relatively slow but gradually accelerating pace during 1983. Some further small gains in export market shares are to be expected for several Community countries, but these are unlikely to be on the same scale as the gains made in 1981 and

Table 4

EC 10: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)				
	1971-80	1981	1982 [3]	1983 [4]	1981	1982 [3]		1983 [4]	
					II	I	II	I	II
	% change over preceding period at annual rate — at constant 1975 prices and PPS								
Private consumption	3,2	0,2	0,1	0,1	0,6	−0,1	0,3	0,1	0,2
Government consumption	3,0	1,5	0,8	0,6	0,9	1,7	−0,4	0,7	0,9
Gross fixed capital formation	1,6	−4,7	−3,0	−0,4	−2,6	−2,9	−3,7	0.0	2,7
Change in stocks [1]	1,2	−0,1	0,5	0,6	−0,6	1,2	−0,4	0.0	0,7
Domestic demand	2,8	−2,1	0,2	0,2	−1,2	2,6	−2,9	0,9	2,0
Exports of goods and services	6,0	3,8	0,8	1,5	9,2	−0,7	−2,0	2,7	4,5
Imports of goods and services	5,4	−2,2	1,4	0,8	4,1	4,5	−7,0	3,1	4,1
GDP at market prices	2,9	−0,4	0,2	0,4	1,1	1,2	−2,0	0,8	2,1
	% change over preceding period at annual rates								
GDP at current prices	13,0	10,1	10,7	9,1	10,6	11,5	7,5	9,9	10,4
Industrial production	2,4	−2,1	−1,5	−0,5	0,5	−0,3	−4,7	0,7	2,3
Unemployment rate [2]	4,2	7,9	9,6	10,6	8,2	9,1	9,7	10,3	10,7
Compensation of employees per capita	13,3	11,5	10,6	8,3	12,7	10,7	10,3	8,6	8,0
GDP (implicit price index)	9,8	10,6	10,5	8,6	9,4	10,2	9,7	9,0	8,1
Private consumption (implicit price index)	9,7	11,8	10,5	8,6	11,3	10,7	10,1	8,9	8,0
	as % of gross domestic product								
Trade balance (fob/cif)	−0,9	−1,8	−1,3	−0,9	:	:	:	:	:
Current balance	−0,1	−0,8	−0,5	−0,3	:	:	:	:	:
Net borrowing of general government	2,8	4,8	5,0	5,0	:	:	:	:	:

1 As % of GDP.
2 Unemployment as % of civilian labour force.
3 Estimates.
4 Forecasts.

Source: Eurostat and Commission services.

1982 when Community export prices became much more competitive because of the appreciation of the dollar. A rise in Community imports should accompany the revival in domestic activity. In the two halves of 1983 the volume of imports is expected to rise at a similar rate to the volume of exports, and so the real foreign balance will not make an appreciable contribution to the growth of gross domestic product.

It should be emphasized that these forecasts, which were established in the latter part of January 1983 and the beginning of February, are based on an oil price assumption which takes into account only a small reduction. A larger fall in oil prices, which seems to be taking place, as well as easing inflation, will give some positive impulse to real demand, output and trade in the Community and in the developed countries as a whole on top of the gradual recovery already forecast.

Unemployment in the Community continued to climb throughout 1982, and by December the number of unemployed (EC 9) had reached a seasonally adjusted level of

11,7 million, representing 10,4% of the civilian labour force. The outlook for the labour market in 1983 remains unfavourable, despite the expected gradual upturn in activity. Total employment in the Community is likely to decline for the fourth consecutive year in 1983, taking it to a level about 3% lower than in 1979. Since the labour force will keep on rising, unemployment will increase further, although at a slower rate than in 1981 and 1982. The average number of unemployed in the Community as a whole in 1983 is expected to exceed 12 million, and the unemployment rate will still be rising in the second half of the year. All the member countries are likely to see a further rise in unemployment in 1983, and particularly sharp increases compared with the average for 1982 are expected for the Netherlands, Ireland, the Federal Republic of Germany and Belgium. Average unemployment rates (on an SOEC harmonized basis) in 1983 are expected to reach as high as 15,4% in Belgium, 14,7% in Ireland, 13,3% in the Netherlands and 12,2% in the United Kingdom.

Considerable progress was made in reducing inflation in the Community during 1982. Falling commodity prices slowed the rise in import prices, despite the continued strength of the US dollar against Community currencies throughout most of 1982. The depressed domestic economy within the Community exerted downward pressure on wage bargains and profit margins. As a consequence the rise in the price deflator of private consumption for the Community as a whole slowed from 11,8% in 1981 to 10,5% in 1982. Some factors should help towards a further slowdown in inflation in 1983.

Although the fall in commodity prices is expected to come to an end, the rise in the prices of manufactured goods exported by the developed countries should remain moderate, so import price pressures for the Community should lessen once more. The rise in the compensation of employees per capita is also expected to slow further. As a result the price deflator of private consumption in the Community is expected to rise by some 8,6% in 1983. Because of the recent devaluation of the drachma, a rise in consumer price inflation is expected for Greece, but all the other Community countries are expected to share in the slowing in inflation. There should also be some narrowing in the dispersion of inflation rates within the Community, although differences in 1983 will still remain considerable, the forecasts ranging from 3,0% in the Netherlands and 3,7% in the Federal Republic of Germany to 12,0% in Ireland, 14,0% in Italy and 22% in Greece.

Progress has also been achieved in re-establishing external balance. The Community's trade balance, in heavy deficit in 1980 because of the oil price rise, has narrowed steadily since then, a process which is expected to continue in 1983, when there should be small gains on both trade volumes and the terms of trade. The Community's deficit on current account should show a similar improvement, and should be almost in balance in 1983, compared with a deficit equivalent to 1,3% of gross domestic product in 1980. The Netherlands, the Federal Republic of Germany and the United Kingdom are expected to remain in current account surplus in 1983, while the other Member States in current account deficit should all see some improvement in their position.

Problems of economic policy

These prospects are moderately encouraging from several points of view: the probability of a recovery of activity, continued disinflation, and the relaxation of balance-of-payments constraints. However, unemployment continues to increase so that the risk that the world recession may last, or even deepen, and the means of dealing with such a situation, deserve special attention.

In trying to define the best macro-economic policy mix in the main industrialized countries in 1983, it is immediately obvious that the conditions in which these policies must be implemented are far from ideal.

One of the main problems is that the progress made towards controlling inflation is yet to be consolidated. This applies in particular to the United States, where the conditions for a spontaneous recovery of economic activity seem perhaps slightly more probable than in Europe, but where this recovery would increase the problems associated with the large deficit of the Federal budget (even allowing for its effects on public revenue), which make it very difficult to implement a non-inflationary monetary policy in the context of renewed economic expansion.

Domestic and US interest rates and rates on international markets could be very different depending on whether or not the United States succeeds in reducing this deficit substantially, and consequently the exchange rate of the US dollar and monetary policy in the European countries would be strongly influenced.

In Japan too, the public finance situation is still giving cause for concern. It exercises constraints on economic policy that affect not only Japan's imports but also—and especially—the exchange rate of the yen and thus the competitiveness of Japanese industry and the current balance-of-payments surplus.

The recent decline in oil prices seems likely to be a positive factor for both growth and disinflation in the industrial countries and in some developing countries. It would be preferable for oil prices not to fall too far in the longer term, however, for such a development could affect investment projects involving alternative energy sources as well as projects to find new sources of oil. This could lead to marked instability in the volume of output or the price of oil, and affect the conditions for exploiting other energy sources, eventually producing pronounced cyclical swings, that could endanger medium-term growth.

This general overview highlights the importance, in 1983, of closer cooperation between the Community and the main industrialized countries. If cooperation is to be effective, it must aim, not so much at regulating the trend of exchange rates for the principal currencies through market interventions by the central banks (however necessary such intervention may be in certain circumstances), but rather at implementing policies geared to improving convergence between the 'fundamentals' of the economies concerned. Such efforts would make it possible to prevent the recurrence of violent fluctuations of the major international currencies, like those of recent years.

The trend of the US dollar against the ECU deserves special attention. The deterioration of the current external balance, which began in 1982, may be expected to induce a weakening of the dollar. There are, however, factors pushing in the opposite direction notably interest rate differentials, expectations, political events and the size of recycling. It is difficult to predict how they will interact in 1983, but it is to be hoped that the stance and mix of the US economic policy will be tailored to achieving greater stability.

A decline in the rate of the US dollar against the ECU, like falling oil prices, should on the whole be a positive factor for the Community; but too sharp a drop, as with oil prices, would lead to instability with the ensuing unwelcome effects.

The financial situation of the developing countries calls for appropriate arrangements to avoid the kind of crisis experienced in 1982, even in the event that these countries could count on firmer demand trends stemming from the industrialized countries.

As the box on 'International debt and less developed countries' shows, it would be far better to reinforce combined operations by the national and international authorities and the commercial banks, to prevent embarrassing financial situations in the lender countries, and to ensure that developing countries have access to financing on terms compatible with adjusting their external financial position while avoiding a downturn in activity. The enlargement of the General Agreement to Borrow (GAB) and the increase in the means available to the International Monetary Fund due to the rise in quotas contribute substantially to solving this problem.

The most favourable combination of conditions described above would place the Community in 1983 in a context of more dynamic world trade, relatively stable raw material prices, international interest rate trends that allow for less strict monetary policy, and more stable international monetary relations and world financial markets.

Such conditions would certainly enlarge the scope for economic policy to ensure the recovery of economic activity in the Community, and consequently strengthen the upswing on a world-wide scale.

The room for manœuvre varies in extent from one country to another, however. It is narrow, or even non-existent, in the Community countries that are still subject to powerful budget or balance-of-payments constraints: their economic policy stance will have to remain very cautious. Only at a later stage, when world activity has recovered, may some relaxation be envisaged.

Moreover, in this case, it would be preferable to leave as much leeway as possible for external disinflationary impulses, and to channel extra real resources to priority investments required for economic restructuring, the most pressing problem in the countries concerned.

In the other Community countries, where more headway has been made with controlling inflation, the scope for monetary policy manœuvre is wider than that for fiscal policy. It now looks possible to construct a monetary framework leaving room for the development of real activity, without abandoning money supply growth targets, whilst keeping a close watch on the velocity of circulation.This type of approach is now indispensable if, for example, nominal interest rates are to follow inflation rates downwards, so that the real return on the main types of financial asset are not too high relative to the yields on new productive investment.

Budget deficits have increased massively over the past few years even in the low-inflation countries, except in the United Kingdom. The authorities are prepared to accept the consequences of cyclical expansion of public deficits, but are anxious to reduce the structural component. The correct identification of the two components of the deficit is technically difficult, and governs the answer to the question how far the actual deficit can increase, without leading to crowding out or excessive money creation. At all events a sound approach will need to take account of the cyclical position when introducing structural adjustments.

The wide divergences within the Community prior to the implementation of appropriate policies, in particular between growth rates, prices and balances of payments, show how important it is to coordinate economic policies.

In some countries this will mean supporting recovery factors as fully as possible without compromising disinflation, in others accepting the discipline required to bring inflation rates down to levels where the risk of acceleration is eliminated and further progress guaranteed.

The conjunction of the two types of strategy should be of general benefit; greater dynamism in the more stable countries will be of benefit to the others, where greater stability resulting from a reasonable and cautious policy will have spill-over effects.

The recent weakening of links between the price index and incomes in the member countries where indexation is generally applied should, if confirmed, improve the outlook for reducing divergences in prices and costs.

Beyond these requirements, which mainly concern the short run, all the Community countries are still faced with the need to speed up the adjustment of their economic structures, to improve acutely difficult employment problems, and, in the medium term, avoid a decline, even a relative decline, in living standards.

These matters were dealt with in *European Economy* No 14 (see in particular pp. 12-19: Annual Economic Report, and pp. 39-43: Annual Economic Review). Particular emphasis was put on loss of momentum due to excessively high labour costs and real interest rates, and on problems caused by the apparent rigidity of structures, in particular inadequate investment in advanced technology, high budget deficits and the 'deformed' structure of public expenditure, 'unfriendly' to productive investment.

At Community level, three major points should be stressed:

(i) the need for more and better structured productive investment, and the creation of favourable conditions for more abundant (but not inflationary) financing, notably in the financial framework of the Community;

(ii) the need to continue the drive to reduce energy dependence;

(iii) the need for gradual removal of the remaining obstacles within the common market, which still prevent the Community, in certain fields, from offering a suitable framework for the development of production on a European scale.

International debt and less developed countries

Borrowing for economic development

The accumulation of external debt is a normal process in the development of a country towards industrialization. Many less developed countries depend on external capital not only for the development of their resources and for the establishment of an industrial sector but also for building up an infrastructure for those industries. The level of external indebtedness often increases with the level of development because, as a country acquires the industrial capacity to generate income, there is an increased willingness to lend, particularly from external private sources. Thus the more advanced developing countries often attract and depend upon very substantial capital inflows. Until recently the growth of indebtedness did not lead to general concern but was treated as a series of individual country problems. However, over the past year debt repayment difficulties have created a more widespread anxiety, both because of their extent and because of their effects on the international banking system.

Origin of the present debt problem

The origins of the present world debt situation are the two oil shocks and the parallel big surge in bank lending to less developed countries (LDCs). While the recovery in the industrial countries after the first oil shock, together with world inflation, contributed to the narrowing of LDC external deficits—so that there was little deterioration in their creditworthiness—the building-up of LDC debt after the second oil shock was accompanied by a marked deterioration in their debt servicing capacity: for the 21 major LDC borrowers the ratio of total debt service to exports, which had increased from 35% in 1975 to 50% in 1979, climbed to 75% during 1982. The deterioration of the LDC debt situation subsequent to the second oil price explosion was due to a more difficult global environment: in contrast to 1973/74, major industrial countries implemented stricter anti-inflationary policies, mainly firmly restrictive monetary policies with a parallel increase of nominal and real interest rates (which represent the true cost of borrowing) often to record levels. This policy reduced import demand in industrial countries, leading in the LDCs to slower growth and deterioration of their terms of trade.

Size of the problem

The outstanding medium and long-term debt of non-OPEC developing countries has expanded from USD 75 000 million in 1971 to an estimated USD 520 000 million in 1982. The cost of servicing this debt (interest and amortization) has risen even more rapidly from USD 9 500 million to USD 98 000 million, equal to over 20% of receipts from exports of goods and services. It is neither the absolute size of the debt, however, nor the growth in debt service payments overall which has led to problems but rather its concentration in the newly industrialized developing countries. The 10 largest debtors account for over 50% of total medium and long-term debt and most of these are among the more developed of these countries. Even within this group there is a heavy concentration of external debt on four or five big borrowers—particularly in Latin America. The debt problem is not confined to the rapidly industrializing countries: Eastern Europe and some of the very poorest countries in the world have had debt repayment problems. Most of the debt of very poor countries is held by governments or international institutions, whereas much of the debt of the industrializing and East European countries is owed to the international banking system, on which their servicing difficulties have had a big impact. About 60% of total outstanding medium and long-term debt in 1982 was owed to private capital markets, mainly to banks.

These developments have increased the extent to which debt has been incurred on commercial terms and have done so in a period of strongly rising interest rates. The average interest rate of the debt of developing countries has risen from 7,6% in 1979 to 11,3% in 1982. While all have been affected by the rise in interest costs, those countries which have relied heavily on private bank financing have been even harder hit as much of their debt is on a floating rate basis. Thus the newly industrialized countries saw their average interest cost rise from 9,7% in 1979 to 14,7% in 1982. Again the big borrowers were affected most: in 1982, Argentina, Brazil, South Korea and Mexico accounted for 84% of the total net floating rate debt among LDCs, excluding OPEC countries.

While the sharp rise in interest costs combined with the effects of the recession on export earnings are largely responsible for debt servicing problems there is also another factor which has been a source of difficulty for some of the borrowing countries, namely the growth in short-term debt (i.e. debt with an initial maturity of less than one year). Total short-term debt of the non-OPEC LDCs to banks amounted to USD 130 000 million gross in mid-1982.

While in many cases this is offset by corresponding short-term assets, in other cases there is a heavy dependence on short-term debt for liquidity, particularly by the Latin American countries. Thus when the need to roll over short-term debt, which is not included in the traditional debt service ratio, is taken into account, the gross financial requirements of some of the debtors to maintain existing debt levels and to meet current account deficits and servicing costs are very large. For some of the Latin American countries it has been estimated that servicing costs, including roll-over of short-term debt, now amount to substantially more than total receipts from exports of goods and services.

The growing difficulties of the borrowing countries in meeting their financial obligations have created severe problems for the international banks; their inability to meet repayment schedules has lowered the quality of loan portfolios and put at risk the traditional prudential ratios. Furthermore, because of the growth in interbank financing and of international syndicated lending, there have been fears that difficulties arising from repayment problems of borrowers would not be confined to a limited number of banks, but would become widespread. Bank failures in recent years, although not directly connected to LDC debt servicing, have illustrated the potential problems. The risks arising from the growth of developing countries' debt have been exacerbated by the fact that they have occurred at a time when banks were facing increasing difficulties in their domestic loan portfolios as a result of the recession.

The problem is made worse by the continuing need of the debtors for new financing and roll-over of existing debt. The lack of willingness of certain banks to continue lending, or a desire to reduce lending substantially, has had strong negative effects on the prospects for world trade growth, as well as increasing the danger to the stability of the international banking system.

Preventing a crisis

There is no simple or quick remedy to the multi-faceted problem of the present world debt situation. To be viable, a solution would obviously require a balanced approach of financing and adjustment and the active cooperation of international institutions, central banks and governments.

There is unanimity that the most important contribution of industrial countries to a long-range solution of the international debt problem would be more rapid economic growth. Sustained growth will enable developing countries to restore a better balance in their current accounts and to increase their creditworthiness. Simultaneously it will reduce pressures for stronger and more rigid protectionist policies in all countries.

Better opportunities to export to industrial countries which are now at the horizon should be accompanied by efforts of the debtors to bring their borrowing requirements into line with available financing. In this context, the International Monetary Fund would continue to play an important role by implementing and policing credible adjustment programmes, aiming at the reduction of current account deficits by curbing imports and promoting exports. As it will take several years for major LDC debtors to regain normal access to markets (i.e. bank credit) the adjustment efforts of the borrowing countries must be accompanied for several years by some form of financial assistance provided by official lending institutions. To this end recent moves to improve, by means of funding operations (increase in IMF quotas, enlargement of the GAB), the liquidity of the IMF are a first step on the road back to stability.

By imposing conditions designed to re-establish the creditworthiness of borrowers in difficulty, the IMF provides an assurance for commercial banks, which encourages them to make their needed contribution to the 'liquidity bridge' for debtor countries. In this respect it is important that all banks, international, national and regional, continue to participate in this effort and lend new funds to developing countries, because even a temporary but severe disruption of debt servicing could be costly to the stability of the entire international financial system.

Indebtedness: Non-OPEC developing countries — 1982

(USD '000 million)

	Total	of which: Argentina	Brazil	Mexico
Total debt	650	38	87	85
— medium/long-term	520[1]	25	68	53
— short-term [2]	130	13	19	32
Debt owed to banks [2]	269	25	55	64
Net floating interest rate debt [1, 3]	166	21	46	59
Debt service payments [4]	98	5	19	15

1 *Source:* OECD — estimates, year end.
2 *Source:* BIS — end June 1982.
3 Excludes all OECD countries.
4 On medium and long-term debt.

The economies of Member States[1]

Belgium

Trends and prospects

In view of the particularly large current account and general government budget deficits, the government took a number of major measures at the start of 1982; the central rate of the Belgian franc was adjusted by 8,5% against the other EMS currencies; on the incomes policy front, the system of proportional indexation was partially suspended and a selective price freeze introduced; and budgetary and tax measures were taken with the aim of bringing public expenditure under control and stimulating business investment.

The current payments deficit came down from 5,4% of GDP in 1981 to 3,8% of GDP in 1982. The real improvement in the external balance was not undermined by a deterioration in the terms of trade, as might have been feared after the realignment of the Belgian franc. Exporters raised their Belgian franc prices substantially, and import prices were favourably influenced by the fall in key commodity prices on world markets.

A further deterioration in the budgetary situation could not be avoided, however. Although revenue was, overall, in line with forecasts, the temporarily uncontrolled overrun of expenditure by recourse to special funds and to amounts carried over from earlier years led to a fresh increase in the central government borrowing requirement in 1982. The Treasury's cash deficit — adjusted for exchange losses — will probably go as high as BFR 508 000 million, whereas the budget tabled in early April 1982 aimed at stabilizing it at its 1981 level (BFR 455 000 million). For general government as a whole, the cash deficit is likely to exceed 15,5% of GDP (15,3% in 1981). As in 1981, over 40% of the central government deficit was covered by foreign currency borrowing.

[1] The forecasts presented in this chapter were essentially finalized in February 1983. The effects of recent oil price decisions, though partially foreseen, have not therefore been fully taken into account.

After improving slightly in the first half of 1982, economic activity again slackened; real gross domestic product probably declined a little (by about ½%). This out-turn is less satisfactory than originally forecast, largely because of the very sluggish trend of external demand. Unemployment continued to increase, reaching 14,9% of the civilian labour force at the end of December.

Despite the realignment of the Belgian franc, it was possible to limit the rate of consumer price increase to an average of 8,8% for the year thanks to the moderate rise in import prices and the prices and incomes policy conducted during the year.

At the end of 1982, the government decided to prolong most of the income restraint measures adopted during the year on the basis of the special powers granted. The present plan is that, after a period during which the system of flat-rate adjustments will remain in force, percentage indexation will be reintroduced. But at the same time, the waiting period before which the sliding scale is activated will be lengthened and the composition of the price index changed. The new system will also apply to minimum incomes and the social transfer payments. The objective of the restraint measures is to maintain company competitiveness, which improved markedly in 1982, and to consolidate the return to profitability.

Despite the unfavourable repercussions which the small rise in personal incomes and the slackness of activity will have on the increase in tax and parafiscal revenue, and hence on the public finance deficit, this deficit is in 1983 unlikely to go much above its 1982 level and might actually fall slightly, provided that spending plans, as set out in the draft budget, are respected.

Changes in the central government public debt [1]

(BFR '000 million)

	1979	1980	1981	1982
Debt in BFR	+ 169,5	+ 204,4	+ 240,6	+ 283,9
of which:				
Short-term debt	(+ 43,4)	(+ 134,9)	(+ 213,9)	(+ 223,9)
Foreign currency debt	+ 42,3	+ 92,4	+ 214,3	+ 219,5
Total	+ 211,8	+ 296,8	+ 454,9	+ 508,4

[1] Excluding exchange losses and the part of the debts formerly not served through the budget but included in the central government debt from 1 January 1982 (BFR 95 500 million).

Wage restraint, plus the raising of certain taxes and social security contributions, will cause real personal disposable incomes to fall by almost 3%. Because of the uncertain economic climate and the unfavourable prospects for employment, the savings ratio can hardly be expected to fall much further, and private consumption, for the third year in succession, is therefore likely to decline appreciably in real terms (−2,4%).

The volume of public consumption is also set to fall, following a more severe clamp-down on operating expenditure and a tighter recruitment policy under which the increase in public sector staffing levels will be limited.

1982 saw a marked improvement in business profitability, which had suffered badly in recent years: the effect of wage restraint was to slow wage costs down significantly, and exporters increased their Belgian franc prices after the currency realignment. Business investment increased slightly and this trend is likely to be sustained in 1983, if sales prospects improve and interest rates ease further. The implementation of major programmes in industries undergoing restructuring, such as the steel industry, will also help. However, activity in residential construction, after reacting very little to the measures taken in 1982, such as the reduction of VAT on new building, is liable to fall further in 1983. The prospects for disposable income, the stock of unsold housing and the high level of interest rates will continue to have a depressive effect. Because of financing difficulties, the public housing sector will also decline. The volume of public investment will continue to contract: the sums committed, both by central and local government, have been falling for some years.

Assuming that the increase in wage costs is moderate, the improvement in company competitiveness achieved in 1982 may well continue in 1983, so that additional market shares can be won; nevertheless export growth will remain modest in view of the sluggish state of the international economy. With domestic demand weakening further, import volume will fall slightly in 1983, as it did in 1982.

In 1983, import prices will reflect the favourable effects of the stability of commodity prices, a very moderate rise in the prices of manufactured imports, and a firmer trend in the Belgian franc's effective exchange rate. The rise in import prices will consequently be a good deal less sharp than in 1982. The increase in export prices will also slow considerably. All in all, the trade balance, after its marked improvement in 1982, could come close to equilibrium in 1983. Nevertheless, because of the deterioration on the factor income account as a result of interest payments on the public authorities' foreign currency debt, the improvement in the current account balance will be smaller, and the deficit in 1983 will be equivalent to 3,1% of GDP.

As in 1982, real gross domestic product will probably fall by some ½%. The result is likely to be a further deterioration in the employment situation, especially since the government will no longer maintain temporary job programmes at their former level. How the employment situation develops will partly depend on the outcome of the negotiations at present under way in many industries on cutting working hours and taking on more workers (see box entitled 'Wage moderation and reductions in working hours in the Benelux countries').

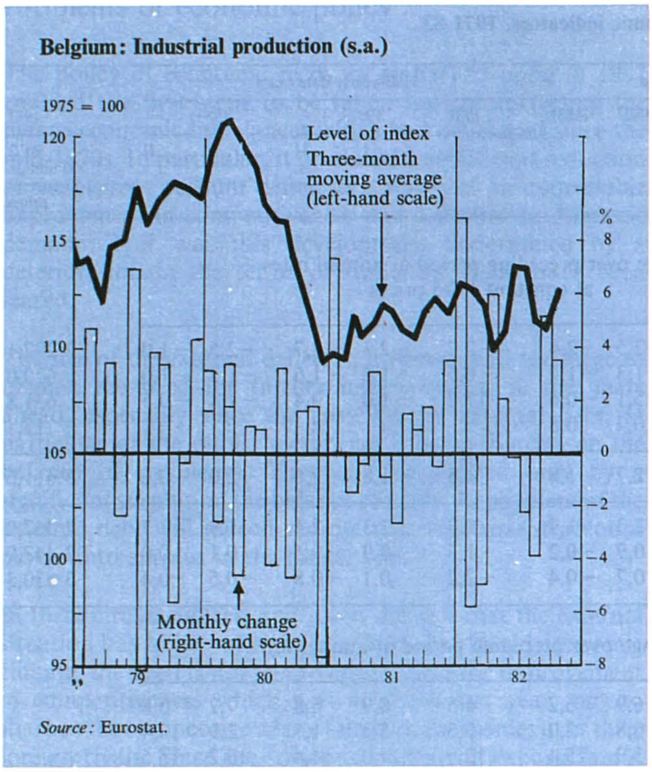
The expected slowdown in import prices and the moderate rise in wage costs will help to bring inflation rates down further during 1983; these favourable effects will be partly offset by the higher VAT rates and public utility charges which came into force at the start of the year. The rise in the consumer price deflator will average some 7,5% for the year, but the rate towards the end of the year will probably be much lower than this average.

The development of competitiveness

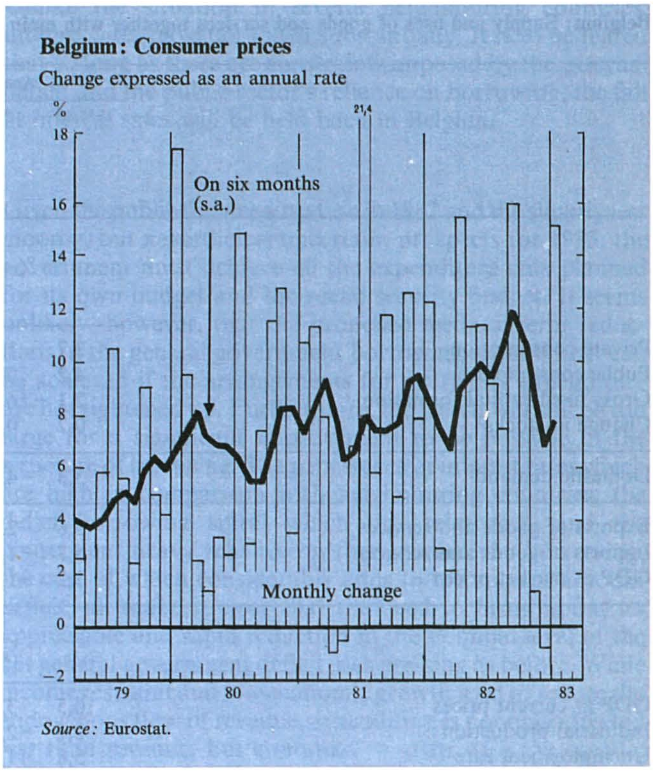
(1970-75 average = 100) [1,2]

	1978	1979	1980	1981	1982
Index of price competitiveness	119,5	117,9	112,9	104,5	93,0
Effective exchange rate	116,1	118,5	118,3	112,2	101,9
Unit wage costs	163,6	170,6	180,1	192,3	202,3

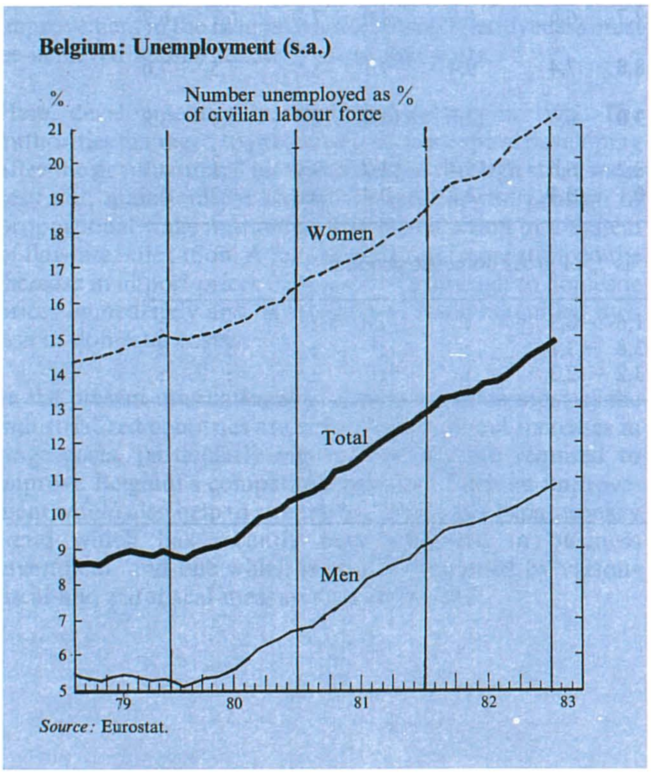
1 Calculated on the basis of unit labour costs in 19 industrialized countries and the effective exchange rate of the Belgian franc.
2 Calculated on the basis of data available at the beginning of 1983.



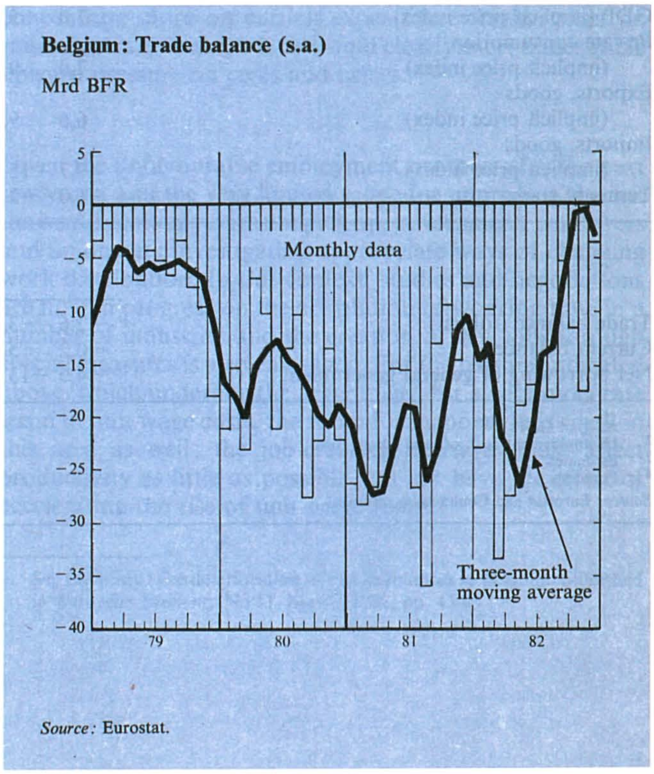
Source: Eurostat.



Source: Eurostat.



Source: Eurostat.



Source: Eurostat.

Belgium: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					
	1971-80	1981	1982[3]	1983[4]	1981	1982[3]		1983[4]		1981
					II	I	II	I	II	BFR '000 million at current prices
	% change over preceding period at annual rates — at constant 1975 prices									
Private consumption	3,7	−1,4	−2,5	−2,4	−2,2	−2,1	−3,7	−2,5	−1,0	2 292,1
Public consumption	4,2	0,6	−1,3	−1,2	−0,6	−1,5	−1,6	−1,2	−1,0	670,0
Gross fixed capital formation	2,1	−16,2	−5,1	−0,6	−17,2	−1,0	0,4	−1,4	−0,5	631,8
Change in stocks[1]	0,7	0,3	0,4	0,5	:	:	:	:	:	17,1
Domestic demand	3,3	−4,0	−2,7	−1,8	−4,5	−1,8	−2,6	−2,0	−0,6	3 611,0
Exports of goods and services	5,6	2,5	2,3	1,9	2,3	2,3	2,1	1,9	1,7	2 367,2
Imports of goods and services	5,7	−1,4	−0,9	−0,2	−1,3	0,9	−0,5	−0,1	0,0	2 447,9
GDP at market prices	3,2	−1,7	−0,7	−0,4	−2,2	0,1	−0,8	−0,5	0,4	3 530,3
	% change over preceding period at annual rates									
GDP at current prices	10,5	3,6	6,9	6,2	4,5	8,9	6,8	7,2	5,8	
Industrial production	2,3	−2,8	0,8	2,0	−0,6	5,5	−1,1	2,9	3,4	
Unemployment rate[2]	5,8	11,7	13,9	15,4	12,6	14,0	14,4	15,2	15,5	
Compensation of employees	11,9	7,5	6,1	5,5	6,4	6,2	5,8	5,5	5,3	
M2	10,4	6,6	5,8	6,0	:	:	:	:	:	
GDP (implicit price index)	7,0	5,4	7,7	6,6	6,9	8,0	7,7	6,7	6,2	
Private consumption (implicit price index)	7,0	9,1	8,8	7,4	9,4	9,1	8,5	7,5	7,0	
Exports, goods (implicit price index)	6,6	9,9	13,0	6,5	12,8	14,4	10,6	5,9	3,8	
Imports, goods (implicit price index)	7,7	15,5	13,2	6,6	15,4	13,9	9,9	6,1	4,4	
Terms of trade	−1,0	−3,9	−0,1	−0,3	−2,3	0,4	0,6	−0,2	−0,6	
	as % of gross domestic product									
Trade balance (fob/cif)	−2,6	−3,5	−1,6	−0,3	:	:	:	:	:	
Current balance	−0,2	−5,4	−3,8	−3,1	:	:	:	:	:	
Net borrowing of general government	−4,6	−13,3	−13,2	−12,3	:	:	:	:	:	

1 As % of GDP.
2 Unemployment as % of total labour force.
3 Estimates.
4 Forecasts.

Source: Eurostat and Commission services.

Problems of economic policy

The policy of economic recovery embarked upon in 1982 enabled the first steps to be taken toward correcting the macro-economic imbalances which had developed since the mid-1970s. In particular, it produced a significant reduction in the current account deficit as a result of an appreciable improvement in competitiveness and a decline in domestic demand. Nor was this development undermined by a deterioration in the terms of trade, as might have been feared.

The size of the external deficit is, however, still too large to obviate the need for further improvements in the years ahead, especially since the costs of the external debt, in particular of the public sector, are a heavy burden on the balance of payments. They can be funded only by a significant surplus on the balance of trade. Repayment of the external debt will indeed require that the current account moves into surplus in the longer run.

In these circumstances, and given the fact that the external situation has to be put right in a depressed world economic climate, the need is not just to consolidate the improvement in competitiveness which was achieved last year, but to sharpen the competitive edge of Belgian companies over their foreign rivals. Since the structure of Belgian exports is not sufficiently geared to the needs of foreign markets, and since restructuring in this area is bound to be slow, the improvement in the Belgian economy's competitiveness must be achieved mainly through prices and costs.

Here, developments were fairly satisfactory in 1982. The authorities managed to prevent a cost/price spiral developing after the devaluation. This was achieved through strict wage restraint, mainly in the shape of temporary suspension of proportional wage indexation and introduction of a system of flat-rate indexation. A temporary price freeze stopped the increase in import prices from working through to domestic prices immediately and its effect from being magnified by a rise in domestic costs.

In the present international situation, in which most of the industrialized countries are very cautious about increases in wage costs, particularly vigorous efforts are required to improve Belgium's competitive position. Such an improvement would also help to strengthen the slightly expansionary trend which has recently been observed in business investment, and one which is also underpinned by various fiscal and parafiscal measures taken in 1982.

Unlike the situation in several neighbouring countries, interest rates have not fallen substantially. It is to be feared that so long as there are constraints imposed by the external deficit and the public sector's reliance on borrowing, the fall in interest rates will be held back in Belgium.

Given the public finance situation in 1982 and the slightly less gloomy, but nevertheless uncertain, prospects for 1983, the government must achieve all the expenditure cuts planned for its own budget and the social security budget. It seems unlikely, however, that the proposed medium-term reductions in the general government borrowing requirement can be achieved if the arrangements for restricting expenditure are not tightened up. Furthermore, the deficit will still be too large for a significant improvement to be possible in the structure of financing. The persistence of interest rates which are high in comparison with neighbouring countries, the deficit/borrowing spiral which this reinforces, and the consequent heavy reliance on foreign currency borrowing, the cost of which considerably adds to the current account deficit, all make it clear that the need to bring about an appreciable and rapid reduction in the nominal level of the net general government deficit is as pressing as before. While income restraint and low economic growth tend to reduce the endogenous flow of revenue, expenditure is not only affected less than revenue, but continues to grow with the specific momentum which it has acquired for some years. [1] Thus, action to correct the public finance situation should concentrate more on cutting expenditure further than on raising extra revenue, which would clearly exert undesirable upward pressure on costs and prices.

Given the unfavourable employment prospects for the next few years, and the very limited scope for improving them if the world economy does not pick up, government, employers and unions are investigating appropriate ways of changing work distribution. In this context, studies and negotiations are now in progress on the adaptation of working time in a number of industries and the creation of new jobs through special measures is also envisaged. For the reasons indicated above, which underline the urgent need for a very moderate trend in unit wage costs, the room for manoeuvre is small in this area as well; the job-creating measures must affect productivity as little as possible and not have the effect of accelerating the rise of unit wage costs.

1 See the study 'The deterioration of public finances in Belgium' published in *European Economy* No 11, March 1982, pp. 43-45.

Wage moderation and reductions in working hours in the Benelux countries [1]

Wage and salary increases in the three Benelux countries have slowed down considerably in recent years, thanks mainly to the joint efforts of the governments and the social partners.

In the *Netherlands,* the aim since 1978 has been to curb the rise in real earnings. However, this objective has been only partially achieved, since the beneficial effects of the slowdown in real increases under collective wage agreements have, in some years at least, been cancelled out by an acceleration in wage drift. At the same time, there has been a growing tendency to offset the sharp increase in taxes and social security contributions by a matching increase in wages. In view of these trends, the automatic linking of wages to rises in the cost of living was temporarily suspended in 1980 and only partially restored in 1981 and 1982, though the top range of incomes was excluded in 1982. The government has decided to freeze public sector pay and social security benefits in 1983 and also initially intended to impose a freeze on private sector pay during the first few months of the year, in conjunction with a price freeze. However, it has abandoned this plan so as to allow employers and unions to negotiate the suspension of wage indexation in exchange for a reduction in working hours.

In *Belgium,* after the government had suspended all wage increases at the end of 1980, except for cost-of-living adjustments, an economy-wide agreement was concluded early in 1981, limiting real wage increases under new collective wage agreements to 1%. Wage costs per worker were also influenced in 1981 by the 'Maribel' operation, which reduced employers' social security contributions; the budgetary effects of this measure were offset by an increase in value-added tax.

In 1982, in conjunction with the realignment of the Belgian franc, the system of proportional indexation was temporarily suspended, except for the lowest incomes, and replaced by a system of flat-rate indexation under which wages are increased by a fixed amount each time the index crosses specified thresholds. For 1983 and 1984, the government has set itself the objective of safeguarding the improvement in business competitiveness achieved in 1982 and hence limiting the rise in wages per worker to the average of wages in Belgium's main trading partners. 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 wage 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.

In *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. In Luxembourg too, the 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 will be maintained in 1983, albeit in a slightly altered form; there will be a maximum of three index-linked increases of 2,5%. The system will be re-examined in the summer in the light of economic developments during the first half of the year.

[1] See also the article on 'Unit labour costs in manufacturing industry'.

Earnings, productivity, labour costs and income share in industry

(% changes)

	Nominal income per worker	Real income per worker [1]	Labour productivity	Nominal unit labour costs	Share of income from employment (whole economy) [2]
The Netherlands					
1979	6,7	2,3	3,3	3,3	0,8
1980	7,4	0,8	3,1	4,1	0,4
1981	4,4	−2,0	3,6	0,8	−1,8
1982	6,5	0,9	2,4	4,0	−0,9
1983	3,4	0,4	3,2	0,2	−1,5
∅ 1979-83	5,7	0,5	3,1	2,5	−0,6
∅ 1974-78	11,1	2,9	4,1	6,9	0,4
Belgium					
1979	7,8	3,8	6,2	1,5	0,0
1980	9,6	2,9	1,6	8,0	1,1
1981	6,2	−2,7	3,7	2,4	1,8
1982	5,4	−3,1	4,0	1,3	−2,9
1983	5,7	−1,6	3,2	2,4	−1,3
∅ 1979-83	6,9	−0,1	3,7	3,1	−0,3
∅ 1974-78	14,3	5,2	5,7	8,4	1,8
Luxembourg					
1979	6,0	0,2	6,2	−0,2	−4,0
1980	5,7	−1,9	−0,4	6,1	1,2
1981	8,0	0,3	−5,2	13,8	2,5
1982	6,9	−2,8	−0,9	7,9	−0,3
1983	6,9	−1,9	1,3	5,6	−1,0
∅ 1979-83	6,7	−1,2	0,2	6,6	−0,3
∅ 1974-78	11,5	3,4	0,7	11,9	4,8
EC					
∅ 1979-83	10,2	0,0	2,0	8,1	0,4
∅ 1974-78	13,9	2,5	3,2	10,6	0,8

[1] Adjusted for changes in the retail price index.
[2] Compensation of employees, adjusted for the share of self-employed in total employment, as a percentage of net domestic income at factor cost.

Source: Commission services.

So as to allow assessment of the actual impact of the strategies described above, the table above shows, for the three countries, the movement in industry of total earnings per employee in nominal and real terms, together with the changes in productivity, labour costs and the share of income from employment.

In the *Netherlands*, the average annual increase in total earnings per employee in industry, which amounted to 11,1% from 1974 to 1978, is down to 5,7% from 1979 to 1983. In real terms, this meant an average increase of only 0,5%, as against 2,9% during the previous period. The rise in unit labour costs also eased, but was nevertheless sharper than the rate suggested by the slowdown in earnings per worker. This discrepancy is the result of less rapid productivity growth, due mainly to the fall in industrial output, to a very marked drop in the investment ratio of firms and to the leeway in technological development. Lastly, the share of income from employment which provides an indication of changes in business profitability, has declined during recent years. After rising by an average of 0,4% in the period 1974-78, it has fallen by an average of 0,6% in the period 1979-83.

Developments were similar in a number of respects in *Belgium*. The average annual increase in nominal earnings in industry fell from 14,3% to 6,9%. Since 1981, there has been a distinct decline in real per capita earnings. Productivity growth, which was very rapid during the second part of the 1970s, has slowed down distinctly since then. This has meant that the rise in unit labour costs averages 3,1% during the period 1979-83 as against 8,4% in the period 1974-78. Lastly, the movement of the share of income from employment seems to indicate a distinct improvement in profitability as from 1982.

In *Luxembourg*, despite an appreciable deceleration in total per capita earnings, the growth of labour costs has remained relatively rapid in recent years compared with the other Benelux countries. This is because productivity growth has been very limited. The share of income from employment has come down slightly in recent years, after rising sharply in the period 1974-78.

In conclusion, it may be seen that wage moderation in industry has been greater in Belgium than in the other two countries in recent years. However, the slowdown in productivity growth was also more marked in Belgium, with the result that the easing in unit labour costs has on average been broadly similar in the three countries in the period 1979-83. Yet in order to draw more specific conclusions as to the trend of competitiveness in the three countries, account must also be taken of the fact that, according to current estimates, the Belgian and Luxembourg francs were subject to an effective depreciation of 2,7% on an annual average during the period 1979-83, while the guilder showed an average effective appreciation of 1,7% a year.

Wage moderation in the Benelux countries has been greater than in the Community as a whole, where the annual growth of nominal wages, having averaged 13,9% in the period 1974-78, still averages 10,2% in the period 1979-83. Similarly, the slowdown in unit labour costs has been significantly greater in the Benelux countries than in the Community as a whole.

The employment situation has deteriorated sharply in the three Benelux countries in recent years. In Belgium, the unemployment rate, which was already very high at the end of 1978 (8,4%), continued to rise and stood at 14,9% by the end of 1982. The Netherlands even had the sharpest increase in unemployment in the Community in 1982; the unemployment rate there climbed from 4,3% in December 1978 to 12,1% in December 1982. In Luxembourg, even according to the latest figures, the official unemployment rate is particularly low (1,6% in December 1982). However, this rate masks the distinct increase since 1981 in the number of workers participating in special employment programmes. [1]

Given the unfavourable growth prospects in the three countries, there is little likelihood that the foreseeable supply of labour can be absorbed in the years ahead without appropriate measures.

In these circumstances, employers and unions in the three countries are attaching increasing importance to the maintenance of existing jobs and the creation of new jobs. They are tending more to link wage moderation to a reduction in working hours, in order to allow such moderation to contribute more directly to improving the employment situation.

[1] The figures given for the three countries are not fully comparable, since there are still significant differences in the definitions of 'unemployment' and in the rules applied. (See special article 'Comparison of the number of unemployed in Belgium and in some other Community countries' published in *European Economy* No 5, March 1980, p. 71.)

Average weekly hours of work, per manual worker, in industry [1, 2]

	1972	1975	1977	1978	1979	1980	1981	1982
The Netherlands	43,9	40,8	41,1	41,1	41,1	40,8	40,7	40,6
Belgium	41,7	37,1	37,1	37,6	38,1	35,7	35,9	:
Luxembourg	43,9	40,9	39,5	40,2	40,8	40,2	40,6	38,9

[1] Excluding public utilities.
[2] Situation as at October, except 1982: situation as at April.
Source: Eurostat.

In the *Netherlands*, an agreement was concluded at national level in November 1982 between employers and employees; under the agreement, those negotiating collective wage agreements in the various sectors of the economy are called upon to forgo nominal wage increases as far as possible in 1983 and to concentrate instead on improving the distribution of employment and stepping up the fight against youth unemployment, the basic idea being that cuts in working hours must not increase companies' costs and undermine their necessary structural improvements. Since then, in response to this recommendation, the wage increases which should have been granted on 1 January by virtue of the automatic linking of wages to the cost of living index have been suspended in a number of industries, and agreement has been reached on reductions in working hours and an increase in the number of jobs. In the public sector, where there will be no nominal increases in wages in 1983, longer annual leave will be granted and 5 000 new jobs created.

In *Belgium*, the hours of work laid down in collective agreements have been reduced significantly during the last 10 years and are now lower than in the other Community countries. Since there has not been any matching reduction in earnings, this has meant a sharp increase in labour costs. Indeed, the aim was to improve the quality of life, and the idea of work sharing was not a consideration. This was again the case with the above-mentioned economy-wide agreement concluded in February 1981 by employers and unions, which provided for the possibility of replacing real wage increases by a reduction in working hours.

Recently, the government recommended a 5% reduction in working hours to employers and employees; this was supposed to be accompanied by a 3% increase in employment, experience having shown that a reduction in working hours results in more rapid productivity growth. So as to encourage recruitment, the government was to grant, for each new worker taken on, a substantially larger reduction in employers' social security contributions under the Maribel operation. In addition, supplementary tax relief was to be authorized on investment connected with reductions in working hours. Firms which did not take on additional workers in accordance with the objective pursued were to be required to pay into an 'Employment Fund' the amount released by the more moderate wage increases. No agreement on these proposals was reached at national level; the negotiations then continued at the level of individual industries. By the end of February, an agreement had been reached in a number of industries. The difficulty during the negotiations was to come to a formal agreement with respect to the creation of new jobs. In the public sector, an agreement was concluded under which working hours are to be reduced, through the granting of additional holidays, to an average of 37 hours a week, and the level of employment stabilized.

In *Luxembourg*, the tripartite conference for the steel industry recently reached agreement on a reduction in working hours in conjunction with a reduction in wages in 1983 and 1984. Each wage and salary earner will receive an additional 12 days' unpaid holiday. The reduction in wages and salaries depends on the level of monthly earning and should average some 6%. The intention here is not to create new jobs, in contrast to plans in the Netherlands and Belgium. Nor, consequently, can the measures be regarded as constituting a redistribution of available work; rather, they are aimed at preventing an increase in short-time working and at reducing the special job schemes.

Progress has no doubt been made recently in the three countries in introducing reductions in working hours that may allow existing jobs to be maintained and indeed new jobs to be created. Nevertheless, a fairly large degree of reluctance persists on the part of the social partners. Because of the need to ensure that competitiveness is not affected and to maintain unit costs at their present level, or indeed in some cases to reduce them further, full compensation of the income losses implied by shorter working hours is impossible, unless there are corresponding gains in productivity. Furthermore, companies often hesitate to enter into contractual undertakings on the recruitment of additional workers, either because they consider that this is not justified by their sales and output prospects or because a higher level of output could be achieved by raising productivity.

Denmark

Trends and prospects

As a result of the recovery in domestic demand at the beginning of 1982 Denmark experienced a higher rate of growth during the year than other countries in the Community. GDP rose by 2,3% in 1982 against 0,2% for the Community as a whole. The rise in real disposable income in the first months of the year caused a temporary pick-up in private consumption, but the demand for consumer goods began to level off during the latter half of the year as a result also of higher indirect taxation. Public consumption on the other hand continued to grow partly due to the employment policy pursued. Although residential construction and business investment remained depressed the sharp increase in energy investment had a considerable impact on overall gross fixed capital formation. The structure of domestic demand was conducive to a further increase in imports, whereas exports tended to stagnate as foreign demand slowed down and the export performance deteriorated. As a consequence the current deficit on the balance of payments grew strongly and attained 4,5 % of GDP against 3,1% in 1981. Total employment in 1982 increased at a rate below that of total labour supply. The deficit of the public sector increased rapidly due to a considerable rise in social transfers and interest payments. The general government borrowing requirement was of the order of 9,2% of GDP in 1982 against 7,1% the year before.

The growing disequilibria made an adjustment of the economic policy as implied in the pluriannual stabilization programme necessary. In October the government presented a programme the main thrust of which was to strengthen Denmark's international competitiveness, to reduce the growing central government deficit and to promote investment and technological innovation. An immediate freeze on wages and profits was introduced until March 1983, when the new biennial wage agreements should come into force. It was recommended that the agreements on the private labour market should be settled along a level corresponding to the 4% ceiling announced for annual pay increases in the public sector. The government might in return envisage an alleviation of personal taxes in 1983. The half-yearly cost-of-living adjustments and other automatic adaptations of wages and social transfers (excluding social pensions) were abolished until March 1985. Dividends etc. paid during the two-year period should not exceed those previously paid.

The outcome of the recent wage negotiations is more or less in keeping with the overall guideline. But indirect wage costs will increase by another 1 ½% of the wage bill mainly due to the trebling of employers' contributions to the unemployment insurance scheme.

Central government expenditure will grow at a somewhat lower rate as a consequence of the slowdown of public sector wages and salaries, the cutback in social transfers together with specific efforts to reduce other expenditure by carrying forward a bigger part of the costs connected with social security, public services and transport to the users. A part of this reduction will be operated by local authorities corresponding to the cut in general grants-in-aid from the central government. A tax on the stock of capital in pension funds and life insurance companies, tax-free up to now, has been introduced. Finally the government put forward a set of proposals with the aim of promoting investment and technological innovation by fiscal and administrative alleviations. Specific efforts should be undertaken to sustain research activities within certain advanced sectors like telecommunication, data processing, biotechnology, etc.

The economic programme outlined above was adopted by the parliament and incorporated in the appropriation bill for 1983. It results in a DKR 10 000 million cut in the estimated central government deficit for 1983. The easing of monetary policy and the fall in domestic and foreign interest rates, imply, according to official estimates, a reduction by some DKR 1 500 million in the costs of government borrowing. Thus the central government deficit may attain some DKR 69 000 million or 13,6% of GDP.

Export markets in 1983 could grow by slightly more than last year if world demand starts to pick up. Although there may be a slight improvement in relative costs the envisaged rise in the effective exchange rate (see figures below) could hamper any further rise in industrial market shares during the year. Whereas the stock of export orders reported by the consumer goods industry remains high, the demand for investment goods could on the other hand level off. The agricultural exports, which make up one quarter of total exports could remain almost stagnant in 1983. They have been distorted by the outbreak of foot and mouth disease, which caused a diversion of exports away from certain markets outside the Community and resulted in lower prices. The total increase in the export volumes of goods and services might thus attain some 2% in average.

(% change over preceding period)

	1980	1981	1982	1983
Improved competitiveness (+) due to:	10,1	7,3	3,0	−2,5
effective depreciation (+)	8,3	6,6	4,2	−3,1 [1]
lower relative labour costs (+)	1,8	0,7	−1,2	0,6

[1] Mid-January.

Note: Relative figures compared to 19 industrialized countries.
Source: Commission services.

The imports of goods rose in 1982, largely as a result of growing domestic demand for consumer durables, and investment goods for the exploitation and distribution of North Sea gas and oil. The import of energy has on the other hand continued to fall due also to growing domestic production. Despite the present uncertainties concerning prices on energy this will help to reduce the trade deficit and could have a growing positive net impact on the balance of payments from 1983 and onwards. The smaller rise in the import-intensive part of domestic demand in 1983 should bring about a minor increase in import volumes and thus a small improvement in the trade deficit. The slight improvement in the terms of trade, which took place towards the end of 1982, might be further accentuated during 1983.

The current deficit on the balance of payments will nevertheless remain important as a consequence of growing interest payments abroad. In 1982, when the current deficit totalled DKR 21 100 million, net interest payments amounted to DKR 19 200 million. A further fall in the US dollar rate as well as in the international interest level could obviously have a favourable impact on servicing the foreign debt, which amounted to some 30% of GDP at the end of last year. The current deficit could then improve by somewhat more in 1983 than presently envisaged, and attain less than DKR 19 000 million.

The average compensation of employees could increase by some 7% in 1983 compared to 11% the year before. The moderate wage settlements agreed in the period until March 1985 and the suspension of automatic wage indexation, which last year accounted for more than half of the increase are the major reasons for the envisaged slowdown. It remains however to be seen whether wage drift, which in 1982 accounted for a quarter of the total increase, can be controlled. However, the access to further individual wage adjustments during the period has been limited.

The rise in indirect taxes and in various public charges reduced the fall in the rate of inflation with the consumer price deflator attaining 8% in 1983 against 10% last year. Despite the moderate fiscal compensations envisaged in connection with the incomes policy there will be a fall in real disposable earned income, contrary to 1982. Private demand for consumer goods, and for durables in particular, should consequently fall during the year. The envisaged slower rise in public wages and smaller increase in public employment result in a slowdown of public consumption this year.

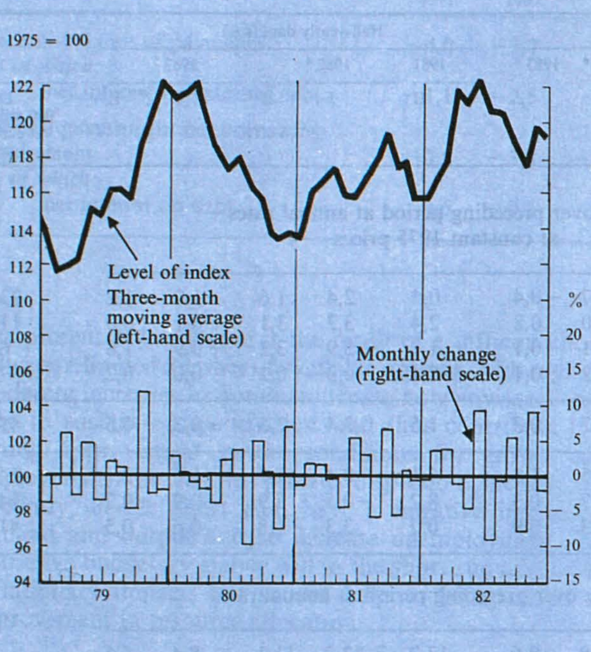
Public investment will continue to fall also in 1983 as a result of cuts within the social service sector and education, as a consequence of the budgetary tightening. Whereas energy investment undertaken in 1982 will slow down in 1983 the propensity to invest could improve in other business sectors, particularly in industry, as a result of improved profitability. The level of activity in residential construction could remain rather depressed due to falling real income and the still high level of real interest rates. Thus after the rise in 1982 total gross fixed investment might stagnate in 1983 and could even start to decline during the year.

On the whole, the growth in gross domestic product could fall to 1% in 1983. After the relative easing of the employment situation last year, due to smaller labour shedding in the private sector, and a continued increase in public employment, the level of unemployment could rise considerably. Despite measures adopted in June 1982 aiming *inter alia* to extend schemes for professional training, increase trainee opportunities and create more subsidized jobs with private or public employers, the rate of unemployment could attain 10% in 1983 against 9,1% in 1982 (SOEC definition).

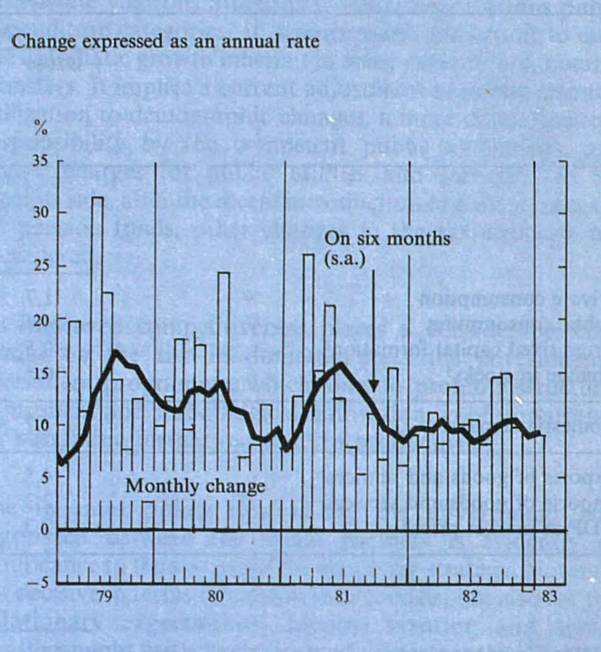
Problems of economic policy

The aggravation of economic disequilibria, for some years now a continuing feature of the Danish economy, has gradually increased the policy constraints. The deficit on the current balance of payments, the growing government borrowing requirement and the underutilization of productive resources, originally due to cyclical changes, have, to a growing extent, become structural problems. Vigorous efforts over several years are needed to restore the situation. This has become more urgent due to the rapid increase in interest payments, which burdens the Danish economy in general and the government budget in particular, and which has narrowed the room for action left to the authorities (see figures below).

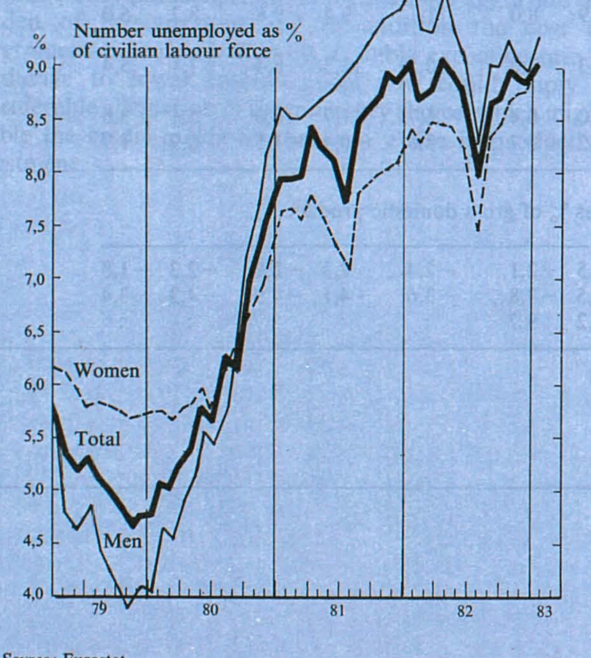
The economic policy pursued until 1982 was based upon the pluriannual programme presented in 1980, which aimed to reduce the external deficit, to sustain employment and to contain the growing budgetary imbalance. The measures taken notably in the field of budgetary policy and incomes policy in 1980 and 1981 did not avert an accentuation of the macro-economic disequilibrium in 1982. As a result of the pick-up in domestic demand and the aggravation of the international environment the external balance deteriorated further. Despite the rise in domestic activity unemployment grew considerably, which prompted the authorities to reinforce the employment and business programmes. Their freedom of action was, however, limited by the strong increase in the public sector deficit. The necessary restructuring of the Danish economy, which should allow a better utilization of resources, became increasingly constrained.



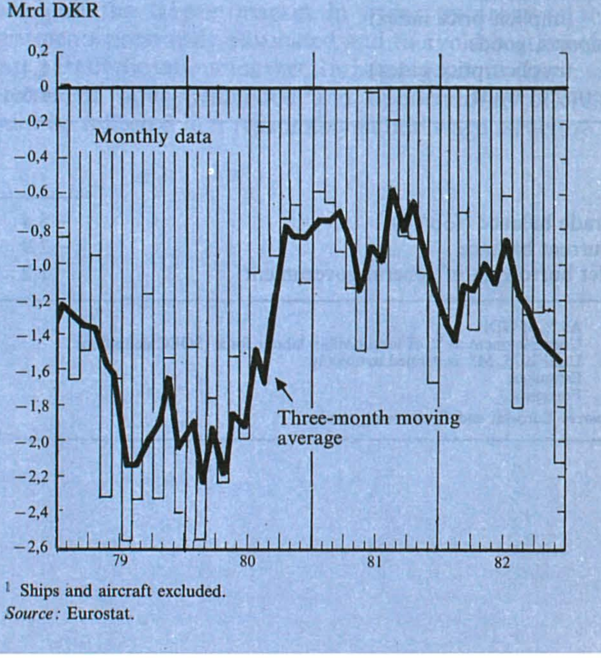
Source: Eurostat.



Source: Eurostat.



Source: Eurostat.



[1] Ships and aircraft excluded.

Source: Eurostat.

Denmark: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					
	1971-80	1981	1982 [4]	1983 [5]	1981	1982 [4]		1983 [5]		1981
					II	I	II	I	II	DKR '000 million at current prices
	% change over preceding period at annual rates — at constant 1975 prices									
Private consumption	1,7	−1,2	1,7	−0,4	0,4	2,4	1,6	−1,0	−1,2	233,0
Public consumption	4,4	3,0	3,0	0,8	2,4	3,2	3,1	0,1	0,0	114,7
Gross fixed capital formation	−0,5	−15,7	4,1	−0,1	1,7	5,9	3,1	−0,9	−1,8	65,0
Change in stocks[1]	0,5	−0,4	−0,2	0,1	−0,4	−0,3	−0,2	0,0	0,2	−1,1
Domestic demand	1,7	−2,5	2,7	0,3	1,5	3,4	2,5	−0,3	−0,5	411,6
Exports of goods and services	4,5	5,6	1,5	1,8	5,1	−0,4	1,7	1,8	2,1	147,3
Imports of goods and services	2,3	−2,1	2,7	0,3	8,2	−0,5	3,9	−0,9	−0,7	144,7
GDP at market prices	2,3	0,1	2,3	0,9	0,7	3,3	1,8	0,6	0,5	414,1
	% change over preceding period at annual rates									
GDP at current prices	12,1	10,9	12,8	8,6	13,2	13,3	11,3	8,4	6,5	
Industrial production	1,9	0,3	1,7	0,0	2,4	5,9	−6,8	1,7	3,8	
Unemployment rate[2]	3,8	8,4	9,1	10,0	8,5	8,9	9,4	10,2	9,8	
Compensation of employees	11,5	10,1	11,0	7,0	11,2	10,8	11,2	6,1	4,6	
M2 (harmonized definition) [3]	11,8[3]	9,6	12,0	9,0	:	:	:	:	:	
GDP (implicit price index)	9,6	10,9	10,3	7,7	12,4	9,7	9,3	7,8	6,0	
Private consumption (implicit price index)	10,2	12,1	9,9	8,0	11,1	9,4	9,8	8,2	6,0	
Exports, goods (implicit price index)	8,9	14,2	10,3	7,0	10,5	11,3	8,4	7,1	5,4	
Imports, goods (implicit price index)	11,4	17,2	10,0	6,4	6,7	11,7	10,0	6,1	3,6	
Terms of trade	−1,6	−2,5	−0,2	0,7	3,6	−0,4	−1,5	0,9	1,7	
	as % of gross domestic product									
Trade balance (fob/cif)	−5,4	−2,4	−2,5	−2,1	−2,4	−2,3	−2,8	−2,3	−1,8	
Current balance	−2,9	−3,1	−4,5	−3,8	−3,6	−4,1	−4,9	−4,3	−3,4	
Net borrowing of general government	−1,2	7,1	9,2	9,7	:	:	:	:	:	

1 As % of GDP.
2 Unemployment as % of total civilian labour force (SOEC definition).
3 Until 1975, M2 as defined nationally.
4 Estimates.
5 Forecasts.
Source: Eurostat and Commission services.

	(% of GDP at current prices)		
	1977	1980	1983
Current balance of payments	−4,0	−3,7	−3,8
of which:			
net interest on external debt	−1,1	−2,5	−3,9
General government net borrowing requirement	−0,5	−3,3	−9,7
of which:			
net interest on debt	0,6	−0,5	−4,4

The present policy stance is the result of a difficult choice between a limited number of available options. Although the moderate increases in nominal income now envisaged may help to sustain competitiveness and thus contribute to a lasting improvement in the conditions for growth and employment, the fall in private disposable income will evidently, in the short run, have a negative impact on demand and output and so increase unemployment. The restrictive budgetary stance will in the short run add to the deflationary impact, but should help to bring about an improvement in resource allocation.

The government considers a greater stability of the Danish exchange rate in the European Monetary System to be one of the prerequisites for the economic strategy to succeed. A devaluation of the Danish currency could compromise the incomes policy pursued, it would furthermore aggravate the burden of foreign debt and in addition the cost of government borrowing. Finally, a stable exchange rate is conducive to lower interest rates and could imply a considerable alleviation of the monetary stance, which might enable the credit policy to stimulate a rise in productive investment.

Further cuts in the central government deficit will probably necessitate vigorous attempts to restructure various public expenditure categories. It is particularly important to curb the automatic growth inherent in some expenditure, notably transfers. It implies a current adjustment of public resource utilization to demographic changes, a more direct financial responsibility by the competent public authorities, and higher charges for public utilities and services. On the receipts side, after the recent introduction of a temporary tax on pension funds, other changes in the tax structure are considered.

As improved competitiveness places a considerable constraint on the rise in domestic costs the government's investment programme, which aims to promote structural adjustment and technological innovation, is of importance for sustaining further increases in productivity.

The incomes policy drafted by the government and negotiated between the social partners is evidently of significance to the success of the economic strategy. Not only is it decisive in terms of relative labour costs, but also for the inflationary expectations. Income taxation and social transfers might furthermore be used to increase the efficiency of an incomes policy as exemplified by the proposed fiscal concessions, which are to accompany the present wage settlement. The correlation between unemployment benefits and wage levels has also been somewhat slackened due to the abolition of automatic adjustments. However, although guidelines may be useful as a framework for overall increases in pay, their application should comply with the flexibility needed on the labour market in order to promote the adjustments previously advocated and to avoid bottlenecks in any part of the labour market. Its heterogeneous character in terms of skills demanded and opportunities offered, should be reflected in a reasonably subtle wage structure.

Federal Republic of Germany

Trends and prospects

Early last year it was expected that economic activity would pick up gradually and that expansionary forces would gather pace in the second half of the year, so creating favourable conditions for growth in 1983. Indeed the prospects for an improvement in the economic situation were quite promising.

(i) The current account had steadily climbed out of its record deficit and the Bundesbank was able to take cautious steps to relax the restrictive stance that it had taken for external reasons. From the turn of the year, its course was to expand central bank money stock, aiming for the upper part of the target range; as early as October 1981 it had started to use its room for manœuvre to bring down interest rates.

(ii) In the field of fiscal policy, in the framework of 'Operation 82', [1] steps were taken to reduce, in the medium term, that part of the central government deficit which does not automatically disappear when utilization of productive potential improves. It was also thought that more favourable depreciation arrangements would increase the propensity to invest in industry and residential construction. As the year progressed, however, it became apparent that the originally targeted deficits were running into danger on both the revenue and the expenditure side, and controversy developed with respect to the thrust of fiscal policy, including the decision on the 'additional investment allowance'.

(iii) Wage settlements were lower than the expected rise in prices and signalled a general consensus on the adjustment of primary income distribution.

The actual out-turn was, however, in stark contrast to what had been hoped for. Gross domestic product declined only slightly in the first half-year, but then sagged abruptly in the second half-year (down 3% at an annual rate).

From the start of the year, foreign orders began to drop off steadily, and goods exports followed suit in the spring.

[1] When the Federal budget for 1982 was put together, the phrase 'Operation 82' was used to refer to a number of laws to improve the budget structure of central and local government and to improve investment conditions. The Sachverständigenrat ('Five Wise Men') estimates that these measures have cut the structural deficit by some DM 7 000 million.

Foreign orders and goods exports

(seasonally adjusted % changes, at annual rates)

	IV-1981	I-1982	II-1982	III-1982	IV-1982 [1]
Orders	4,4	− 6,3	− 30,6	− 13,6	1,2
Exports (volume)	3,0	13,4	− 12,6	− 10,5	− 4,6

[1] Estimate.

Thus, before the upward movement of sales abroad, which up to that point had underpinned German economic activity, could spark off a revival of domestic demand, exports fell back. Production remained at a high level until almost the middle of the year and, as a result, stocks built up substantially and unintentionally. No favourable stimulus came from domestic demand. The business climate deteriorated dramatically. It was therefore unavoidable that output would adjust to declining demand from the second quarter of the year.

Output in manufacturing industry, excluding construction

(seasonally adjusted % changes, at annual rates)

	IV-1981	I-1982	II-1982	III-1982	IV-1982 [1]
Production index	− 2,4	6,4	− 7,2	− 11,9	− 8,7

[1] Estimate.

Some of the conditions needed for a turn-round in the cyclical position during 1983 have continued to improve during the past year, although part of the environment is still unfavourable or has actually deteriorated.

The main determinants in the field of economic and social policy for the economic outlook in 1983 are the following:

Monetary policy is endeavouring to create sufficient scope for economic growth but without endangering the successes achieved in stabilizing prices. Given the persistent under-utilization of productive potential, the success in restoring external equilibrium as well as the favourable trends in prices and costs, the Bundesbank again set the target range for the expansion of central bank money stock for the fourth quarter of 1982 to the fourth quarter of 1983 at between 4 and 7% and announced its intention of aiming initially for the upper part of the target range. This implies that the Bundesbank would use any room for manœuvre to bring down interest rates further.

Budgetary policy is facing two ways at once. The government continued along its chosen path of reducing the hard core of the government deficit, but is willing to make room for additional expenditure in view of the level of capacity utilization. Reduction in the 'structural' deficit has been possible as a result of a two-pronged strategy of restricting social benefits and increasing social security revenue; [1] this has had the effect of dampening down domestic demand. These restrictive factors are, however, offset by the considerable stimulatory effects of a package of measures to encourage residential construction. The change in the tax on industry and trade will also help to improve company profits and supply-side conditions.

Wage settlements are reflecting the difficult economic situation. The advance announcement by the public employers to the effect that civil service pay and pensions would go up by only 2% at mid-year 1983 was no doubt also helpful in this respect.

However, the world economic situation still presents considerable risks.

This year's forecast points to an increase in real GDP in the course of 1983, but still implies a small reduction on a year-on-year comparison as a result of the low level of activity at the end of 1982.

A turn-round in the downward trend in private consumption is expected in the second half of 1983. It is assumed that the decline of 3½% in the volume of private consumption in the two years 1981 and 1982 has already required a considerable adjustment on the part of households, and that certain limits are set on their flexibility, so that the decline in the personal savings ratio, already evident in 1982, is expected to continue. As the year progresses, the assumption therefore is that an expected further small decline will be followed by a slight increase in the second half-year (an annual rate of 0,5% at most).

Given the underutilization of capacity, the prospects for a significant turn-round in demand for plant and machinery are still unfavourable. However, the passing of the 31 December 1982 deadline for claiming the 'additional investment

Private consumption at 1976 prices

(DM 1 000 million)

1977	1978	1979	1980	1981	1982	1983 [1]
657	681	702	713	704	688	682

[1] Estimate

allowance' had the desired effect on new orders. The government measure certainly had the effect of bringing forward investment demand, and this is likely to be followed by a gap in orders. Companies as a whole are, however, facing a markedly better profit situation, their self-financing capacity will improve, the fall in interest rates will ease financing costs perceptibly, and the attractiveness of investing in financial assets as compared with physical capital will diminish further. As the year progresses, equipment investment will therefore tend upwards and, on a year-on-year comparison, will fall no further. The improvement in the business climate, as expressed in the surveys of the Ifo Institute for Economic Research, goes a long way to support this estimate.

Overall, economic growth is certainly likely to receive a considerable boost from construction investment. All the data point to the fact that the cyclical trough has been passed in the construction industry. The turn-round in trend is particularly evident in residential construction. This development has been helped by a marked fall in interest rates (mortgage interest rates are more than 3% down on their 1981 peak), the favourable price situation in the building industry and above all the government measures. For 1983, a sharp increase in investment in residential construction is therefore to be expected, and it is assumed that last year's 5,6% decline will be followed by an increase of 5% or so this year.

For public investment, however, a further slight real decline seems unavoidable (a fall of 1% as against one of 8,8% in 1982). Public investment in construction in real terms has fallen by a total of 16,7% in three years and is now at a level comparable with that of 1965.

Slack domestic demand is again putting pressure on domestic producers to export. Given current trends in

Public investment in construction at 1976 prices

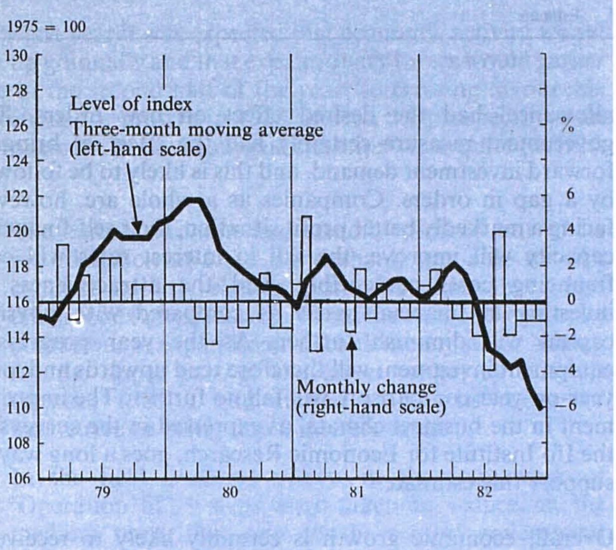
(DM 1 000 million)

1965-69	1970-74	1975-79	1980	1981	1982	1983 [1]
31,2	36,8	35,7	37,3	34,6	31,7	31,4

[1] Estimate.

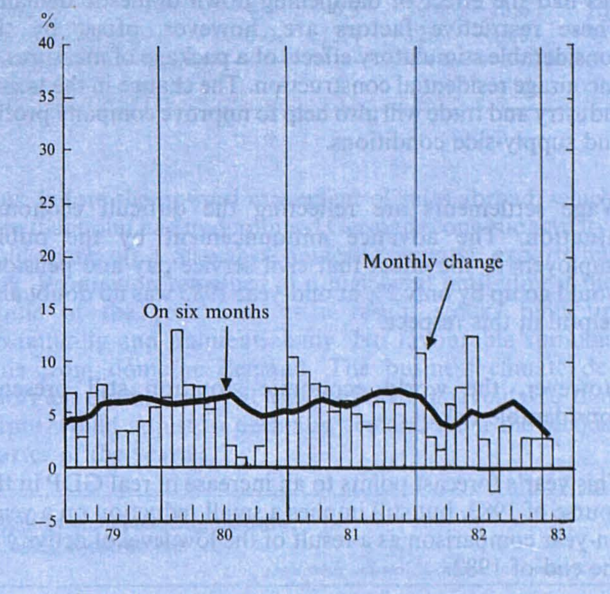
[1] The most important of these measures are:
(i) the postponement of the pensions increase from 1 January to 1 July. Pensioners will also have to pay a contribution to medical insurance: on 1 July this will be 1% of their pension and this will go up to 5% by 1985;
(ii) the bringing-forward of the ½% increase to 18,5% in pension insurance contributions by four months to 1 September;
(iii) the reduction of family allowances for higher income families;
(iv) tighter eligibility requirements for unemployment benefit, and a strengthening of the principle of payment for services rendered. Unemployment insurance contributions were raised by 0,6% from 1 January, half the increase to be borne by employers and half by employees.
The Sachverständigenrat estimates that these measures taken together will further cut the structural deficit by some DM 7 000 million.

Federal Republic of Germany: Industrial production (s.a.)



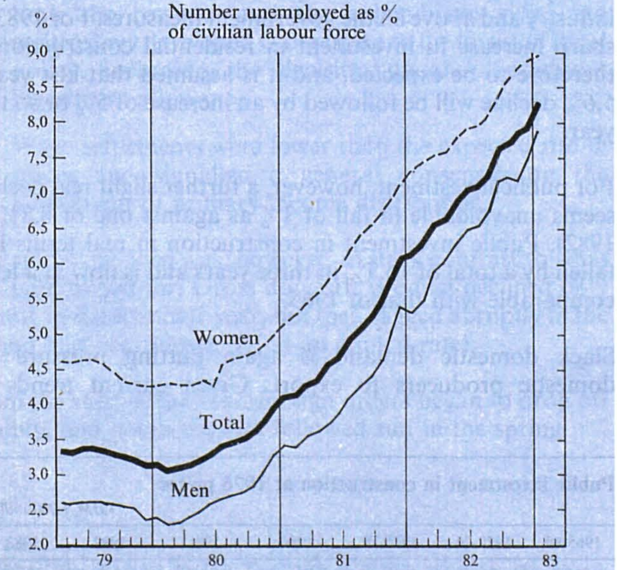
Source: Deutsche Bundesbank.

Federal Republic of Germany: Consumer prices (s.a.)



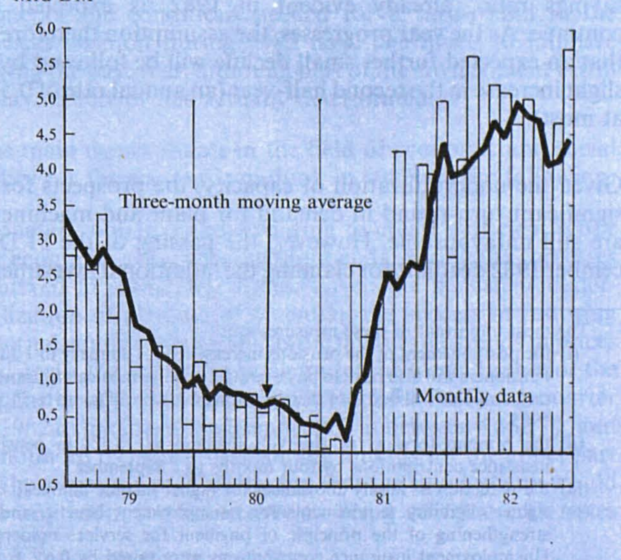
Source: Eurostat.

Federal Republic of Germany: Unemployment (s.a.)



Source: Eurostat.

Federal Republic of Germany: Trade balance (s.a.)



Source: Eurostat.

Federal Republic of Germany: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					
	1971-80	1981	1982[4]	1983[5]	1981	1982[4]		1983[5]		1981
					II	I	II	I	II	DM '000 million at current prices
	% change over preceding period at annual rates — at constant 1975 prices									
Private consumption	2,9	−1,2	−2,2	−0,9	−0,7	−2,5	−3,3	−0,3	0,2	874,1
Public consumption	3,2	2,0	0,1	0,0	−1,3	1,5	−1,1	0,3	0,5	319,8
Gross fixed capital formation	1,5	−3,8	−6,2	2,0	−1,9	−10,5	−1,4	2,9	3,8	339,3
Change in stocks[1]	0,8	−0,1	0,5	0,4	−0,9	1,0	0,1	0,2	0,6	−1,4
Domestic demand	2,5	−2,4	−2,0	−0,3	−4,2	0,3	−4,2	0,7	1,9	1 531,7
Exports of goods and services	5,1	8,1	2,8	0,6	14,8	2,1	−6,7	2,8	3,8	461,1
Imports of goods and services	5,1	−0,7	−0,2	0,4	−3,2	7,4	−11,1	4,4	5,2	448,8
GDP at market prices	2,5	0,1	−1,0	−0,2	0,8	−0,9	−3,1	0,4	1,6	1 543,9
	% change over preceding period at annual rates									
GDP at current prices	7,4	4,2	3,7	3,6	5,8	2,9	3,4	3,3	5,0	
Industrial production[2]	1,7	−1,5	−2,5	−1,0	0,0	−1,9	−6,2	0,5	1,4	
Unemployment rate[3]	2,7	4,7	6,8	8,9	5,4	6,3	7,3	8,4	9,3	
Compensation of employees	8,0	4,7	2,4	1,8	6,2	1,1	1,3	1,9	2,1	
M3	9,8	6,5	6,5	6,3	4,7	7,7	6,0	6,0	7,1	
GDP (implicit price index)	4,7	4,2	4,8	3,9	4,9	4,0	6,0	2,8	3,4	
Private consumption (implicit price index)	4,5	6,0	5,3	3,7	7,1	4,5	5,2	3,3	3,0	
Exports, goods (implicit price index)	4,5	6,0	4,3	2,5	12,4	1,8	2,1	3,2	1,3	
Imports, goods (implicit price index)	5,6	10,4	2,1	1,0	9,1	−0,3	0,2	1,4	1,0	
Terms of trade	−1,0	−3,9	1,8	1,5	−4,6	5,6	1,4	1,4	1,8	
	as % of gross domestic product									
Trade balance (fob/cif)	2,9	1,5	2,8	3,2	3,2	3,4	3,7	4,0	3,9	
Current balance	0,6	−1,1	0,5	0,6	:	:	:	:	:	
Net borrowing of general government	−2,1	−4,0	−3,9	−4,1	:	:	:	:	:	

1 As % of GDP.
2 Manufacturing industry.
3 Unemployment as % of total labour force.
4 Estimates.
5 Forecasts.

Source: Eurostat; Commission and national services.

competitiveness, German exporters are therefore likely to take a more than proportionate share of the expected increase in world trade. Import volume will grow less than export volume. World market prices will lead to a further improvement in the terms of trade, and the corporate sector will benefit from the distributive effect. This, plus the continuing favourable trend on the tourism account, will again improve the current balance.

The rates of increase of prices and costs are, broadly speaking, on the decline. Even taking account of the increase in value-added tax in the middle of the year, it is assumed that the private consumption deflator will increase by 3,7%.

Problems of economic policy

The gains made in reducing inflation, and in achieving a more satisfactory external position, following three years of substantial deficits on current account, have contributed to a change in the stance in economic policy.

The low level of economic activity from 1980 onwards and the structure of expenditure and revenue established in earlier years, when the growth performance was more favourable, have contributed to high levels of borrowing by general government. These high levels, it is argued, have had an adverse impact on financial markets with the government crowding out the private sector from sources of capital finance. In responding to these criticisms, and in considering how borrowing could be reduced, attention has been focused upon the underlying or structural deficit of general government, which can only be reduced over the medium term, in contrast to short-term variations in borrowing, reflecting changes in economic activity, which should be accommodated.

Consequently, in their recent formulations of fiscal policy, the authorities have sought to:

(i) adapt the trends of expenditure and revenue so as to reduce the structural deficit;

(ii) ensure that the structure of expenditure and taxation improves the conditions for economic growth and employment over the longer term.

These objectives remain of importance in determining the form of budgetary policy for 1983 and later years. According to the authorities, an overall contribution to achieving both objectives and to strengthening financial confidence will be made if plans for general government expenditure ensure that its level, as a proportion of GDP, is steadily reduced. At the same time, despite the weakness of activity, tax rates should be set so as to stabilize or even reduce the level of general government borrowing, as a percentage of GDP. In addition the structure of expenditure should continue to favour investment and support the development of high technology programmes in areas such as communications and transport.

The further reform of the social security system can also make a significant contribution towards controlling general government expenditure and borrowing. Such a move would be a response to the widely held view that, in certain aspects, the present level of provision is excessive, and reduces the flexibility of the labour market.

A satisfactory control of general government expenditure and borrowing should increase further the room for manœuvre in monetary policy which has already been substantially extended by the fall in the rate of inflation and the improvements on the external side. Indeed, the conduct of monetary policy in the course of 1982 and early 1983 has already begun to reflect the increased preoccupation with growth and employment, and through 1982 the expansion of the central bank money stock (CBM), remained at the top of the official target range of 4-7%. For the year to the fourth quarter of 1983 the authorities have announced that the target range for the CBM remains at 4-7%. This choice reflects a number of considerations:

(i) the marked easing of inflationary pressures,

(ii) the need to provide scope for a significant expansion of economic activity at a time when the level of capacity utilization is low,

(iii) the likelihood that the velocity of circulation of money will decline as interest rates fall.

Indeed, the rate of inflation, inflationary expectations and general financial confidence, and the external position both on current and capital accounts are now favourable and point to the likelihood of a decline in nominal and real rates in the period ahead.

The possibility of a fall in the velocity of circulation underlines the importance of managing the growth of the monetary aggregates, through 1983, so as to make the growth of the CBM consistent with a further fall in interest rates and the potential for expansion in the real economy.

Lower interest rates are particularly vital for ensuring a strong and sustainable recovery in investment. In this context it is important that real rates of return to productive assets should compare favourably with real rates of interest obtainable on low-risk financial assets (in particular on government bonds), so facilitating a recovery of industrial investment.

As regards incomes policy, in the view of the authorities, two particular developments could make a significant contribution to achieving price competitiveness, a flexible arrangement for earnings, and sufficient incentives to effort namely:

(i) a development of wages and salaries in the public sector consistent with the required reduction in the level of general government expenditure, as a proportion of GDP;

(ii) that discussions on introducing schemes permitting the more direct participation of company employees in the wealth creation process once again become an important part of the wage bargaining process.

Conversely a reduction in real wages does not seem to be appropriate. Although such an approach might seem, *prima facie*, to improve the conditions for investment, by containing labour costs, it suffers from two major disadvantages:

(i) it would have an adverse impact on demand and on the level of economic activity,

(ii) it carries the risk that during a later upswing it would be followed by a period of rapid wage inflation.

The evolution of the returns to both labour and capital in the period ahead must take account of the need to ensure that investment reaches an adequate level so as to ensure, amongst other things, that comparative advantages in exporting capital intensive and technologically advanced goods, can be maintained in world markets.

This point becomes of particular importance when the longer term is considered. In the short to medium term, demographic developments will contribute to a marked increase in the population of working age. However, from the late 1980s onwards, the composition of the population will begin to change with the proportion of older people increasing, and this is likely to be accompanied by a contraction in the labour supply. The rates of growth and levels of public expenditure required by such a situation point to the need for a capital-intensive production structure, and the development of an appropriate capital stock, which will itself depend on the investment taking place from now on.

Encouraging investment and increasing the investment share in GDP seems therefore to be an optimal policy objective. Clearly a fall in interest rates and inflation, and an economic policy that permits the required returns to capital and the appropriate productivity gains to be made, will make an important contribution in this regard. There are in addition a number of other measures that can be taken that reduce the restrictions on investment and adjust, in a favourable way, real rates of return. These include removing bureaucratic obstacles to investment, establishing the most favourable tax regime, and restructuring the present framework of grants and subsidies.

Though it may be appropriate to consider plans for increasing public sector investment there is no clear case for giving a further stimulus to activity in the house building industry. Indeed it is widely argued that the policy measures taken in 1982 to promote activity in this sector, were excessive, given the recovery in output already under way, and there is now even a risk of substantial inflationary pressures developing.

Even if the authorities achieve their objectives with regard to fiscal, monetary and incomes policies, unemployment is likely to remain high in the period ahead. Hence the question arises whether it would be appropriate to consider specific actions in this regard.

It is frequently suggested that working time should be further reduced, by varying the length of the working week and by varying the age of retirement, both because this would increase the demand for labour, and because this is a desirable end in itself. Such proposals have implications for industrial costs and point to the need for corresponding changes in labour productivity, and labour mobility, to compensate for any inflationary pressures that might arise. In particular, in the past, reductions in working time have occurred in periods of faster economic growth and the experience then gained is not necessarily a guide to what might occur now, when growth is slower. Moreover, an adjustment of working time arrangements would need to be flexible, to allow for the contraction in the labour supply foreseen, in the Federal Republic, in the late 1980s, and should also contribute to the general objective of improving the supply side conditions of the economy.

Growth potential and structural adjustment in the Federal Republic of Germany

The concept of growth potential

The growth potential of the country's economy is defined as the hypothetical change in gross domestic product that would be possible if the factors of production available in the economy were being consistently utilized at high levels. This concept does not therefore take account of cyclical fluctuations in factor utilization and indicates the possibilities of expansion in an economy's productive capacity, free from cyclical movements. However, the growth potential revealed by such a measure, is not insensitive to fluctuations in the degree of utilization of productive potential. Because of the strong positive correlation between growth rates of GDP and of investment, i.e. the creation of additional productive capacity, high GDP growth generates high growth potential whereas an economic downturn not only causes capacity to become idle but also reduces the future growth potential.

The most common estimating procedures

The concept of productive potential, whose annual rates of change reflect long-run growth possibilities, was first introduced into the general debate in 1967 by the Sachverständigenrat ('Five Wise Men') which draws on empirical and theoretical groundwork carried out by the Deutsches Institut für Wirtschaftsforschung (DIW) in Berlin. Since the Bundesbank's decision in 1974 to announce its money supply targets in advance, special importance has attached to the calculation of the economy's productive and growth potentials, made and published by the Bundesbank and used by it as a factor in determining money supply growth. The two estimating procedures use different methodologies. Their essential features can be summed up as follows:

According to the *Sachverständigenrat*'s methodology, the production potential is defined as the aggregate of the potential value added of firms, of the government sector, of the housing sector and of private households and organizations. For the non-enterprise sectors it is then assumed that their production potential is fully exhausted and therefore is equal to their contribution to gross value added. The main estimation problem hence rests with the potential output of firms. The Sachverständigenrat, and the DIW, base their ideas exclusively on the stock of gross capital disposable at a particular period and on the productivity of the capital stock when capacity is fully used. The potential output is thus limited by the amount of the available capital stock. The labour input needed to achieve the potential output—the employment potential—is then estimated, in a subsidiary calculation, via the average capital intensity.

In addition to the problems of assessing the gross capital stock, the estimation process concentrates on the potential productivity of capital. This is derived from a trend-function of the empirically measured capital productivity. In this way capital productivity also reflects various factors such as structural change, reduction of working hours, factor substitution and technical progress.

The *Bundesbank* defines the production potential as the gross domestic product that can be attained when the available factors of production work together at normal capacity utilization, taking account of technical progress. In the bank's concept, the country's production possibilities could be mapped with a production function of the Cobb-Douglas type, in which the available supply of labour (measured in hours), the economically usable gross capital stock and—as a most recent development—the availability of energy constitute the factors of production. Technical progress is taken as autonomous, and hence does not depend upon the level of gross fixed capital formation; and the capital stock is taken as homogeneous in that its age structure has no direct effects on potential output.

The assumption of a Cobb-Douglas production function further implies an *ex post* substitutability between the factors of production. The available units of the production factors can at any time be fully exhausted in the production process. In this approach the problem of structural unemployment does not so much result from a shortage of capital stock, as is the case in the Sachverständigenrat's analysis, but is rather a question of relative sector prices. Some arguments suggest, however, in an *ex post* consideration to look at the capital stock as a limiting factor, which cannot be combined with a variable quantity of the labour force. The estimation method of the Bundesbank could therefore lead to an overestimation of the Federal Republic's production potential in the case of structural unemployment.

Declining growth potential

In spite of their differing approaches, the two methods of estimation paint much the same picture of the trend in the growth potential of the German economy.

Both methods reveal a very pronounced contraction of the growth potential since the first oil crisis in 1973. In the years 1974-79, potential growth rates were some 1,8% lower than the average for the period 1962-73. Following the second oil price shock, growth potential seems to have been further squeezed, but to an extent that cannot yet be fully measured. The observed and expected rates of fixed capital formation suggest, however, that

Average annual growth rate of productive potential and GDP in the FR of Germany

(%)

	1962-67	1968-73	1974-79	1980-83
Sachverständigenrat	4,5	4,1	2,3	1,7
Bundesbank	4,2	4,5	2,7	2,0
GDP (at 1976 prices)	3,5	5,0	2,4	−0,4 [1]

[1] Commission estimate.

the potential growth rate at present and in the near future is significantly less than 2%.

In addition to the decline in fixed capital formation since 1980, the growth prospects of the German economy are also affected by structural problems due mainly to the redistributive effects of the two oil price shocks at world level and to the emergence of new competitors on the world market.

It is assumed for example that the disturbances in the structure of factor prices and the associated shifts in the pattern of demand have destroyed some of the productive potential in the economic sense. The Bundesbank [1] in particular believes that part of the stock of fixed capital, although technically operational, can no longer be put to profitable use. The need for structural adjustment, reinforced by the fall in demand since the second half of 1980, is particularly evident in the steel sector, where existing capacities can no longer be utilized and where plant closures, and adjustments of the plant retained, have become inescapable.

On the other hand, the effects on productive activity of the increasing number of business failures in recent years have probably been exaggerated. In attempting to quantify the 1982 loss of fixed capital attributable to insolvencies, the DIW comes to the conclusion that, at most, 0,3% of all firms' gross fixed capital was affected and that the impact on growth potential was therefore small. [2]

However, it is not only the phenomenon of declining potential growth rates that clearly distinguishes the period since the first oil price shock from earlier years, but also the gap that has consistently been recorded between actual GDP and the level made possible by the factor endowment of the German economy. Even in the period from the second half of 1978 to the first half of 1980, when economic growth rates were generally satisfactory (averaging 4,5% in annual rates), productive potential was never fully utilized. The Ifo Institute estimates that, even at the peak of the most recent upswing (1979), the degree of capacity utilization was some 6% lower than at the time of the 1969/70 boom. The shape of the productive potential curves constructed by the Sachverständigenrat and by the Bundesbank (see Graph 1) might therefore be taken to indicate that, since 1979, Germany has been unable to make full use of its productivity and growth potentials. But there is much to suggest that the 6% of unused capacity consists of plant that can never again be put to profitable use because of its low productivity and that the situation is one of structural overcapacity [3] ('structural unemployment' of fixed capital) that is complementary to structural unemployment in the labour force.

1 Deutsche Bundesbank, 'Neuberechnung des Produktionspotentials für die Bundesrepublik Deutschland', *Monatsberichte*, Vol. 30, No 10, October 1981.

2 DIW, 'Insolvenzen: Nur geringe Auswirkungen auf Produktionspotential und Arbeitsmarkt', *Wochenbericht*, 45/82.

3 See K.D. Schmidt, 'Das Produktivitätspotential der deutschen Wirtschaft', *Die Weltwirtschaft*, 1981, No 1, Tübingen 1981.

Reasons for the decline in growth potential

One of the main reasons for the marked contraction of growth potential has been weak investment demand (i.e. a shortage of new and more efficient plant) which also became apparent at the time of the first oil crisis. In the period 1962-71, real gross fixed capital formation thus grew at an average annual rate of 4,5%, compared with an annual rate of only 0,6% or so in the 10-year period to 1981.

The depressed level of investment activity resulted in a steady, relative fall in net additions to the economy's stock of fixed capital. The share of annual gross fixed capital formation that simply served to offset capital consumption climbed from around 30% of the volume of gross investment in 1960 to 57% in 1981. In absolute terms, net fixed capital formation, i.e. the effective expansion of the productive apparatus, was actually lower in the 1970s than in the 1960s (annual growth rate of 3,0% in the period 1962-71, compared with a rate of −2,7% in the period 1972-81). Graph 2 shows the trend in gross fixed capital formation (as % of GDP) and the trend in capital consumption (as % of gross fixed capital formation) for Germany and for a number of other industrialized countries. As the time paths of these variables for France and the United Kingdom show, the tendency for net capital accumulation to slacken is not confined to Germany. The curve for Japan, on the other hand, contrasts sharply with the typical curve for the European Community. The comparatively vigorous expansion of the capital stock in Japan, reflected in the curves, clearly explains much of the success of Japanese manufacturers on world markets.

Because of this trend, Germany's growth potential diminished and German industry's stock of fixed capital became increasingly aged. The 'degree of up-to-dateness' of the stock of fixed capital in manufacturing, defined by taking the quotient of the existing stock of net fixed capital and the existing stock of gross fixed capital, [4] has fallen steadily.

The view that the current structural crisis and growth crisis can be overcome only if we manage to reverse the process of ageing industrial plant now commands widespread support.

4 The stock of gross fixed capital is the sum of all the original values of existing plant adjusted using a common price base; this aggregate less cumulative capital consumption up to the moment of observation gives the stock of net fixed capital.

Degree of up-to-dateness of the stock of fixed capital in manufacturing

(%)

1960	1970	1973	1975	1978	1981
67,9	63,0	62,7	60,9	58,0	56,8

Source: DIW.

The quality of productive plant in individual branches of industry

Plant has not, of course, aged to the same extent in all branches of industry. The DIW has published figures on the degree of up-to-dateness in 35 branches. [1] According to its calculations, the age structure of the capital stock improved in the period 1970-81 in only two branches, namely coal mining and oil and natural gas production and refining. However, since they occurred only in the second half of the 1970s, these improvements are undoubtedly positive adjustment responses aimed at securing more efficient utilization and allocation of energy.

The up-to-dateness of plant has deteriorated in all other branches of industry, but the phenomenon was less pronounced in the capital goods industry than the average for industry as a whole. The most unfavourable structure is found in those branches which have little, if any, scope for product diversification and innovation and which use predominantly traditional processes. Since Germany's natural factor endowment in these branches is such that it does not enjoy any comparative advantage, they are in jeopardy across their entire product range. Consistent with this picture is the fact that the leather processing industry, for example, possesses a significantly better age structure than the leather production industry, that the textile industry is in a much worse position than the clothing industry and that the shipbuilding industry has a much poorer age structure than the other capital goods industries. The trend in the age structure of plant and machinery in industry illustrates these findings very clearly. The following table compares for 1978 the age structure in the branches with particularly weak structures and growth with the situation in a number of 'strong' branches. [2]

It is also worth noting that none of the branches of manufacturing products with a particularly high technology content, in which the Federal Republic of Germany probably enjoys a comparative advantage and which are regarded as future engines of growth, has improved the age structure of its capital stock since 1970. However, the statistical breakdown by branch is presumably too rough to identify the real growth points. Since it is only very rarely that a particular branch of industry has to cope with positive or negative structural changes across its entire product range, a breakdown into only 35 to 50 branches will be insufficient to bring to light changes within sectors.[3]

1 DIW, *Produktionsvolumen und -potential, Produktionsverfahren des Bergbaus und des verarbeitenden Gewerbes in der Bundesrepublik Deutschland*, Berlin, October 1982.

2 E.R. Baumgart, 'Zur Entwicklung der Altersstruktur des Anlagevermögens in der Industrie der Bundesrepublik Deutschland', *Empirische Wirtschaftsforschung*, ed. J. Frohn and R. Stäglin, Berlin 1980.

3 H.R. Peters, 'Strukturdiagnosen und -prognosen als wirtschaftspolitische Entscheidungshilfen', *Wirtschaftsdienst*, Vol. 61, No 1, Hamburg 1981.

Aspects of the age structure of industrial plant and machinery (for two age categories)

(as % of total plant and machinery)

	5 years or under	11 years or over
Weak branches		
Flour milling	11,6	75,7
Iron ore extraction	13,9	71,2
Leather production	16,7	60,1
Cellulose and paper	19,6	50,1
Textiles	19,9	50,5
Strong branches		
Plastics processing	36,8	27,8
Office machinery and data-processing equipment	36,4	28,1
Precision engineering, optical instruments	35,9	35,0

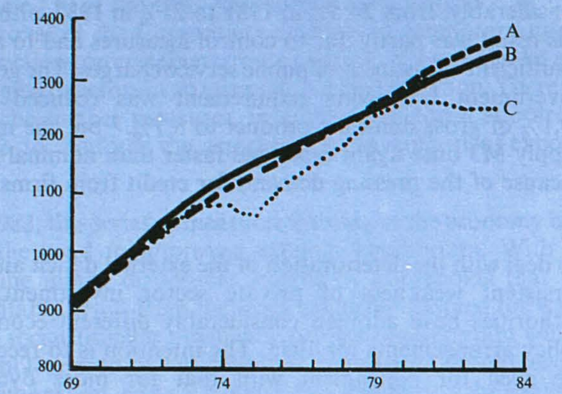
Source: Baumgart (see footnote 2 on this page).

Ageing of the capital stock as observed here for German industry has not, however, occurred in the service sector (or has occurred there only to a comparatively minor degree). In the 10 years up to 1981, growth rates in gross fixed capital in transport, banking, insurance and in other service enterprises were quite comparable with those recorded in the 1960s. The dynamic growth of the service sector in the 1970s is also to be seen as an adjustment response to the 'overindustrialization' that took place in the 1960s as a result of the continuing competitive edge conferred by the exchange rate. It is quite normal that a relationship should slowly emerge between the production of goods and the supply of services that corresponds to the international norm and is broadly consonant with the stage of maturity of the economy. This must not, however, allow us to lose sight of the need to expand and renew the capital stock in industry. The pressing problems of the medium-term trend in the labour force, the preservation of living standards, the satisfactory functioning of the social welfare system and, last but not least, the maintenance of a healthy environment can be resolved only if the basic growth potential is reinforced and resolutely adapted to the new supply and demand conditions on world markets and to technological development. These fundamental requirements and the obstacles to investment that need to be removed were set out in detail in the Commission's communication to the Council of 8 June 1982. [4] The Commission also put forward practical proposals for boosting investment in its communication of 14 October 1982. [5]

4 COM(82)365: Commission communication to the Council on the problem of investment.

5 COM(82)641: Commission communication to the Council on initiatives for promoting investment.

GRAPH 1: **Trends in productive potential and in GDP in the Federal Republic of Germany (in DM '000 million; at constant 1976 prices)**



A: productive potential as calculated by the Bundesbank.

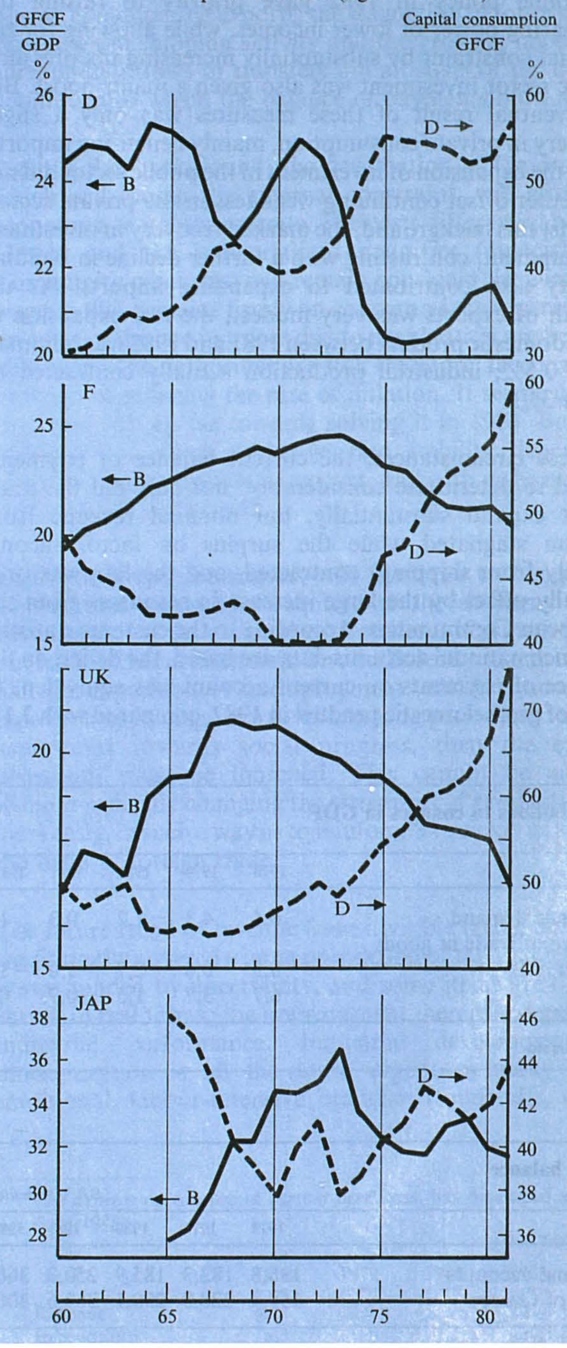
B: productive potential as calculated by the Council of Economic Advisers.

C: real GDP.

GRAPH 2: **Trends in gross fixed capital formation (as % of GDP) and in capital consumption (as % of gross fixed capital formation)**

B: gross fixed capital formation as % of GDP (left-hand scale).

D: capital consumption as % of gross fixed capital formation (right-hand scale).



Greece

Trends and prospects

Economic policy in 1982 gave priority to raising the purchasing power of lower incomes, while allowing for the external constraint by substantially increasing tax pressure. Public sector investment was also given a major boost. But the eventual result of these measures was only a slight recovery in private consumption, mainly benefiting imports, while the expansion of investment in the public sector did not altogether offset continuing weakness in the private sector. Against this background, the marked recovery in investment in equipment, contrasting with a further decline in building activity also contributed to expanding imports. As the growth of exports was very modest, the real expansion of gross domestic product between 1981 and 1982 was minimal: some 0,5%; industrial production actually contracted by about 3%.

In these circumstances, the current balance of payments tended to deteriorate considerably: not only did the trade deficit expand substantially, but nominal revenue from tourism stagnated while the surplus on factor income (mainly from shipping) contracted, and the loss was only partially offset by the large increase in resources from the European Communities. According to the customs statistics on which national accounts data are based, the deficit on the balance of payments on current account was equivalent to 5,6% of gross domestic product in 1982, compared with 2,1% in 1981.[1] The net inflow of private capital, moreover, declined sharply.

However, there was some progress toward reducing internal imbalances. The rise in consumer prices slowed down considerably, from 24,5% in 1981 to 21% in 1982, although this result was partly due to control measures and to as yet insufficient adjustment of public service charges. The general government borrowing requirement was reduced from 10,1% of gross domestic product to 8,7%,[2] but the money supply M3 once again expanded faster than nominal GDP because of the pressing demand for credit from firms.

To deal with the deterioration of the external deficit and the persistent weakness of private sector investment, the authorities have adopted considerably different economic policy arrangements for 1983. The intention is to reconcile the need for adjustment with that for more dynamic investment. The main feature of the arrangements is a strict wage policy that severely limits indexation, reinforcing the regressive effect by maintaining the initial definition of brackets for indexation, and also by delaying application of the arrangements.[3] To compensate for this, price controls introduced in 1982 have been tightened, while taxes on certain basic consumer products have been maintained. Budgetary policy will be geared to stabilizing the deficit as a percentage of nominal gross domestic product, and to effecting a major increase in investment expenditure by using up all the extra resources made available by the large increase in revenue and the compression of current expenditure. Of particular relevance here are the financial incentives to private investment provided for in the law of June 1982, by which investments are extremely finely graded according to a set of economic, sectoral and regional criteria. As to monetary policy, the quantitative aims adopted point to money supply (M3) growth at a rate slightly faster than that of nominal GDP, which implies that firms will have fairly easy access to credit. In exchange-rate policy, the strategy of

Contributions to changes in GDP

	1978	1979	1980	1981	1982[1]
Domestic demand	6,4	4,3	−1,2	0,3	1,6
Balance of trade in goods and services	0,3	−0,6	2,7	−1,0	−1,2
GDP	6,7	3,7	1,5	−0,7	0,4

[1] Estimates.

Trade balance

(DR '000 million)

	1978	1979	1980	1981	1982[1]
National accounts	136,8	182,3	185,9	250,3	366,0
Bank of Greece	159,4	228,8	290,1	369,6	406,0

[1] Estimates.

[1] This deterioration is not apparent in the Bank of Greece statistics referring to settlements, which show a marked reduction in the negative position evaluated in dollars, and indeed a slight reduction in drachmas, compared with the major deficits of the preceding two years. The contradiction is mainly due to the way in which oil imports are accounted for, since large quantities of oil were paid for in advance in 1981 but not actually imported until 1982.

[2] In terms of national accounts. The deficit in terms of budget accounts declined from 11,8% in 1981 to 9,4% in 1982.

[3] Increases in the index are fully reflected in monthly wages of up to DR 35 000; wages between DR 35 000 and DR 55 000 are increased by an amount equal to half the percentage increase of the index, and wages between DR 55 000 and DR 80 000 by an amount equal to a quarter of that percentage; wages over DR 80 000 are not increased. The amounts corresponding to the period from September to December 1982 will be paid in two instalments, on 1 January and 1 May 1983; those covering the period from January to August 1983 will be paid on 1 September 1983.

gradual depreciation followed previously was abandoned with the devaluation of the drachma, by 15,5%, in early January 1983. This devaluation restored at a stroke the competitiveness lost by the economy because the exchange rate did not fall far enough in view of the inflation-rate differential. At the same time, it was decided to resort to Article 130 of the EEC Accession Treaty, to apply, with the approval of the Community authorities, temporary import restrictions on certain narrow categories of products, so as to safeguard sectors in an especially critical situation. There will also be further measures, in addition to those adopted in 1982, to reinforce the arrangements in support of exports.

In 1983, this series of measures should put the economy back on the road to improved external equilibrium. With the decline in the disposable income of households that will inevitably result from the strict measures adopted for wages and social transfer payments, private consumption will no doubt lose momentum. However, investment should recover to some extent, although how far will depend on the results of the current policy of incentives, which are difficult to predict in the short run. It is expected, on the other hand, that the combined effects of languishing consumption and of devaluation will lead to a marked improvement in the real balance of external trade, due as much to a contraction in the volume of imports as to an expansion in the volume of exports, which will continue to be adversely affected by the international environment. The improvement should more than offset the falling off of domestic demand, and enable the economy to expand slightly faster in 1983 than in 1982, although, probably by hardly more than 1 %.

Expected nominal trends will still, however, be well short of eventual targets. Not only will the devaluation hamper the decline in the rate of inflation (which could once more exceed 20% in 1983), but the nominal trade deficit and the balance-of-payments deficit on current account will probably remain large, although as a percentage of GDP they should decline appreciably.

Price competitiveness index [1]

(average for 1970-75 = 100)

1978	1979	1980	1981	1982
98,0	102,3	93,5	99,6	108,9

[1] Calculated on the basis of unit labour costs in 19 industrialized countries and of the effective exchange rate of the drachma.

Problems of economic policy

The development that led to the devaluation of the drachma in January 1983 highlighted not only the major deterioration in the economy's price competitiveness but also the fragility of the structure of foreign trade in an increasingly difficult international environment. The penetration of imports, the obstacles hampering exports, the stagnation of tourism, [1] the slowdown in shipping activity and the growing uncertainty surrounding flows of transfers are all signs of the difficult conditions to which the balance of payments must adjust.

Against this background, the devaluation of the drachma, which will loosen the external constraint, will afford the economy a temporary respite. The costs differential between Greece and the industrialized countries (especially the Community countries) will remain considerable, even if the wages policy remains firmly on course and the repercussions on costs of the rise in prices due to devaluation are kept to a minimum. The authorities are still, therefore, faced with the problem of reducing the rate of inflation. It seems unlikely that they will go far towards solving it in 1983. But price stability, on which exchange rate stability depends, is required if investment is to recover, and with it the medium-term outlook for growth.

Inflation, if not moderated, will continue to hamper the considerable adjustment required of the economy by the development of the external environment. If growth is to be put back in the medium term on a sufficiently strong trend to halt the expansion of unemployment (which is now rising rapidly after having been low for a long period) and to fulfil aspirations towards social progress, then the external constraint must be loosened. This cannot be achieved without radically changing the structures of production and marketing, in such a way as to reinforce as quickly as possible the basis of foreign trade.

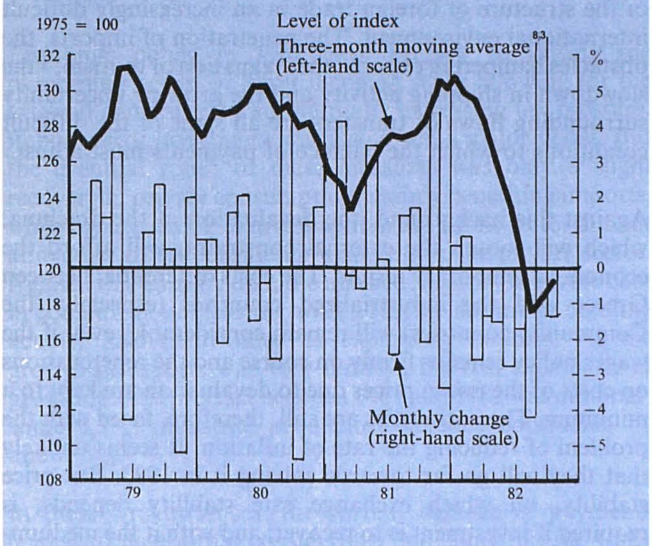
The future trend of revenue from invisible trade, which has traditionally covered a large proportion of the visible deficit, is surrounded by uncertainty, and some items are likely to shrink in real terms; the improvement therefore depends on industrial performance. Industrial development and modernization is all the more urgent as many of the traditional, labour-intensive branches (foodstuffs, current

[1] The balance on tourism in current drachmas, has developed as follows since 1978:

(DR '000 million)

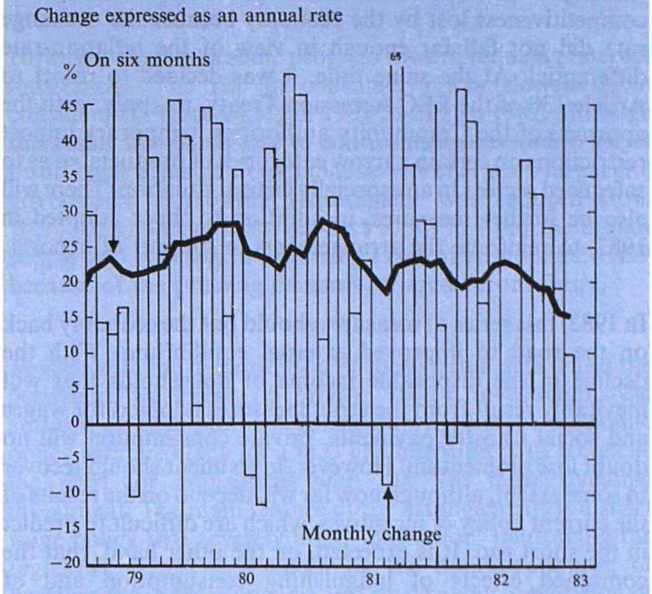
	1978	1979	1980	1981	1982
Revenue	48,2	60,9	73,2	104,0	104,0
Expenditure	8,3	11,3	13,3	20,1	25,0
Balance	39,9	49,6	59,9	83,9	79,0

Greece: Industrial production (s.a.)



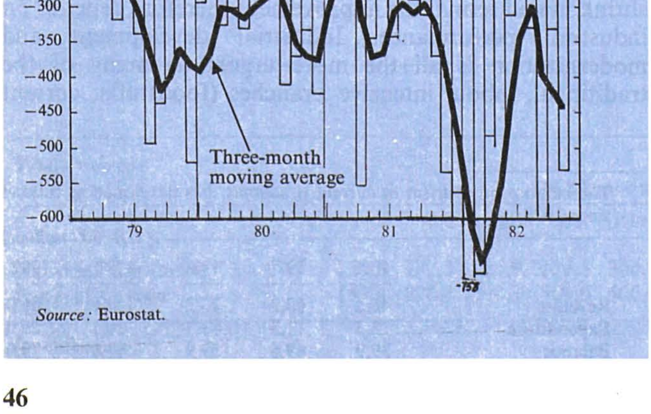
Source: Eurostat.

Greece: Consumer prices (s.a.)



Source: Eurostat.

Greece: Trade balance (s.a.)



Source: Eurostat.

consumption goods) are very old-fashioned, and cannot stand up to international competition. Industry must therefore rapidly develop new specializations and structures, at a higher technological level and with more value added. In these conditions industry can contribute to improving the terms of trade as well as the real balance.

A major and lasting investment drive will be required to modernize the industrial network, and will be the main economic policy priority of the next few years; it will have to involve infrastructures as well as plant. The medium-term plan 1983-87 will constitute, in this respect, a means of coordinating the various efforts to be undertaken and of compatibility with the overall economic context. As we have seen, the 1983 budget devotes substantial financial resources to investment; but the aim implies recovery of private investment, to which the powerful incentives provided for in the law of June 1982 should eventually contribute.

Greece: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					1981
	1971-80	1981	1982[4]	1983[5]	1981	1982[4]		1983[5]		DR '000 million at current prices
					II	I	II	I	II	
% change over preceding period at annual rates — at constant 1975 prices										
Private consumption	4,7	0,7	1,0	−0,6	:	:	:	:	:	1 462,9
Public consumption	6,1	6,5	2,5	2,6	:	:	:	:	:	361,3
Gross fixed capital formation	2,4	−10,1	−2,6	2,2	:	:	:	:	:	426,0
Change in stocks[1]	4,2	3,0	4,0	3,5	:	:	:	:	:	29,8 [3]
Domestic demand	4,4	0,3	1,5	−0,2	:	:	:	:	:	2 280,0
Exports of goods and services	10,6	5,4	2,6	3,0	:	:	:	:	:	293,8
Imports of goods and services	5,8	9,0	7,2	−3,5	:	:	:	:	:	539,9
GDP at market prices	4,7	−0,7	0,4	1,1	:	:	:	:	:	2 033,9
% change over preceding period at annual rates										
GDP at current prices	19,1	18,9	18,5	21,5	:	:	:	:	:	
Industrial production	6,5	−1,1	−3,0	0,6	7,3	−5,3	0,3	0,5	1,1	
Unemployment rate[2]	2,3	4,0	5,0	5,2	:	:	:	:	:	
Compensation of employees per capita	:	21,6	27,6	16,7	:	:	:	:	:	
M2	23,8	34,3	27,8	26,0	:	:	:	:	:	
GDP (implicit price index)	13,7	19,7	18,1	20,2	:	:	:	:	:	
Private consumption (implicit price index)	13,4	24,4	21,3	21,0	21,9	21,3	20,7	21,5	20,4	
Exports, goods (implicit price index)	14,4	3,4	24,5	19,0	:	:	:	:	:	
Imports, goods (implicit price index)	16,9	15,7	27,4	24,0	:	:	:	:	:	
Terms of trade	−1,6	−4,4	−2,5	−4,0	:	:	:	:	:	
as % of gross domestic product										
Trade balance (fob/cif)	−12,1	−12,3	−15,2	−14,6	:	:	:	:	:	
Current balance	−2,5	−2,1	−5,6	−4,7	:	:	:	:	:	
Net borrowing of general government	:	10,1	8,7	8,9	:	:	:	:	:	

1 As % of GDP.
2 Unemployment as % of total labour force.
3 Including a statistical discrepancy of DR 43 300 million.
4 Estimates.
5 Forecasts.

Source: Eurostat and Commission services.

France

Trends and prospects

After developing relatively dynamically until the middle of the year, the situation changed as a result of the currency realignment in June and the strict accompanying measures. The arrangements adopted mainly involved a temporary prices and incomes freeze, and were intended rapidly to reduce the widening differentials in both demand and inflation rates between France and its main trading partners; these differentials had combined to cause a serious aggravation in the external deficit during the first half-year. The arrangements were basically effective, at some cost in terms of activity during the third quarter,[1] although there was a slight recovery in the fourth.

Domestic demand slowed down considerably from the summer. The expansion of consumption by households, which had been vigorous since the second half of 1981, became considerably more moderate as a result of the freeze measures that halted the rise in aggregate purchasing power, and thereafter expanded only at the cost of a marked slowdown in savings. The decline in investment was accentuated, because both firms and households are continuing to experience financing problems, and because of stricter constraints on public finances. Finally, stocks ceased to expand in the second half of the year after the continued recovery of the first half.

Slower domestic demand and the positive effects of the currency realignment in June led to a reversal in the real external trade position, due even more to the improvement in exports than to the decline in imports. However, the further worsening in the terms of trade following currency developments meant that the impact of this major improvement in real terms was not immediately passed on to the nominal balance, which hardly changed over the six-month period.

[1] During the past two years, industrial production (excluding building and public works) has continued to decline in spite of cyclical fluctuations; in 1982, the level was lower than in 1980.

Contributions to changes in GDP

(volume at 1970 prices)

	1978	1979	1980	1981	1982 [1]
Final domestic demand	3,7	3,0	1,8	1,0	2,2
Changes in stocks	−0,1	0,9	0,3	−1,8	0,5
Trade balance	0,2	−0,6	−1,0	1,1	−1,3
GDP	3,8	3,3	1,1	0,3	1,4

[1] Estimates.
Source: INSEE and Commission services.

On balance, real gross domestic product will have expanded by about 1,5% in 1982 as a whole, but by the end of the year the growth trend was very slow. It was possible to limit the balance-of-payments deficit on current account to the equivalent of 2,5% of gross domestic product. Finally, thanks to the freeze consumer prices slowed down considerably in the second half-year, with the year-on-year rate down to below 10%.

The main priority of economic policy in 1983 is a considerable reduction in the external deficit through further moderation of real demand and of the price trend, and its main thrust is still control of the trend of prices and incomes.

The price freeze was lifted on 31 October, but replaced by control that should limit the rise in prices and in most incomes to 8% in 1983. Contracts have been signed between the government and most sectors of activity to ensure that the prices objective is attained. A recommendation has been made to the two sides of industry to keep increases in

Change in consumer prices

(%)

	12 months 1981 [1]	Average 1981	1982 [2] I	II	III	IV	12 months 1982 [1]	Average 1982
France	13,4	13,9	14,0	13,8	11,0	9,5	9,8	11,6
Differential in relation to:								
— FR of Germany	7,5	7,6	8,2	8,4	5,8	4,8	5,2	6,3
— EC 10	0,6	1,0	1,8	2,4	0,3	−0,2	0,4	0,7
— Competitor countries	3,4	4,2	5,2	5,6	4,0	2,2	3,0	4,5

[1] Change over 12 months (T ÷ (T − 12)).
[2] Quarterly average of changes over 12 months.

Consumption by households

(1970 prices)

	1980				1980	1981				1981	1982 [1]				1982
	I	II	III	IV		I	II	III	IV		I	II	III	IV	
Change T ÷ (T−1) as %	0,8	−0,7	0,7	0,6	1,7	0,2	1,1	1,2	0,3	2,3	1,5	0,7	0,4	0,5	3,4
Share in GDP as %	63,4	63,3	63,9	64,4	63,8	64,9	64,8	65,5	65,0	65,0	66,1	65,9	66,7	66,6	66,3

[1] Estimates.
Source: INSEE and Commission services.

remunerations in line with that objective and not to consider making up for purchasing power lost as a result of the freeze until the end of the year. Social benefits will be adjusted only in line with the expected price rise. Basically, only the minimum wage and the social benefits linked to it will continue to increase in real terms, and even here the increase will be slower.

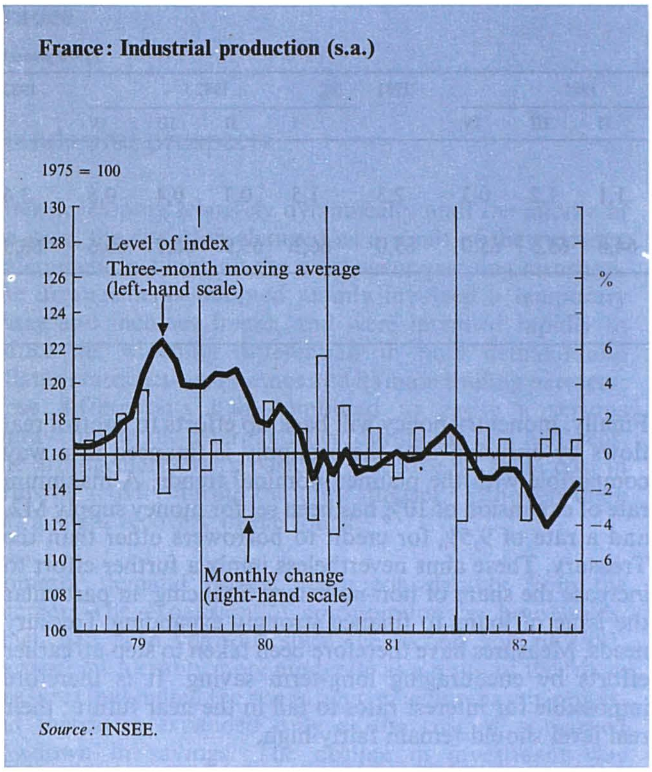
Severity will also continue to apply to public finances, where the provisions of the 1983 Finance Act and measures under various social security schemes aim at limiting net general government borrowing to about 3% of gross domestic product, in spite of the major increase in interest costs, the stepping-up of efforts to promote investment, research and employment, and the persistent worsening in the financial situation of most of the social security schemes. The impact of various earlier social measures, the increase in the numbers entitled to old-age pensions and unemployment benefits, and the structural expansion in the consumption of health care are still producing real growth in social transfer payments. In order to keep borrowing within the limits set, it was therefore necessary to correct other trends, in particular by severely compressing the operating and equipment expenditure of management departments and hospitals, and by making major savings on the cost of unemployment. These arrangements did not, however, prevent a further increase in contributions. [1]

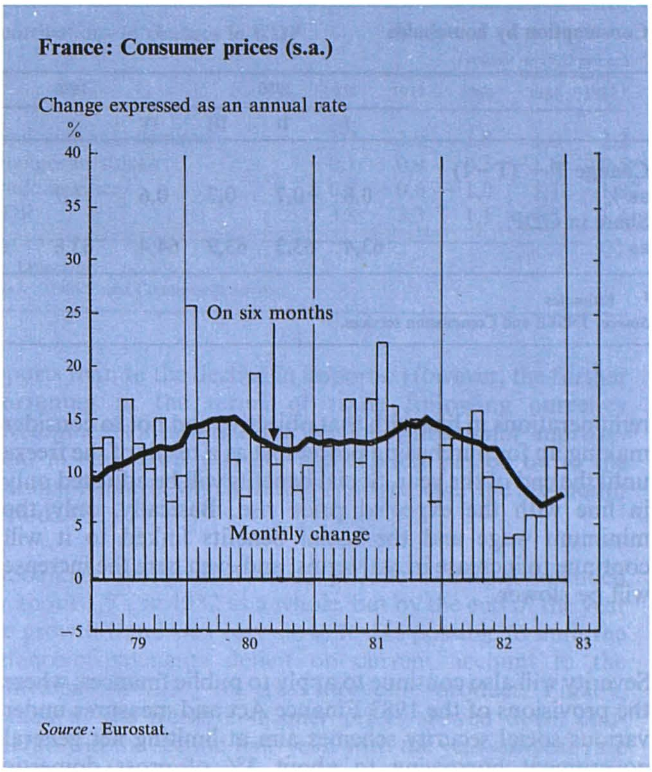
[1] In October 1982 the government took measures to restore financial equilibrium to the social security scheme and the unemployment insurance system (Assédic). The measures involving social security mainly consist in the harmonization of rates and bases for contribution (farmers, bridging pensions) and the limitation of expenditure. Insured persons will henceforth be liable for a daily charge of FF 20 for stays in hospital. Furthermore, the proceeds of a number of new taxes will be paid into the general scheme: the tax on advertising of branded pharmaceuticals reimbursed by the scheme, the 25% tax on tobacco, the FF 10 tax per litre on spirits. Assédic revenue will be increased through a solidarity contribution of 1% of the salaries of civil servants and public officials, and by an increase in unemployment contributions of 0,48% for wage-earners and 0,72% for firms. These measures may not be sufficient if the future trend of employment and activity is not as good as the government expects.

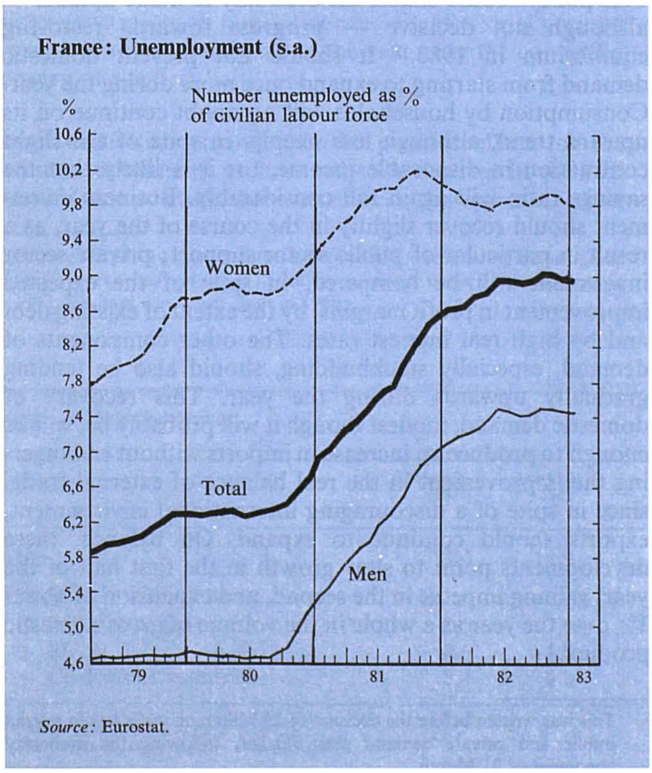
Finally, monetary policy will back up efforts to control real flows by ensuring that the economy is financed in a way compatible with the planned nominal trends. A maximum rate of expansion of 10% has been set for money supply M2, and a rate of 9,5% for credit to borrowers other than the Treasury. These aims nevertheless imply a further effort to increase the share of non-monetary financing, in particular the issue of loans to finance strongly expanding Treasury needs. Measures have therefore been taken to step up earlier efforts by encouraging long-term saving. It is therefore impossible for interest rates to fall in the near future; their real level should remain fairly high.

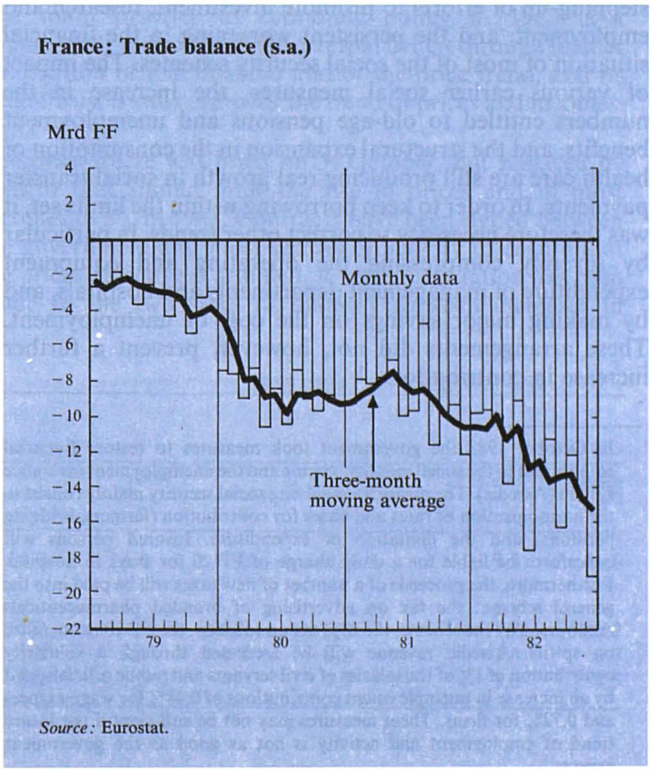
This policy should enable the economy to make notable — although not decisive — progress towards restoring equilibrium in 1983. [2] It should not prevent domestic demand from starting to expand once more during the year. Consumption by households will no doubt continue on its upward trend, although less steeply, in spite of the slight contraction in disposable income, for it is likely that the savings ratio will again fall considerably. Business investment should recover slightly in the course of the year, as a result in particular of public sector support; private sector investment will be hampered, in spite of the expected improvement in profit margins, by the extent of existing debt and by high real interest rates. The other components of demand, especially stockbuilding, should also be tending gradually upwards during the year. This recovery of domestic demand, modest though it will probably be, will be enough to produce an increase in imports without endangering the improvement in the real balance of external trade, since in spite of a discouraging international environment, exports should continue to expand. On balance, these developments point to slow growth in the first half of the year, gaining impetus in the second, and expansion of about 1% over the year as a whole in the volume of gross domestic product.

[2] This was written before the decision of 25 March on measures to restrict public and private demand even further, following the monetary alignment of 21 March.


France: Industrial production (s.a.)
1975 = 100
Level of index
Three-month moving average
(left-hand scale)
%
Monthly change
(right-hand scale)
130
128
126
124
122
120
118
116
114
112
110
108
106
6
4
2
0
−2
−4
−6
79
80
81
82
Source: INSEE.


France: Consumer prices (s.a.)
Change expressed as an annual rate
%
40
35
30
25
20
15
10
5
0
−5
On six months
Monthly change
79
80
81
82
83
Source: Eurostat.


France: Unemployment (s.a.)
Number unemployed as %
of civilian labour force
%
10,6
10,2
9,8
9,4
9,0
8,6
8,2
7,8
7,4
7,0
6,6
6,2
5,8
5,4
5,0
4,6
Women
Total
Men
79
80
81
82
83
Source: Eurostat.


France: Trade balance (s.a.)
Mrd FF
4
2
−0
−2
−4
−6
−8
−10
−12
−14
−16
−18
−20
−22
Monthly data
Three-month
moving average
79
80
81
82
Source: Eurostat.

France: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)						
	1971-80	1981	1982[3]	1983[4]	1981	1982[3]		1983[4]		1982	1983
					II	I	II	I	II	FF '000 million at current prices	
	% change over preceding period at annual rates — at constant 1970 prices										
Private consumption	3,1	2,2	3,4	1,4	3,6	4,0	1,6	1,0	1,8	2 318	2 560
Public consumption	:	1,5	1,8	1,2	2,2	2,4	0,0	0,8	1,2	560	623
Gross fixed capital formation	2,4	−2,8	−1,5	−1,6	−2,6	0,2	−3,8	−3,0	3,4	723	785
Change in stocks[1]	1,4	0,1	0,7	0,2	0,4	2,4	0,4	0,0	0,6	5	6
Domestic demand	:	−0,8	2,7	0,1	2,6	5,0	−1,6	−0,4	2,8	3 606	3 974
Exports of goods and services	8,0	5,1	−2,0	3,4	7,3	−10,3	5,9	2,2	3,4	765	869
Imports of goods and services	7,7	0,4	3,6	0,7	6,9	4,4	−0,8	0,8	1,8	860	943
GDP at market prices	3,6	0,3	1,4	0,8	2,6	1,4	0,0	0,0	3,2	3 508	3 900
	% change over preceding period at annual rates										
GDP at current prices	13,4	12,0	13,4	11,2	14,2	12,8	15,7	9,0	10,1		
Industrial production	:	−2,3	−1,5	−0,7	2,1	−1,3	−1,6	−0,6	3,0		
Unemployment rate[2]	3,8	7,6	8,6	9,2	8,0	8,4	8,8	9,0	9,5		
Compensation of employees	:	13,5	12,1	9,8	:	:	:	:	:		
M2	14,8	11,4	12,5	10,5	:	:	:	:	:		
GDP (implicit price index)	14,8	11,7	11,9	10,3	14,3	13,0	10,0	10,3	8,8		
Private consumption (implicit price index)	9,5	12,5	11,2	8,9	13,4	10,8	8,6	9,0	8,0		
Exports, goods (implicit price index)	8,5	12,6	12,9	10,0	14,4	14,0	7,2	9,0	14,2		
Imports, goods (implicit price index)	9,9	16,7	10,5	8,8	15,6	4,4	18,0	3,7	8,4		
Terms of trade	−1,3	−3,5	2,2	1,1	−1,0	9,2	−9,2	5,1	5,4		
	as % of gross domestic product										
Trade balance (fob/cif)	:	−3,0	−3,9	−3,0	−3,2	−3,9	−3,8	−2,6	−3,1		
Current balance	−0,4	−1,8	−2,4	−1,7	−2,1	−2,3	−2,6	−1,6	−1,9		
Net borrowing of general government	−0,1	−1,5	−2,8	−3,1	:	:	:	:	:		

1 As % of GDP.
2 Unemployment as % of total labour force.
3 Estimates.
4 Forecasts.

Source: Eurostat and Commission services.

The restoration of a favourable trend for the terms of trade should combine with the better real balance to produce a marked improvement in the balance on goods and services in terms of value. The extra costs involved in the growth of the foreign debt will, however, substantially attenuate the effects of this improvement on the balance of payments on current account, which will still show a deficit equivalent to about 1,7% of GDP.[1] Even if the increase in prices from the beginning to the end of 1983 does not exceed the planned 8%, the slower rate will not be sufficient to neutralize the inflation differential between France and its main trading partners. However, import prices might slow down even faster, which would make for improvement in both the current balance and the price trend, and offset the upsurges that are still possible in domestic prices.

On the other hand, the more stable trend of unemployment that appeared at the end of 1982 was due to specific employment policy measures whose effects will automatically run out. Unemployment will consequently rise once again during 1983.

Problems of economic policy

The process of adjusting the French economy will be far from completed by the end of the year unless it speeds up much more than seems feasible at present, and unless the international environment improves unexpectedly. The longer the process takes, the greater will be the burden of external debt taken on to cover the current deficit, and the stricter will be the constraint on the future expansion of domestic demand. It could thus be appropriate to restore balance more rapidly, by aiming at both stricter control of domestic demand and faster disinflation. [2]

If this line is adopted, care must be taken to ensure that the increased burden of taxes and other contributions on incomes does not result in a further decline in the savings ratio, for this would limit the restrictive effects of the measures on consumption and increase the difficulty of financing investment. Moreover, imports and exports will need to react flexibly to any slackening in demand if the effects of such slackening on domestic supply are to be attenuated; but their flexibility depends on behavioural factors that are difficult to control. Finally, the measures for incomes and prices that will be required to follow up this effort must contribute to restoring the financial situation of undertakings so that eventually the indispensable recovery of productive investment is assured.

The restoration of external equilibrium will not, however, depend primarily on short-term arrangements; these can only help to gain time to allow the factors of a more fundamental improvement to come into play. The serious problems the economy is still facing in its relations with the rest of the world are now due much more to structural shortcomings than to inappropriate demand regulation or (at least since the currency realignment of June 1982) to insufficiently competitive prices.

The foreign trade situation is particularly serious because the problem is almost entirely due to the deterioration of the balance on manufactured products other than food, and this deterioration can be corrected only by several years of sustained effort. This is a long-established tendency, although it only became fully apparent recently as a result of its accentuation. A growing imbalance appeared in the 1970s between the rapid and steady penetration of foreign industrial products on the national market[3] and the much less regular and in general slower penetration of national products on foreign markets. These trends were most marked in the current consumption branch and in the consumer durables branch, where the car industry, with the rapid decline in its export surplus, has recently joined such traditionally weak sectors as electrical domestic appliances and consumer electronics. The balance on business equipment, although it still shows a large surplus, has recently been tending to deteriorate as well. In fact, only military equipment has progressed steadily. The deficit on trade in goods with the industrialized countries — particularly the Community countries — has thus been dramatically widened over the past few years.

The new industrial policy is based on the implementation of a number of sectoral plans aiming notably at the restoration of external balance in some of the sensitive sectors. It requires major investments, and raises financing problems that will be particularly difficult to solve at a time of almost zero growth.

The efforts to encourage long-term savings are intended to prevent the inflationary pressure that could be created. The policy also implies, through the choice of instruments, a considerable and in many cases almost direct commitment on the part of the authorities; the risks inherent in the

---

1 Several factors explain the vigorous growth expected for exports on average in 1983: on the technical side, the 1982 profile shows a major advance at the end of the year (about 3% in volume); on the economic side, as the 1982 harvest was particularly good, agricultural and agri-food exports should expand considerably in real terms in 1983 because the decrease in market shares over the past two years was partly due to a deterioration in price competitiveness, which was temporarily corrected by the currency readjustments of October 1981 and June 1982, so that in 1983 France should make up some of the lost ground.

2 See note 2 on page 49.

3 Nominal trends are sometimes considerably different from volume trends. For example, the rates of penetration of business equipment in volume increased little from 1980 to 1982, while those in terms of value increased substantially; the opposite was true for current consumption goods.

concentration of means of action can be avoided only if the exercise of responsibilities is sufficiently decentralized.

Industrial policy is the most important component of structural policy, since it governs both the restoration of external equilibrium and, up to a point, the improvement of the employment situation; but problems of compatibility may arise between the aims of industrial policy and those of social policy. The authorities are aware that it is now absolutely vital to ensure that further social progress, such as bringing forward the age of retirement or continuing to reduce working hours, does not lead to extra costs to firms, making it more difficult for them to achieve the indispensable improvement in their capacity for investment. The authorities are thus considering a reduction in costs by gradually taking over the burden of financing family allowances, having already increased considerably the central government's share in financing other contributory schemes, particularly unemployment insurance. While it is necessary and just that a proportion of social costs should be transferred from firms to households, it is nevertheless true that the economy will, at all events, find it difficult to tolerate the inexorable expansion of these costs until such time as it has returned to a more sustained growth path.

Ireland

Trends and prospects

In 1982 domestic demand fell sharply, but good export growth was recorded and the deficit on the current balance improved considerably. Private consumption fell by 5%, a magnitude experienced only once before in Ireland, in 1975, and unprecedented in any other Member State since the foundation of the Community. This development was partly due to a continued fall in real wages which suggests that a painful but necessary process of adjustment has begun. However, the unexpected depth of the fall reflected a sharp increase in the personal savings ratio, which could possibly prove to be largely a matter of postponed consumption.

Investment fell by 5,3% in volume, mainly due to a fall of about 10% in building and construction activity. Demand for commercial premises was slack while high interest charges for mortgages depressed the market for private housing.

Despite the sharp fall in domestic demand, a modest GDP growth rate of 1,4% was nevertheless recorded. Buoyant industrial exports, reflecting the coming into production of new, often foreign-owned companies, ensured strong export growth overall. The table below shows how well industrial exports have performed in recent years in spite of difficult international trading conditions.

Imports declined in line with domestic demand while the trend towards lower import prices continued. The deficit on the current balance fell markedly from 13,8% of GDP in 1981 to 8%. Although the average rate of inflation for the year was somewhat over 17%, it moderated significantly in the last quarter (for the year November/November 12,3%) although still remaining substantially above the EC average.

Two developments gave rise to increasing concern, however. Unemployment accelerated and by the end of the year the rate exceeded 14% of the labour force. The current budget deficit exceeded the target of 6,0% of GDP and reached 8% of GDP because of a massive shortfall in revenue. The Exchequer borrowing requirement, originally planned at 13,2% of GDP, turned out at about 16%.

(% annual volume growth)

	1978	1979	1980	1981	1982 [1]
Industrial exports	13,0	12,0	5,5	9,3	9,0

[1] Estimate.
Source: Central Bank of Ireland, Annual Reports.

Budgetary policy in 1982 once again stressed large increases in indirect taxes and in social security contributions, although limits to raising the burden of taxation have increasingly been felt in recent years. With this in mind, the authorities also took steps to contain expenditure. Payment of the final (5%) phase of the current round of wage increases for public sector employees was postponed for three months and agreement was obtained from the public sector unions to limit special wage increases in 1983. Overall spending fell somewhat under the level originally budgeted. At year end however, the national debt stood at nearly 100% of 1982 GDP while debt interest costs during the year amounted to over 22% of total current expenditure or, put another way, some 90% of revenue from income tax.

The budget of 9 February aims at reducing in 1983 the current budget deficit and the Exchequer borrowing requirement to about 6,5% and 12,5% of GDP respectively. Heavy emphasis is placed on increases in indirect taxes (the 30% VAT rate is to be increased to 35% and the 18% rate to 23%) and on measures to raise the income tax take; all farmers will now be liable for income tax and there will be a temporary 1% levy on gross income. While a reduction in the volume of public capital spending is anticipated no volume reduction is planned in current spending. However, no provision was made in the budget for a wage increase in 1983 for public sector workers, apart from the carryover of the 1982 pay increases, in particular the postponed 5% final phase.

In spite of some success in increasing the share of domestic borrowing in 1982, the Exchequer deficit is still likely to be funded mainly from foreign sources in 1983. The effect on domestic liquidity of the Exchequer's heavy reliance on monetary financing is offset by the deficit on the current balance and by capital outflows. Since these movements may not be synchronized however, one of the central tasks of

Ireland: Recent budgetary trends [1]

(million IRL)

	1981	Provisional out-turn 1982	Official target 1983
Total current receipts	3 973	4 908	5 758
Total current expenditure	4 775	5 896	6 655
Current budget deficit	802	988	897
Exchequer borrowing for capital purposes	920	957	825
Total Exchequer borrowing requirement	1 722	1 945	1 722
Exchequer borrowing requirement as % of GDP	16,6	15,8	12,5

[1] Budgetary definitions.
Source: Budget booklets.

monetary policy is to manage fluctuations in domestic liquidity. As the current balance improves in 1983, the flow of external payments may no longer offset to the same degree the expansionary effect of net government foreign borrowing even with substantial capital outflows. So far, the monetary authorities have maintained a relatively flexible policy. Interest rates were allowed to fall moderately during the year. The monetary authorities also fixed a guideline of 14% for bank credit creation for the private sector in the credit-year to mid-February 1983. The task of the authorities was assisted by a relatively low level of demand for private credit and by a relative decline in the importance of foreign-currency-based lending during the year.

The forecast for 1983 (see table) was made before the budget in the wider context of a forecast for all EC countries. The impact of the budget of 9 February, in particular the emphasis on indirect taxes and a substantial cut in public capital spending, together with a restrictive stance by the authorities on pay in 1983, would result in slower economic growth than presented in the table.

The fall in domestic demand is likely to come to an end. A small decline in the savings ratio is assumed but any liquidation of accumulated savings is likely to be offset by the restrictive stance of budgetary policy. Real wages are expected to stabilize but a firm government attitude in the 1983 wage negotiations could cause them to fall somewhat. Overall private consumption in real terms should remain broadly at the level of 1982. Expenditures under the public capital programme will be curtailed but lower interest rates would give some support to private investment.

The balance of payments will continue to improve markedly. Industrial exports should continue to perform strongly, aided by an expansion of 2,5% in export markets, and agriculture will be able to make an important contribution through current production and the running-down of intervention stocks accumulated in 1982. Because of the stabilization of domestic demand and the fact that a substantial proportion of industrial inputs are imported, some increase in imports is foreseen. Nevertheless, the trend towards lower import prices will continue and together with some easing of interest charges on foreign debt, should result in a further reduction of the deficit on current balance to some 6% of GDP compared with 8% in 1982. [1]

The continued slowdown in imports will also assist in getting inflation down further. It will still remain high by EC levels however, and success in reducing it further will depend on domestic policies.

[1] Taking account of the budget measures of 9 February this percentage will be lower.

All in all, some modest growth is expected, but it will not be sufficient to arrest the growth of unemployment which will approach a rate of 15% in the early part of the year.

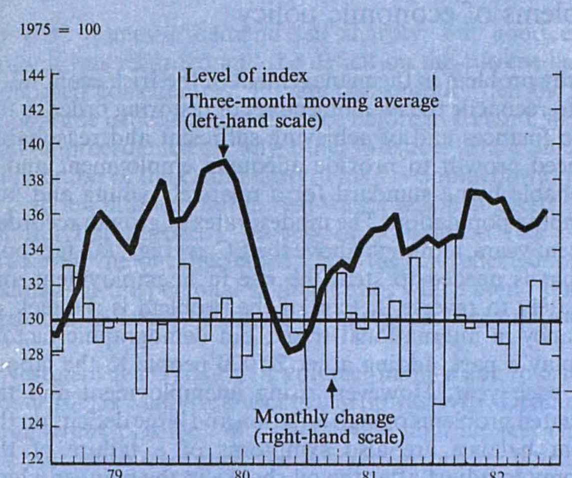
Problems of economic policy

The key problem in the management of the Irish economy is how to reconcile the twin objectives of restoring order to the public finances and of achieving sufficient and reasonably balanced growth to provide adequate employment and a reasonable living standard for a relatively young and fast expanding population. The modest rates of growth recorded in recent years, although above the EC average, fall far short of what is needed to stem the rise in unemployment and ultimately to reverse it. Part of the problem is the lack of buoyancy in international trade; but demographic factors also play a part, adding a net 20 000 people to the labour force each year. However, rising unemployment and the associated problems of high inflation and large deficits on the current balance are also symptoms of a failure of the economy to adjust after the oil shocks in the manner which would have been required in view of the fall in the terms of trade and Ireland's heavy dependence on foreign commerce. Up to 1981, levels of real pay continued to increase at the expense of mounting Exchequer indebtedness. Borrowing only bought time however, and although Ireland was one of the later countries to feel the effects of the recession in terms of lost output and employment, severe measures of adjustment could not be postponed indefinitely. In the meantime, the cost of repaying the borrowing had pre-empted resources for the future and had absorbed any margin for traditional anti-cyclical measures.

The sharp fall in private consumption and the marked improvement in the external balance in 1982 suggests that the adjustment process has begun. Since current circumstances are, however, the result of an accumulation of drift over a number of years, they cannot be reversed overnight. To restore a propre balance between Exchequer expenditure and revenue, and between what the economy earns and what it absorbs, and to lay the foundation for growth and prosperity in the future will require several years of rigorous effort.

The budget of 9 February is an important step in the process of adjustment. The budgetary targets — current budget deficit about 6,5% of GDP and Exchequer borrowing requirement about 12,5% — represent substantial progress in restoring balance to the public accounts; some of the measures to increase taxation (current year assessment of the self-employed), and to cut expenditure should produce considerably greater cumulative savings in 1984 and thereafter. However, in the context of the evolution of budgetary policy over the next few years — and the target set for the elimination of the current budget deficit over a period

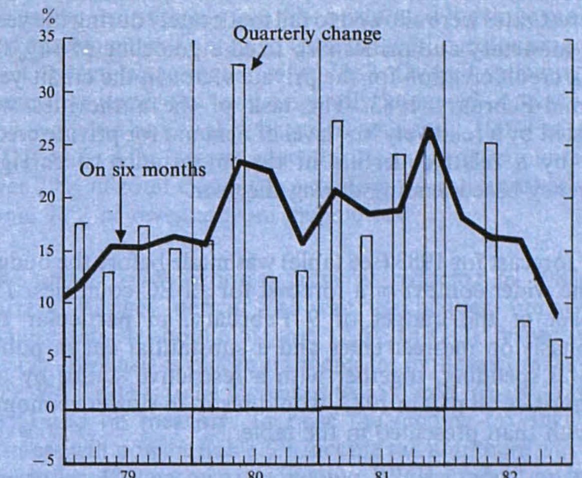
Ireland: Industrial production (s.a.)



Source: Eurostat.

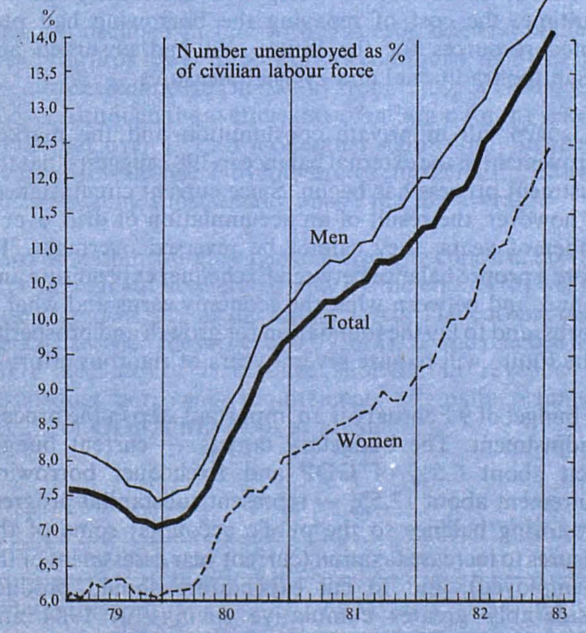
Ireland: Consumer prices (s.a.)

Change expressed as an annual rate



Source: Eurostat.

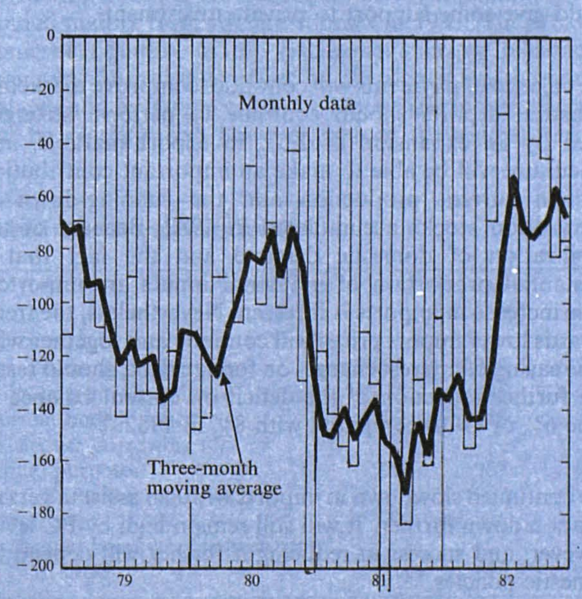
Ireland: Unemployment (s.a.)



Source: Eurostat.

Ireland: Trade balance (s.a.)

Mio IRL



Source: Eurostat.

Ireland: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					1981
	1971-80	1981	1982[3]	1983[4]	1981	1982[3]		1983[4]		
					II	I	II	I	II	million IRL at current prices
	% change over preceding period at annual rates — at constant 1975 prices									
Private consumption	2,7	−0,5	−5,0	−0,8	−3,7	−6,0	−4,1	−0,2	1,3	6 565
Public consumption	6,1	−0,1	1,5	0,0	−3,5	3,4	3,1	−1,1	−1,1	2 271
Gross fixed capital formation	5,2	5,2	−5,3	0,0	−0,6	−4,3	−6,1	1,5	3,4	3 089
Change in stocks[1]	1,1	−0,9	0,0	0,0	−0,2	−0,1	0,1	0,0	0,0	−88
Domestic demand	2,7	1,1	−3,1	−0,8	−1,7	−3,7	−3,0	−0,1	1,3	11 837
Exports of goods and services	8,0	1,5	6,4	6,0	6,7	7,2	4,5	7,5	4,5	5 576
Imports of goods and services	6,3	1,6	−1,8	2,4	2,8	−1,2	−7,7	6,9	5,3	7 024
GDP at market prices	4,1	1,1	1,4	1,5	−0,1	0,8	4,6	0,1	1,2	10 389
	% change over preceding period at annual rates									
GDP at current prices	18,3	19,0	20,2	14,2	18,3	22,2	21,5	13,9	12,6	
Industrial production	4,3	3,0	1,0	1,5	2,5	0,6	0,4	0,8	1,2	
Unemployment rate[2]	7,4	10,5	12,1	14,7	:	:	:	:	:	
Compensation of employees	18,0	20,5	13,2	11,9	:	:	:	:	:	
M2	19,2	:	:	:	:	:	:	:	:	
GDP (implicit price index)	13,6	17,8	18,5	12,5	18,4	21,2	16,2	13,8	11,3	
Private consumption (implicit price index)	13,8	19,6	17,5	12,0	25,0	20,9	14,5	13,3	10,5	
Exports, goods (implicit price index)	14,5	17,1	10,5	8,5	18,0	13,8	8,0	7,7	9,2	
Imports, goods (implicit price index)	15,8	18,9	7,5	6,5	9,0	8,0	7,0	6,3	6,8	
Terms of trade	−1,8	−2,1	2,8	1,1	:	:	:	:	:	
	as % of gross domestic product									
Trade balance (fob/cif)	−9,9	−15,8	−8,5	−5,4	:	:	:	:	:	
Current balance	−4,6	−13,2	−8,0	−5,9	:	:	:	:	:	
Net borrowing of general government	−8,1	−15,4	−15,0	−13,0	:	:	:	:	:	

1 As % of GDP.
2 Unemployment as % of total labour force.
3 Estimates.
4 Pre-budget forecasts.

Source: Eurostat; Commission and national services.

of five years is a key factor — it will become necessary to reassess the appropriateness of the present balance between tax-increasing and expenditure-reducing measures. Despite the performance of the authorities in 1982 in keeping expenditure within the budgeted limits for the first time in years, upward pressure on expenditure will continue until programmes which have relatively low priority are phased out and the overall efficiency of spending in the others is improved. In addition, indirect tax increases add both to inflationary pressures and to industrial costs, so that the required savings should perhaps be better obtained by expenditure cuts. Increasing further the burden of direct tax on the PAYE sector may also raise problems. The Commission on Taxation, in its first report published last year, recommended that the system of direct taxation should be simplified, made more equitable by broadening the tax base and its economic efficiency should be improved. The 1983 budget contains a series of measures designed to this effect. A measure to be particularly welcomed is the curtailing of the interest relief on personal loans which will contribute to a better allocation of national resources. If substantially increased direct tax revenue is to be sought in the context of a restrictive budgetary stance over the next few years, further progress should be made in improving the working of the direct taxation system.

With regard to the use of resources, doubts have arisen about the quality of certain capital outlays. Central to this concern is policy in regard to the State-owned industries. Some of these operate with substantial losses or are given Exchequer assistance in the form of loans and equity capital which they do not remunerate adequately. The improvement of quality of public capital outlays would involve making the operations of these bodies subject to the normal market disciplines. Two other areas of substantial public intervention are under review. Output and productive efficiency in agriculture have not shown an improvement proportionate to the substantial amount of funds invested in this sector by the Exchequer. Furthermore, the effectiveness of the present generous levels of fiscal incentives, grant-aid and other assistance now made available to promote new industry is also being questioned. It is argued that these are perhaps too high and that they encourage marginal projects to be undertaken and tip the balance in favour of capital-intensive projects. Moreover, domestically-owned firms account for a major part of the grants provided. Some of these do not engage in international trade although it is desirable that more indigenous firms be encouraged to export. While foreign-owned firms have made the greatest contribution to export growth, the high level of incentives may not have encouraged them to commit as much of their own financing as they might otherwise have done. A more selective use of incentives may not only encourage a greater financial stake by these companies but also the location in Ireland of sophisticated parts of their operations. These issues are being examined by the authorities in an overall review of industrial policy. A successful industrial policy will also have to take account of structural defects in the Irish economy such as the unbalanced skill structure of the labour force and a standard of infrastructural services which needs to be improved in some respects.

Substantial growth in output particularly for export will require an improvement in the competitiveness of Irish products both as regards price and non-price factors such as reliability and service. Between 1981 and 1982 Irish competitiveness measured on the basis of unit labour costs (whole economy) declined by 2,5% against the main trading partners. In comparison with the EMS partners, however, the decline was about 3,2%. More serious, however, was the decline of over 5% relative to the UK, the main market. The main factor contributing to the higher rate of cost increase in Ireland in 1982 was the increase of nearly 14% in average employee earnings in the non-agricultural sector. While this rate was lower than in previous years, it was seriously out of line with the increases in the main trading partners. For example the average earnings increase was less than 9½% in the United Kingdom, 4% in the Federal Republic of Germany, and 6-7% in the Benelux countries. Movements in the total level of international trade, however, arguably have a greater impact on the volume of Irish exports than have modest changes in relative domestic costs. Similarly it must be remembered that in many cases import costs form a higher proportion of total Irish production costs than do domestic costs. As a result, an improvement in cost competitiveness should not lead to expectations of an immediate and dramatic increase in exports or import substitution and thus to a major easing of the unemployment problem. Indeed, for this to happen, a sustained period of wage moderation is necessary.

In both the public and private sectors the carryover into 1983 from the previous year's increases will be substantial, 11½% and something approaching half that figure respectively. Taking account of the interaction between the public and private sector, the approach of the authorities to public sector pay has a very distinct impact on the trend in wage costs in the whole economy in the years to come.

A policy to boost output through improving the quality of investment, marshalling more domestic resources and at the same time practising budgetary restraint and curbing real wages can only be successful if it has the assent of all the social partners. For this reason it certainly is desirable to place policy in a medium-term framework where the benefits ultimately accruing from present sacrifice would be seen. An essential part of such a framework might be a medium-term financial plan which could embrace not only budgetary but also monetary aggregates.

Italy

Trends and prospects

In 1982 the economy continued to adapt under the close control of a policy designed to prevent any revival of domestic demand. Not only was the strict monetary policy confirmed, with real interest rates being kept relatively high throughout most of the year; indirect taxation was also considerably increased from 1 August. Delays in renewing the collective agreements that ran out in 1982 contributed to holding back the expansion of the wages bill, and all these factors contributed to a further decline in final domestic demand accentuated, during the second half of the year, by a halt in the recovery of stockbuilding observed in the first half.

Nevertheless, these developments did not produce the favourable effects that might have been expected on the real balance of external trade. Exports declined steadily throughout the year—although it is true that the initial level was very very high—while the decline of imports in the second half of the year did no more than offset the strong expansion, due to stockbuilding, of the first half. On balance, the positive contribution of the real balance to growth was very slight for the year as a whole so that in 1982, for the second year running, the volume of gross domestic product contracted slightly. There was, however, a marked contrast between the sustained activity of the first half of the year, and the considerable contraction in the second half.

In spite of the decline, there was only fairly modest progress towards restoring basic equilibria. The downward movement of the rate of consumer price increase was hampered at the beginning of the second half of the year by the incidence of tax increases, and it did not get under way again until the last months of the year; consequently, the average increase for 1982 was 16,5%, only 2,5 points lower than in 1981. As a result of the favourable trend of the terms of trade and the substantial contribution of tourism, the deficit on the balance of payments on current account was significantly reduced in relation to 1981; it still, however, amounted to the equivalent of 1,5% of gross domestic product.

Contributions to changes in GDP

	1978	1979	1980	1981	1982
Final domestic demand	2,2	4,6	4,5	0,3	−0,6
Changes in stocks	−0,3	0,8	2,2	−3,0	0,2
External balance	0,8	−0,5	−2,8	2,5	0,2
GDP	2,7	4,9	3,9	−0,2	−0,2

The economic policy defined for 1983 once again concentrates on the earlier objectives of gradual disinflation and eliminating the external deficit. It is designed both to restrain domestic demand far enough to ensure some improvement in the real balance of trade, and to attain a more marked slowdown in nominal trends, with a rate of inflation of 13% for the year as a whole. While the objectives of the policy are unchanged, the means of achieving them have been greatly reinforced by a set of decisions taken in late 1982 and early 1983.

First, the drive to control the public deficit was considerably stepped up through a series of budget and tax provisions adopted on 30 December and 7 January; their aggregate effect should be to reduce both the general government borrowing requirement and net Treasury borrowing by the

Expenditure, revenue and position of general government

(as % of GDP)

	1978	1979	1980	1981	1982 [1]	1983 [2]
Current revenue	36,7	36,3	38,0	39,3	41,1	44,4
of which:						
direct taxes	(10,1)	(9,9)	(11,2)	(12,7)	(13,9)	(15,1)
Current expenditure	42,3	41,6	42,0	46,6	48,2	49,8
of which:						
interest	(5,9)	(5,8)	(6,2)	(7,5)	(8,5)	(8,9)
Capital transactions	4,1	4,2	4,4	4,6	4,9	5,1
of which:						
investment	(3,1)	(3,1)	(3,4)	(3,7)	(3,8)	(4,1)
Borrowing requirement	−9,7	−9,5	−8,4	−11,9	−12,0	−10,5

[1] Estimates.
[2] Forecasts.

equivalent of three percentage points of GDP, to 10,5% and 14% respectively; this is lower than the level reached in 1982.[1] On the monetary side, the 1983 target for total domestic credit has been set (subject to possible revision) at LIT 105 000 000 million; it is planned to discontinue controls on bank credit from the middle of the year, and to regulate banks' assets and liabilities thereafter through market instruments and especially the manipulation of interest rates; real rates should, at all events, remain fairly close to the level of 1982.[2] Finally, and most importantly, the two sides of industry and the government reached a general agreement on wage adjustments on 22 January, after long negotiations; this agreement should lead to the disinflation of wage costs, starting in 1983 and gaining momentum thereafter. The main points of the agreement concern the sliding scale: its scope has been considerably narrowed by a series of provisions, mainly the reduction of 15% in the value of each point in the index,[3] and the statutory increases for 1983 and 1985. Maximum permitted increases are small[4] and there will be no supplementary increase under individual firms' agreements for 18 months. Some compensation will be provided if actual price rises (excluding the incidence of any rise in the average exchange rate of the dollar against the Community currencies) exceed predicted rises.[5] In return for this restraint, the government will adjust further for fiscal drag, increase family allowances on 1 July 1983, and limit the 1983 increase in administered and controlled prices to 13%. The agreement also includes provisions for improved labour productivity and a gradual reduction in working hours.

The economic policy provisions for 1983 thus apparently ensure a considerable reduction in the rate of increase of costs and prices, although some wage drift is expected to offset the restrictive effect of bargaining rules. One may reasonably expect a decline of about four points in the rate of expansion of the wages bill in relation to 1982, and a decline of two and a half or three points in the rate of price rise. This would still, however, leave a wide gap in 1983 between the rate of increase in unit labour costs in Italy, which will be about twice the average rate expected for the rest of the Community.

Unit labour costs

(change in %)

	1978	1979	1980	1981	1982	1983
1. Italy	13,9	13,4	17,3	22,7	18,6	15,3
2. EEC	7,9	8,5	11,3	10,7	8,7	6,7
3. Differential (1:2)	5,6	4,5	5,4	10,8	9,1	8,6

The measures adopted will not permit more than a modest recovery in domestic demand during 1983, so that the change in terms of annual growth will probably be slightly negative once again. Real disposable income of households, which did not move in 1982, should decline slightly in 1983 in spite of the attenuation of fiscal drag; consumption is therefore likely to contract slightly too, even though the savings ratio will probably not remain at the high level reached last year. Investment is more difficult to predict, but some recovery may be expected in the course of the year. It should be supported to some extent by the marked rise in capital expenditure of general government as well as by the gradual recovery of demand from firms, which still have strong incentives for substitution investment, and whose profit margins should be improving during the year after two years of sharp contraction. On balance, gross fixed capital formation will be ending to improve in 1983, but its contribution to growth will remain negative for the year as a whole. Some increase in stockbuilding should occur as a result of the slow recovery of final demand.

19The expected slow recovery of domestic demand should be accompanied by a slightly more favourable trend of the real balance of external trade. From the beginning of the year, exports should show a marked improvement on the abnormally depressed level of the second half of 1982, but as domestic demand—particularly stockbuilding—gradually gathers momentum during the year, imports will no doubt recover fairly strongly as well. Altogether the real balance of external trade will probably tend to improve slightly during the year, but its contribution to growth will be practically nil for 1983 as a whole.

This outlook for demand points to some improvement in activity in 1983, but probably not enough to prevent real gross domestic product from contracting slightly once more, by about 0,5% for the year. In the circumstances, unemployment will inevitably expand to over 11%.[6]

Although the external environment will probably still provide little stimulus for growth, it is likely, on the other hand, to be more favourable where relative price trends are

[1] These provisions, in the form of decree-laws or draft laws, account altogether for about LIT 18 000 000 million, including LIT 4 500 000 million in savings on expenditure (pensions, health, central government departments) and LIT 13 500 000 million in extra revenue from taxation and public service charges.

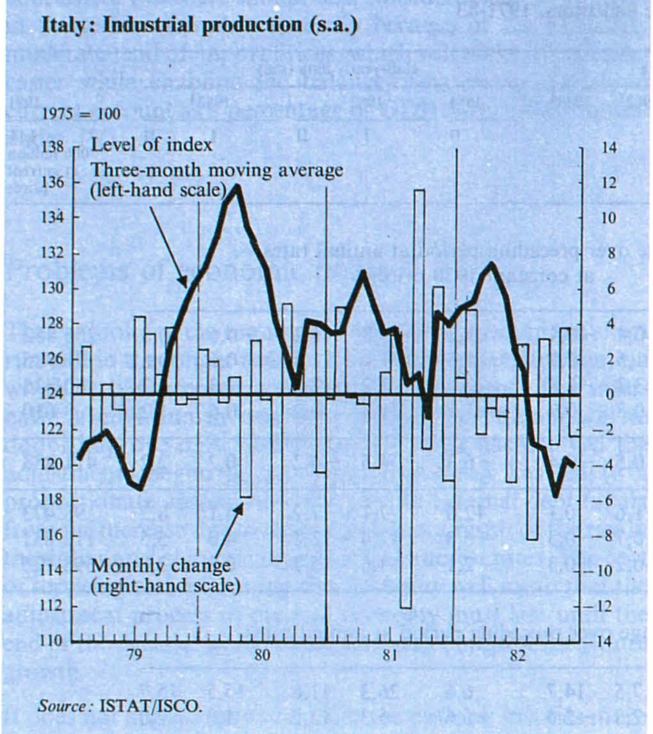
[2] This new system of monetary regulation, consistent with the 'divorce' between the Treasury and the Bank of Italy decided in 1981, should have a dual advantage: not only will it increase the flexibility of the credit market, it will also be a more effective defence against the inflationary risk of any overshooting of the limit on net Treasury borrowing (see box).

[3] It was further agreed that the incidence of any future increase in indirect taxation would be only partially incorporated in the index.

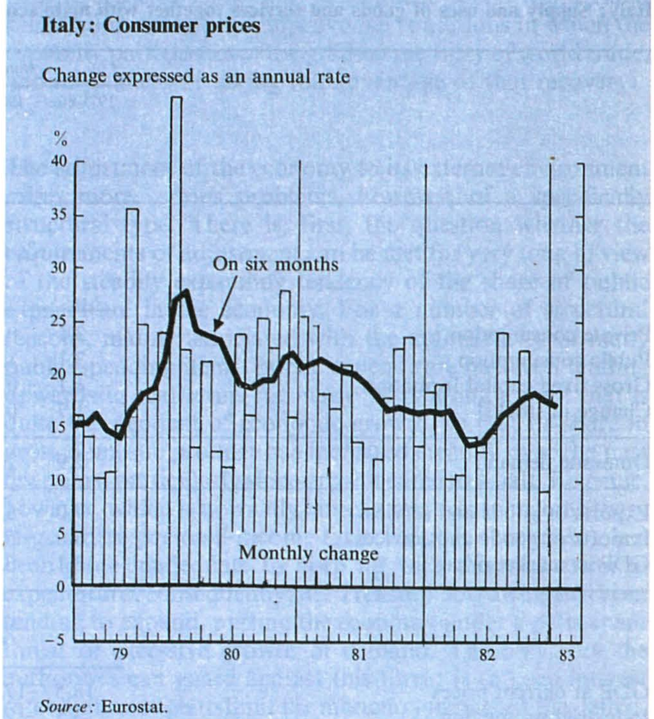
[4] A maximum of LIT 25 000 a month on 1 January 1983, LIT 35 000 on 1 January 1984 and LIT 40 000 on 1 January 1985. No compensation is planned for delays in renewing agreements that ran out in 1982.

[5] 13% for 1983 and 10% for 1984.

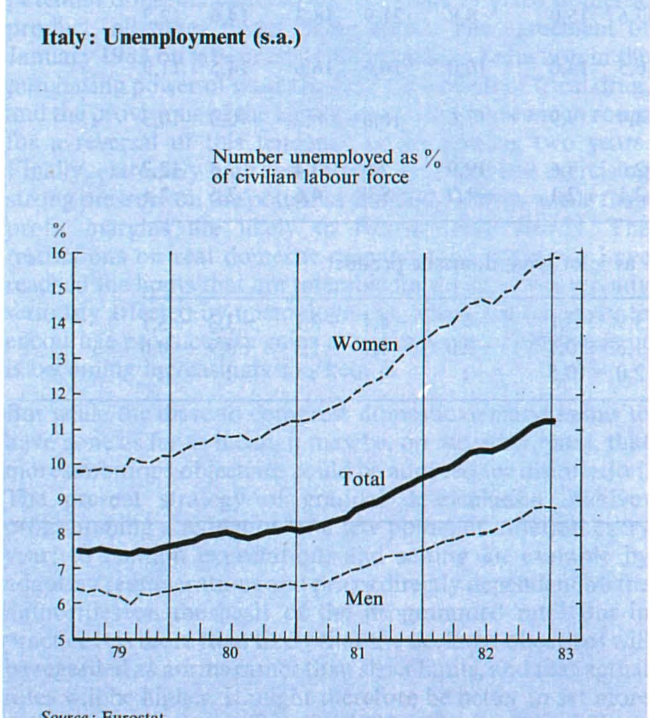
[6] According to Eurostat definition.



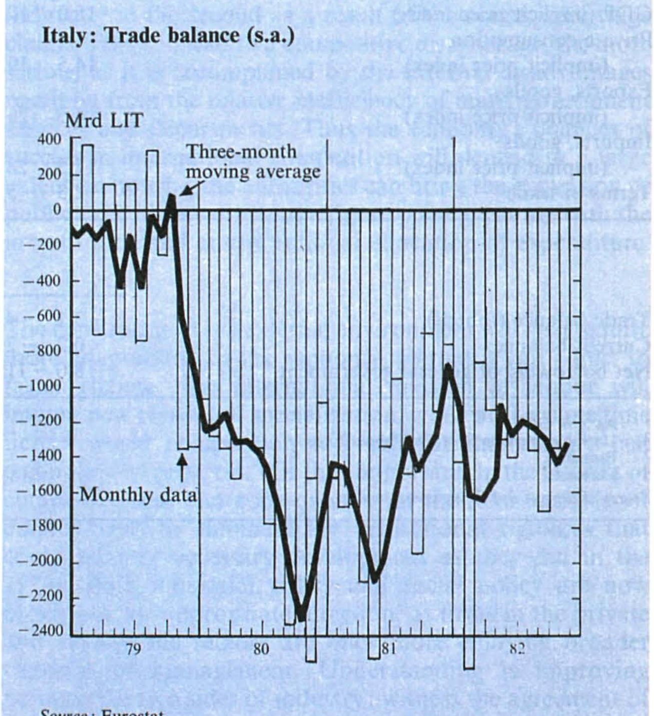
Source: ISTAT/ISCO.



Source: Eurostat.



Source: Eurostat.



Source: Eurostat.

Italy: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					1981
	1971-80	1981	1982[3]	1983[4]	1981 II	1982[3] I	1982[3] II	1983[4] I	1983[4] II	LIT '000 million at current prices
	% change over preceding period at annual rates — at constant 1970 prices									
Private consumption	3,1	0,2	−0,4	−0,4	1,2	−0,8	−1,2	−0,6	0,8	255 452
Public consumption	3,1	1,8	1,5	0,9	1,5	1,4	1,8	0,6	0,6	71 985
Gross fixed capital formation	1,1	−0,2	−3,3	−2,8	−2,9	−1,2	−7,8	−2,3	1,7	80 836
Change in stocks[1]	1,7	0,6	0,8	0,9	−1,1	1,3	0,2	0,6	1,2	3 610
Domestic demand	2,9	−2,7	−0,5	−0,4	−6,3	4,5	−4,2	0,2	2,2	411 883
Exports of goods and services	7,0	6,0	1,6	0,1	12,0	7,1	−17,2	6,1	8,2	98 473
Imports of goods and services	6,0	−5,4	0,7	−0,3	−6,3	12,4	−13,2	4,0	5,5	112 231
GDP at market prices	3,1	−0,2	−0,2	−0,3	−2,1	3,6	−5,7	0,8	3,0	398 125
	% change over preceding period at annual rates									
GDP at current prices	18,5	17,4	17,5	14,7	6,6	26,3	11,6	15,5	15,7	
Industrial production	3,5	−2,2	−2,3	−2,6	−5,6	5,3	−13,2	1,0	2,0	
Unemployment rate[2]	6,0	8,8	10,4	11,3	9,2	10,0	10,8	11,2	11,4	
Compensation of employees	22,0	22,3	18,4	14,7	22,4	17,8	16,0	14,5	14,5	
M2	19,5	16,0	19,0	17,0	:	:	:	:	:	
GDP (implicit price index)	15,0	17,6	17,6	15,0	8,8	21,9	18,3	14,6	12,3	
Private consumption (implicit price index)	14,5	19,0	16,5	14,0	16,0	16,6	16,6	14,5	11,9	
Exports, goods (implicit price index)	14,5	20,2	14,4	9,9	17,6	16,6	8,2	10,3	10,3	
Imports, goods (implicit price index)	17,5	28,4	12,0	7,6	19,9	7,9	3,4	7,5	12,7	
Terms of trade	−2,3	−5,7	2,1	2,1	−1,9	8,0	4,6	2,6	−2,1	
	as % of gross domestic product									
Trade balance (fob/cif)	−3,1	−4,8	−3,9	−3,1	−4,6	−4,1	−3,7	−3,3	−3,1	
Current balance	−0,2	−2,3	−1,5	−0,7	−2,0	−1,7	−1,3	−0,9	−0,6	
Net borrowing of general government	−8,0	−11,9	−12,0	−10,5	:	:	:	:	:	

1 As % of GDP.
2 Unemployment as % of total labour force.
3 Estimates.
4 Forecasts.

Source: Eurostat and Commission services.

concerned. For there should be a considerable improvement in the terms of trade, especially because of the extremely moderate tend of import prices, which will make disinflation easier while enabling the balance-of-payments deficit on current account as a percentage of GDP to be halved to well under 1%.

Problems of economic policy

The outlook for the economy is still dominated, in the short run and in the longer run, by the international situation, on which it has become considerably dependent. The international environment was rather adverse in 1982, and will no doubt improve only slightly in 1983; this has delayed the adjustments begun in late 1980. The delay has led to a proportionate autonomous increase in external debt (apart from the increase due to other causes) as a result of the rise in the dollar and high real international interest rates. The cost of servicing and redeeming this debt may well mean that the adjustment process in the real economy must last until the end of the decade, which could seriously compromise future growth.

It does not appear, however, that the outlook justifies more stringent restrictions on domestic demand than those applied at the moment. Recent budget and tax provisions will reduce potential domestic demand by 2,5 points of gross domestic product, all other things being equal. The agreement of January 1983 on labour costs also implies a reduction in the purchasing power of wages in 1983, as a result of fiscal drag, and the provisions of the agreement do not leave much room for a reversal of this tendency in the coming two years. Finally, extremely high real interest rates are still exercising strong pressure on the potential demand of firms, while their profit margins are likely to recover only slowly. The restrictions on real domestic demand thus appear to have reached the limits that are tolerable for an economy already seriously affected by unemployment, where the tendency to encourage productivity gains at the expense of employment is becoming increasingly marked.

But while the drive to compress domestic demand seems to have gone as far as it can, it may be, on the other hand, that more ambitious objectives could be adopted for disinflation. The present strategy of gradual de-escalation involves programming a reduction of a few points of inflation every year, to contain expectation, and setting an example by adapting remunerations and prices directly dependent on the authorities on the basis of the programmed rate. But in practice it is more than likely that the declared obectives will be regarded as norms rather than strict limits, and that actual rates will be higher. It might therefore be better to set more ambitious objectives—if not for 1983, when it will be difficult to achieve the present aim, in view of the initial situation, then at least for 1984 and subsequent years. More rapid disinflation cannot but improve the conditions in which the economy participates in the gradual recovery of world trade, and its chances of taking full advantage of that recovery.

The adjustment of the economy to its external environment raises more serious problems, however, of a specifically structural type. There is, first, the question whether the requirements of adjustment can be met for very long in view of the steadily expanding tendency of the share of public expenditure in the economy. For a number of structural reasons, mainly associated with the automaticity of many public spending items, public expenditure has been tending upwards in real terms for many years along a path that is quite independent of economic growth, so that its share in gross domestic product has increased steadily over the past few years, particularly since growth came to a halt. Revenue, however, which is normally large in relation to income (very large where personal income tax revenue is concerned), has been quite inadequate to keep up with this expansion in expenditure; consequently, net Treasury borrowing has been tending to expand, putting the economy under a permanent threat of excessive growth of demand. The only way the authorities can guard against this threat is to keep interest rates high enough to limit the monetary impact of the deficit, or to reduce the deficit by increasing the tax burden. In both cases, these financing constraints will lead to higher costs in the productive sector: either directly in the first case, or indirectly in the second as a result of the consequent wage claims. This will lead to a competitive disavantage, the more serious as it is accompanied by the external disadvantages resulting from the relative inefficiency of many government services and departments. Thus the economy's chances of success in international competition will depend to a large extent on how far the authorities can bring the expansion of public expenditure down to a figure commensurate with the growth rate, and ensure rational allocation of expenditure.

The constraints of the external environment will also require more adaptability of the economy, so that it can adjust to faster change. The international division of labour will impose new choices of specialization, while at the same time fiercer world competition will call for increasingly fast technological progress. It is thus important, in the interest of competitiveness and consequently, in the final analysis, of employment, to eliminate the institutional rigidities that could hamper necessary development as they did in the 1970s. Both industrial policy and social policy are now moving in the appropriate direction, as firms in the private and semi-public sectors are once more enjoying broader freedom of management. Understanding is improving between the two sides of industry: witness the agreement of 22 January on costs and working conditions. This should make for easier progress.

In the new industrial policy now emerging, the authorities will still have important responsibilities, including that of providing infrastructures required for adjustment not only in the industrial sector but also in agriculture and certain services, such as tourism. This will involve, among other things, the major task of carrying out the plan to minimize energy dependence by 1990. They also have to draw up a new strategy for action in favour of sectors where their aid is indispensable. Finally, they will have to implement employment policies, training policies and research policies that actively support the drive to adjust production structures.

Italian monetary policy: from the bypassing of the banks to the return to indirect credit controls

The control of bank credit by the Italian monetary authorities has traditionally been indirect, through the manipulation of market instruments to limit the banks' liquid reserves and thus control their capacity to grant credit.

None the less, the rapid increase in public sector deficits during the 1970s, a high and variable rate of inflation, as well as a considerable lack of balance in the external accounts, pointed to the need for a restrictive monetary policy which would have caused substantial interest rate instability. This led the authorities, from 1973 onwards, to the use of administrative controls for the growth and composition of bank credit, rather than to marked increases in interest rates. This framework made it possible to limit demand rapidly, whilst restraining the fluctuations of interest rates and, by so doing, moderating the negative effects on the financing of investment.

At the same time, the choice in favour of direct controls freed the Treasury from the constraints imposed by a credit control by means of regulating interest rates.

The public sector deficit therefore led to substantial monetary creation, as a result of the difficulty in selling to the public government securities, both medium and long-term, which generally offered a negative rate of interest.

The banks themselves, in spite of the credit ceiling imposed, which obliged them to place the funds received from the public in Treasury bonds and other government securities and in bonds issued by the specialized medium-term credit institutions, did not take up all the monthly offer of Treasury bonds at the rates set. Consequently the Bank of Italy had to purchase that part of the issue not taken up, so abandoning the strict control of monetary creation.

As government securities carried a relatively low interest rate, and as the rates for the bonds of the specialized institutions [1] were maintained at an artificially low level, these measures squeezed the banks' profitability, especially as compulsory reserves of 15,75% [2] of any increase in deposits taken had to be placed in an account yielding only 5,5%. The banks therefore maintained a wide margin between lending and deposit rates.

In 1979, with the renewal of inflation, the reversal of the trend of the balance on current account and the global rise in interest rates, rates on Treasury bonds rose steeply; the banks, however, were not willing to increase their deposit rates to the same extent, because they needed to keep a substantial margin between lending and deposit rates, and they were anxious not to increase lending rates too far.

As the differential widened between interest on Treasury bonds and interest on deposits, private operators rearranged their portfolios, substituting Treasury bonds for bank deposits and thus bypassing the banks, whose resources were reduced in proportion to the share of savings invested directly in Treasury bonds. The banks have therefore preferred to lose deposits (i.e. reduce balance sheets) rather than reduce the rate of profit by narrowing the margin between lending and deposit rates.

The shift to disintermediation was sharpened by the monetary authorities, in 1981, when the rates on Treasury bonds, as well as the whole range of interest rates, were raised at a time of declining inflation rates. This move led to positive real interest rates for savers so enabling the Treasury to finance its needs without obliging the Bank of Italy to intervene at the monthly issuing of Treasury bonds. Since July 1981, the Treasury has not asked the Bank of Italy to honour its undertaking to buy up the unallocated portion of bonds; since September 1981, the Bank has not been systematically subscribing medium-term government securities. This was the famous 'divorce' between the Treasury and the Bank of Italy.

During this period, the Bank of Italy perfected instruments for the indirect control of credit and improved facilities for the regulation of bank liquidity, with a view to the possible removal of credit ceilings at some future date. The new arrangements involved auction sales of Treasury bonds during the month (in addition to regular sales at the end of the month); purchase and sale of Treasury bonds on the secondary market, with a commitment to re-sell or buy back on a specified date; the introduction of the competitive method [3] for bond auctions, heretofore used only on the secondary market, but now to be adopted for new issues.

Credit ceilings had become a problem, since they reduced competitiveness within the banking system and affected the flexibility of balance sheets. However, if ceilings had simply been lifted, the banks would no doubt have reacted by increasing loans to the private sector and reducing purchases of Treasury bonds, unless the interest rates offered by the Treasury could compete with bank lending rates. The problem of restoring the banks' freedom to manage their assets would have been solved if the Treasury could have done without bank financing, borrowing direct from the public at competitive rates in relation to those paid on bank deposits; this would have reduced the amount flowing into bank deposits, and thus kept banking liquidity down to a level where the monetary authorities could control it through market instruments to limit credit to the private sector.

And this is exactly what happened as a result of the bypassing of the banks. However, the system could continue to work only if the difference in interest rates between Treasury bonds and bank deposits was maintained; in 1982, the difference narrowed when a decline in the inflation rate brought down the rate on bonds,

1 Banks must place a proportion of liquidities in the securities of certain special credit institutions.

2 20% from March 1981.

3 With this method, successful bidders do not all pay the same price; bonds are allocated at the price bid for each quantity, starting with the highest bid.

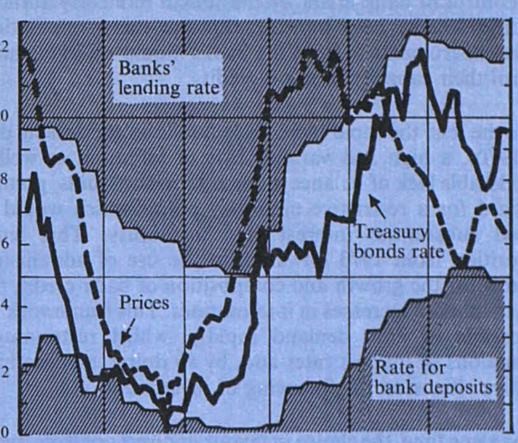
while the banks went on raising the rate on deposits during the early months of the year, holding it steady thereafter at close to the inflation rate. A difference of about nine points in December 1981 had shrunk to only about four points by September 1982. [1] In these conditions, bypassing was less popular during the second half of 1982: the Treasury was finding it increasingly difficult to raise finance on the market, while deposits were flowing into the banks [2] at an estimated annual rate of expansion of 18% in December 1982 compared with 12,2% in December 1981. Bank liquidity was expanding.

In spite of the slight rise in the rate on Treasury bonds at the end of 1982, the Treasury was finding it more and more difficult not to overshoot the legal limit on its line of credit with the central bank.

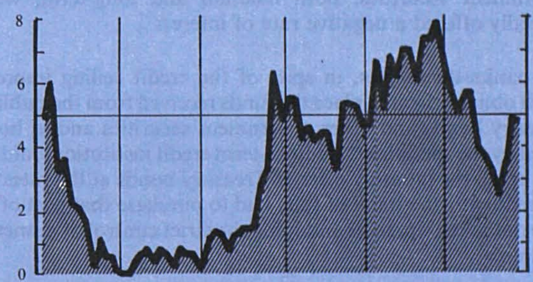
The monetary authorities were anxious to maintain the 'divorce' between the Treasury and the central bank; they were thus unwilling to oblige the bank to resume unlimited purchase of Treasury bonds, and preferred to present Parliament with a draft law authorizing the Bank of Italy to make the Treasury an exceptional advance of LIT 8 000 000 million for 12 months. A renewal of bypassing should help the Treasury find the funds to repay this advance. The authorities do not appear to have abandoned the idea of bypassing the banks, or their plans to lift credit ceilings. With this in view, the monetary authorities announced at the end of 1982 that credit ceilings would be removed at the end of June 1983, and they increased compulsory reserves from 20% of new deposits to 25%. This measure not only limits banks' liquid reserves, it also constitutes a warning to banks not to try to compete with Treasury bonds by raising the rate on deposits; for if the banks attract new deposits and thereby acquire extra liquidity, a quarter of that liquidity is transformed into compulsory reserves yielding 5,5%. To permit recourse to the use of compulsory reserves more frequently, and therefore to use this instrument within the framework of indirect credit control, the government extended the limits within which the Treasury Minister, following a proposition from the Bank of Italy, has the option to change the compulsory reserves.

The monetary authorities are now taking into consideration the allocation of the public's financial assets between deposits and Treasury bonds; previously, they took account of the public's assets as a whole. As part of this new approach, and with a view to consolidating a larger proportion of sight deposits in the form of time deposits, the Bank of Italy has decided to pay a higher rate on the compulsory reserves corresponding to time deposits. The possibility of varying yields on compulsory reserves increases the banks' profitability and thus enables them to reduce the differential between lending and deposit rates. Now that the Bank of Italy has taken the first step in this direction, the trend may develop, especially as the difference between lending and deposit rates in Italy is one of the widest. At all events, since bank loans correspond to about =four times the amount of

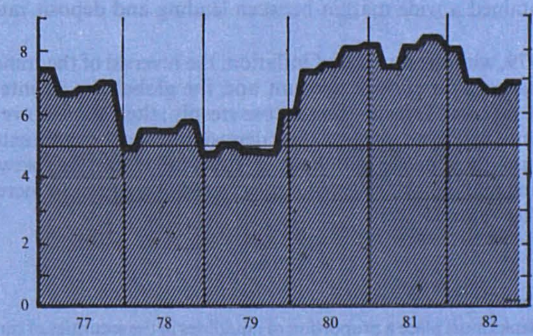
Interest rates and variation over 12 months of the consumer price index



Differential between three-month Treasury bond rate and bank deposit rate

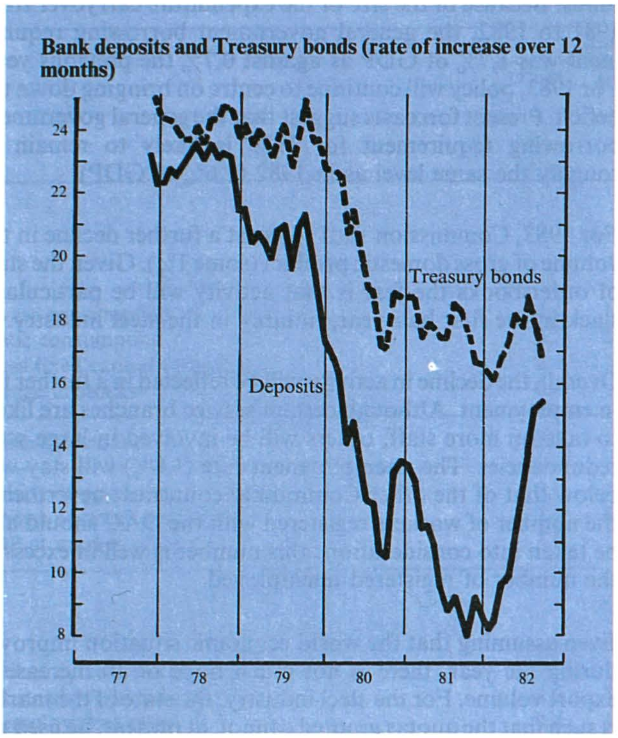


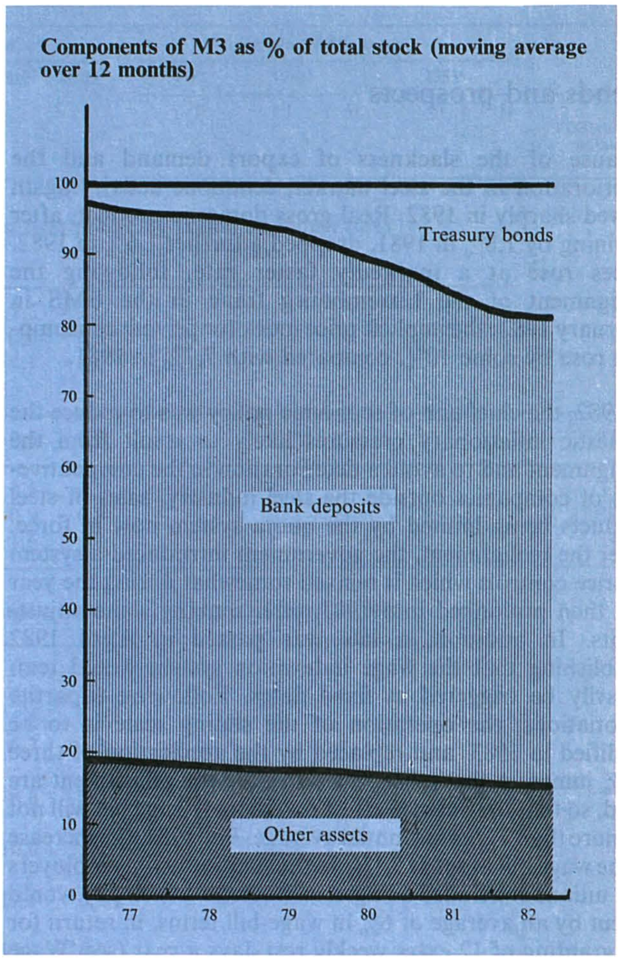
Differential between bank lending rate and rate for bank deposits



[1] Rate on 3-month Treasury bonds and average rate on deposits of LIT 10 million to 25 million.

[2] Net of deposits from public institutions.





compulsory reserves, the rate on these reserves must rise by four points for lending rates to fall by one point.

Three factors, the Treasury borrowing requirement, the need to pay a positive real rate on savings, and the need for more flexibility in bank balance sheets, have thus led the Italian monetary authorities to change their policy in two important ways: on the one hand the abandonment of the credit ceiling, and the return to the indirect control of credit, based on the regulation of bank reserves; on the other hand attention is now focused more on the development of the money supply as such, and no longer only on the total of financial assets held by the public.

Luxembourg

Trends and prospects

Because of the slackness of export demand and the deterioration in the steel market, economic activity again slowed sharply in 1982. Real gross domestic product, after declining by 1,8% in 1981, dropped a further 1,6% in 1982. Prices rose at a markedly faster rate, following the realignment of the Luxembourg franc in the EMS in February 1982; the implicit price index for private consumption rose by some 10%, compared with 7,7% in 1981.

In 1982, the chief aim of economic policy was to reduce the domestic inflationary pressures likely to result from the realignment and to avoid a deterioration in the competitiveness of companies outside the steel industry, sales of steel products being limited by the quota system now in force. After the realignment, the government introduced a system of price controls which it relaxed somewhat during the year and then prolonged into 1983, after making some adjustments. In addition, a law was passed in April 1982 establishing that the wage indexation system would temporarily be triggered at fixed dates. Following tripartite negotiations, the operation of the sliding scale is to be modified in 1983, and replaced by the application of three 2,5% jumps in the index; the dates for the adjustment are fixed, so that the induced effect on the total wage bill will not be more than 7% as an annual average. For 1982, the increase in the wage bill is put at 5,1%. In the steel industry, employers and unions concluded an agreement under which pay would be cut by an average of 6% in wage-bill terms, in return for the granting of 12 extra weekly rest days a year (see 'Wage moderation and reductions in working hours in the Benelux countries').

Budgetary policy has been tight. Total revenue increased more vigorously than forecast, thus offsetting the extra expenditure attributable to the poor economic situation, *inter alia* for work programmes within the DAC (the anti-crisis unit in the steel industry) and for the unemployment funds. Because of the size of the expenditure carryover from 1981 to 1982, the general government borrowing requirement was 1,7% of GDP as against 0,7% the previous year. For 1983, policy will continue to centre on bringing down the deficit. Present forecasts suggest that the general government borrowing requirement for 1983 is likely to remain at roughly the same level as in 1982 (1,6% of GDP).

For 1983, Commission staff forecast a further decline in the volume of gross domestic product (some 1%). Given the state of order-books the fear is that activity will be particularly slack in the first half-year, notably in the steel industry.

Overall, the decline in activity will be reflected in a further fall in employment. Although certain service branches are likely to take on more staff, others will be involved in large-scale redundancies. The unemployment rate (1,8%) will stay well below that of the other Community countries; nevertheless the number of workers registered with the DAC should also be taken into consideration: this number is well in excess of the number of registered unemployed.

Even assuming that the world economic situation improved during the year, there is not much hope of an increase in export volume. For the steel industry, the state of the market is such that the quotas granted cannot, at present, be used up. Sales of other products will be hit by the slackness of demand in most of the customer countries. The banking sector will, as before, contribute to the surplus on current account, but future expansion might be influenced by the unfavourable

(monthly average)

	1978	1979	1980	1981	1982
Registered unemployment					
— numbers	1 166	1 055	1 094	1 559	2 039
— as % of civilian labour force	0,7	0,7	0,7	1,0	1,2
Number of workers registered in the DAC	2 412	2 206	2 096	3 619	3 310

Index of industrial production

(1975 = 100 — % change over previous year)

	1978	1979	1980	1981	1982	1982 I	1982 II	1982 III	1982 IV	Weighting
General index	3,3	3,3	−3,3	−6,8	−3,7	4,5	−3,4	−5,8	−10,0	100
General index excluding steel industry	−0,7	3,4	−2,7	0,0	−2,9	2,0	−3,7	−5,2	−4,9	59,5
Steel industry	9,2	3,6	−4,1	−16,6	−5,0	9,2	−2,9	−7,0	−19,2	40,5

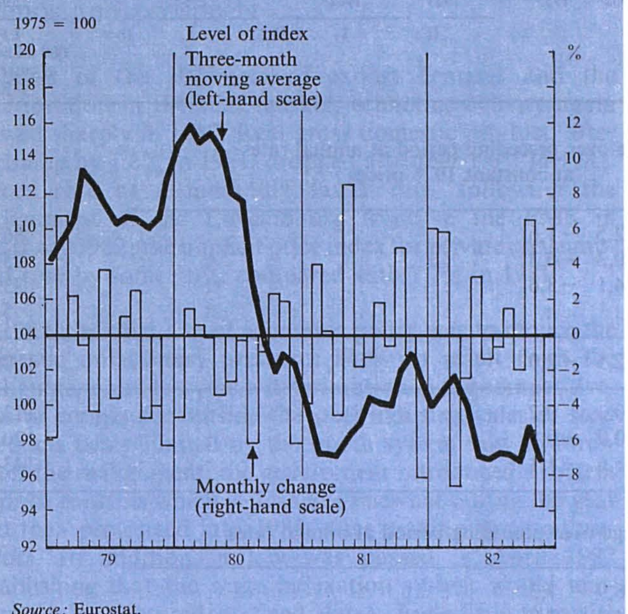
Luxembourg: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					1981
	1971-80	1981	1982[3]	1983[4]	1981	1982[3]		1983[4]		
					II	I	II	I	II	LFR '000 million at current prices
	% change over preceding period at annual rates — at constant 1975 prices									
Private consumption	4,1	1,7	−2,5	−1,6	:	:	:	:	:	86,6
Public consumption	3,7	2,1	0,3	−0,3	:	:	:	:	:	25,0
Gross fixed capital formation	2,4	−13,3	−4,1	−3,6	:	:	:	:	:	33,3
Change in stocks[1]	−0,4	:	:	:	:	:	:	:	:	5,4
Domestic demand	3,7	−1,2	−2,5	−2,0	:	:	:	:	:	150,4
Exports of goods and services	3,0	−4,9	0,3	0,2	:	:	:	:	:	113,7
Imports of goods and services	3,6	−4,2	−0,9	−0,8	:	:	:	:	:	120,9
GDP at market prices	3,0	−1,8	−1,6	−1,1	:	:	:	:	:	143,2
	% change over preceding period at annual rates									
GDP at current prices	9,5	6,1	6,9	7,3	:	:	:	:	:	
Industrial production	0,0	−8,0	−4,0	−1,0	:	:	:	:	:	
Unemployment rate[2]	0,3	1,0	1,2	1,8	:	:	:	:	:	
Compensation of employees	10,5	7,7	6,7	7,3	:	:	:	:	:	
M2	:	:	:	:	:	:	:	:	:	
GDP (implicit price index)	6,3	8,1	8,6	8,5	:	:	:	:	:	
Private consumption (implicit price index)	6,7	7,7	10,0	9,0	:	:	:	:	:	
Exports, goods (implicit price index)	5,3	8,3	12,5	6,2	:	:	:	:	:	
Imports, goods (implicit price index)	6,9	10,6	13,4	6,0	:	:	:	:	:	
Terms of trade	−1,5	−2,1	−0,8	0,2	:	:	:	:	:	
	as % of gross domestic product									
Trade balance (fob/cif)	−3,0	−15,9	−16,7	−15,7	:	:	:	:	:	
Current balance	21,3	31,0	30,2	29,8	:	:	:	:	:	
Net borrowing of general government	2,0	−0,7	−1,7	−1,6	:	:	:	:	:	

1 As % of GDP.
2 Unemployment as % of total labour force.
3 Estimates.
4 Forecasts.

Source: Eurostat and Commission services.

Luxembourg: Industrial production (s.a.)



Source: Eurostat.

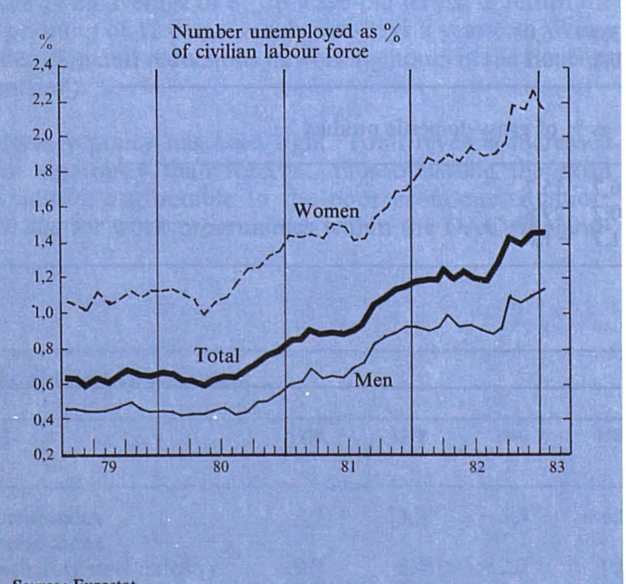
spin-offs from certain of the banking sector's national and international activities. The rise of export prices will be markedly less rapid than in 1982 when most exporting firms exploited the devaluation to improve their profit margins.

The drop in domestic demand will bring with it a decline in import volume. Given the increased surplus on the services and factor incomes account, the overall balance on current account, will show a slightly greater surplus than last year, in terms of the absolute amount.

Private consumption will again drop back because of the income restraint measures. Investment prospects remain very poor. In the steel industry the present crisis and the difficult financial situation will act as a brake on the implementation of the investment programme. In some other industries, improved sales prospects may trigger slight expansion. In new companies, investment will again be high. On the other hand investment in residential construction will decline further.

The increase of consumer prices is likely to decelerate appreciably during the year, due to the moderation of import price inflation. But despite this favourable development, the increase in the consumer price deflator is likely to remain fairly high on average (around 9%) because of the large statistical carryover at the end of 1982.

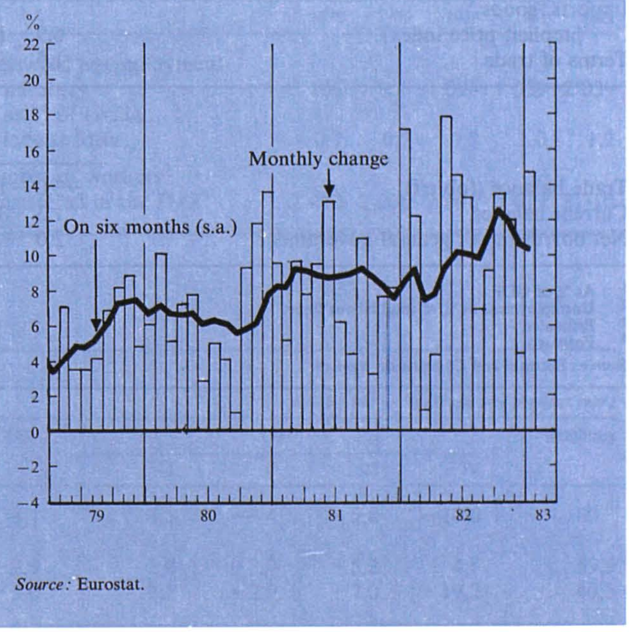
Luxembourg: Unemployment (s.a.)



Source: Eurostat.

Luxembourg: Consumer prices

Change expressed as an annual rate



Source: Eurostat.

Problems of economic policy

The tripartite conference for the steel industry (the key sector of the Luxembourg economy) enabled a recovery plan to be drawn up which, starting from the assumption that demand would pick up, provides, among other things, for a temporary adjustment in working hours, wage restraint by the workers, and financial assistance from the State. In the light of a recent study on the problems of the industry, it is legitimate to wonder whether a restructuring operation involving a significant cut-back in activity can be avoided. Such an operation would have substantial financial repercussions not only for the steel industry but also for the private banks and public financial institutions: whether it will be advisable also depends on how the situation of foreign ventures of the Luxembourg steel industry develops.

The mortgaged future of the steel industry underscores the need to step up efforts to diversify the Luxembourg economy by attracting new companies and by encouraging the specialized foreign companies already there to expand. The unfavourable economic climate makes this task both more difficult and more urgent.

Despite the uncertainty surrounding the steel industry, the Luxembourg economy does have some major advantages. First, cooperation between employers, unions and the government is producing satisfactory results, as the tripartite agreements confirm: for 1983, these provide for a temporary modification of the automatic wage indexation system. Nevertheless, it is particular to ask whether the choice of fixed dates for wage adjustments is not liable to bring with it wage increases which exceed both price increases in the Grand Duchy itself and average wage increases in competing countries, so that the government's policy of safeguarding Luxembourg's competitive edge is undermined. It would probably also be wise to avoid the development of excessively wide wage differentials between industries: these could have knock-on effects, with the general level of pay drifting out of control as a result.

The balanced trend in public finance is another of the Luxembourg economy's advantages. Nevertheless, as in other countries, care must be taken to avoid the danger of overrunning expenditure and declining revenue.

The difficulties which arose within the BLEU system of monetary association when the Belgian and Luxembourg francs were devalued can probably be avoided in the future, as a result of the conclusion of improved monetary cooperation agreements. Nevertheless, these have not solved the problem of how to coordinate the economic policies pursued in the two countries, one main aim being to avoid excessively wide divergences in company competitiveness.

The Netherlands

Trends and prospects

In 1982, the trend of economic activity and employment in the Netherlands was much less favourable than in most of the other Community countries. Real gross domestic product fell by some 1 ½% while the number of unemployed increased from an average of 7,5% of the labour force in 1981 to 10,5% in 1982.[1] However, there was a further slowdown in inflation: the rise in consumer prices in 1982 at 5,5% was well below the Community average. The balance of payments on current account again showed an appreciable surplus, equivalent to 3,3% of gross domestic product. The general government borrowing requirement (excluding social security) continued to increase despite the various measures taken to reduce it; in cash terms, it amounted to 9,5%[2] of net national income, as against 8,3%[2] in 1981.

The aim of budgetary policy is to reduce this borrowing requirement (excluding non-budgetary operations) to 10,7%[2] of net national income in 1983. Accordingly, new spending cuts will be imposed; they will apply principally to public employees' pay and to social security benefits. Sharp cuts in central government contributions to the social security funds will lead to a significant increase in social security contributions.

In trying to improve business profitability, particular importance is being attached to a continued policy of wage moderation. In 1983, the trend of the wage and salary bill per person employed will depend to a quite significant extent on the way in which the national agreement concluded at the end of 1982 between employers and employees is implemented. The agreement provides for the possibility of replacing the automatic cost-of-living adjustment due at the beginning of 1983 by a proportional reduction in working hours and the preservation of jobs (see box on 'Wage moderation and reductions in working hours in the Benelux countries').

Domestic demand will probably continue to decline in 1983. Even if export demand picks up during the year, there is little hope of any upturn in economic activity. According to the most recent Commission estimates, real gross domestic product, which fell by 1 ½% last year, will, on average,

[1] According to the definitions used by the Statistical Office of the European Communities.

[2] In national accounting terms, the general government borrowing requirement amounted to 4,6% of gross domestic product in 1981, 6,0% in 1982 and to 6,2% in 1983.

Contributions to changes in gross domestic product [1]

	1978	1979	1980	1981	1982	1983
Domestic demand [2]	3,9	1,8	− 0,5	− 3,4	− 1,8	− 1,0
External balance	− 1,3	0,6	1,1	4,1	− 0,3	1,1
GDP	2,7	2,1	1,0	− 1,2	− 1,5	0,1

[1] Change as % of GDP of the previous year.
[2] Excluding changes in stocks.

remain at its 1982 level. It is to be feared that this will result in a further deterioration in employment.

On the other hand, cost and price increases this year will probably again remain well below those in most of the other Community countries. With the anticipated moderate trend of wages and salaries and a further improvement in labour productivity, unit wage costs are expected to increase by barely 1%. Furthermore, in addition to the anticipated further fall in commodity and petroleum product prices in world markets, a possible further appreciation in the guilder will have a favourable impact on import prices: the Commission departments estimate that import prices will fall by an average of 2% in 1983. The decline in wage costs and import prices should be reflected in an equivalent reduction in export prices. Consequently, in contrast to developments in 1982, when an appreciable rise in export prices produced an improvement in the terms of trade, there is little likelihood of any such improvement in 1983 as things stand at present. The rise in consumer prices will probably be limited to an average of 3% in 1983, even though there will be sharp increases in a number of public utility charges.

The moderate growth of total wages and salaries in the private sector, the cuts in public sector pay and in transfer payments, and the further increase in social security contributions will result in a decline in disposable wage and social security incomes. However, other incomes will increase slightly. Given the relatively low rise in consumer prices, the volume of private consumption will, for the fourth consecutive year, show a decline, this time of the order of 2%.

On the whole, the conditions for a recovery in investment remain rather unfavourable. The propensity to invest will no doubt be improved by the appreciable fall in interest rates which got under way during the last few months of 1982. The long-term interest rate, which was as high as 11,3% in January 1982, was down to around 8% in February 1983. However, while wage incomes as a proportion of firms' value added are decreasing somewhat, firms' profitability remains very low.

Wage incomes as a proportion of firms' value added (excluding mining, public utilities and residential property)

1978	1979	1980	1981	1982	1983
87	89	90,5	91	89	88

Source: Centraal Planbureau.

Unemployment by age category

(as % of the end-period total number of employees)

	1979	1980	1981	1982
Up to 24 years of age	8,8	10,0	15,7	21,8
From 25 to 64 years of age	3,8	4,4	6,5	9,2
Total	5,1	5,8	8,9	12,4

Source: Ministry of Social Affairs and Employment.

The propensity to invest is also being affected by the heavy indebtedness of many firms and by capacity underutilization and weak markets. For the time being, therefore, there is little hope of any general improvement in investment activity. The increase in investment in plant and machinery expected in 1983 is due to a major investment project in the petrochemical industry. In residential construction, a further decline must be expected in public housing, while subsidized housebuilding is likely to pick up somewhat, partly as a result of the fall in interest rates. In the non-subsidized sector, the outlook remains rather bleak, mainly because of the large stock of unsold housing. As in 1982, the volume of public investment will decline.

If world trade picks up a little in 1983, exports of goods and services from the Netherlands will no doubt grow further particularly since the relatively favourable trend of prices will probably allow domestic firms to improve their positions on foreign markets. However, the volume of exports of natural gas will expand only marginally. The volume of imports will show little or no increase, mainly because of the anticipated weakness of domestic demand; imports of services will actually decline significantly because of the sharp reduction in spending on tourism abroad. Overall, there will be a further increase in the current balance-of-payments surplus, which is expected, on present estimates, to amount to 4,4% of gross domestic product as against 3,3% in 1982.

As a result of the prospective slowdown in economic activity and a further increase in the labour force, the official unemployment rate could average more than 13½% in 1983, which, in contrast to previous years, would be above the Community average; use of the calculation method introduced on 1 January[1] would bring the figure up to almost 16%. Youth unemployment is particularly worrying.

[1] Since 1 January 1983, a new and broader definition of unemployment has been used. Now, in contrast to the previous definition, the number of unemployed includes persons who, in the opinion of the employment services, are not placeable; it also includes persons seeking a job of at least 20 hours a week as against 25 hours previously. Under the new definition, the number of unemployed in the period 1981-83 will be some 20% higher than hitherto supposed.

Problems of economic policy

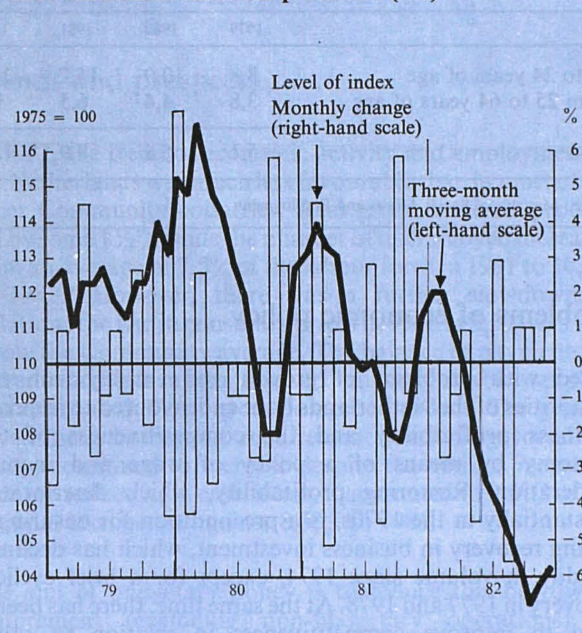
Faced with problems of growth and employment, the authorities of the Netherlands have endeavoured to improve business profitability and the competitiveness of the economy by means of a policy of wage and income moderation. Restoring profitability, which deteriorated substantially in the 1970s, is a precondition for ensuring a lasting recovery in business investment, which has declined steadily in volume since 1974, except for a brief cyclical recovery in 1977 and 1978. At the same time, there has been a need to improve competitiveness in relation to other countries, which had been seriously eroded by the sharp wage increases granted in earlier years. A further task has been to contain the sharp growth of private consumption evident in the 1970s and to increase private saving. A reduction in the general government deficit and a cut-back in the level of taxation and parafiscal charges must also be seen as preconditions for reviving economic activity and restoring employment.

Since 1980, the volume of private consumption has contracted by an average of almost 2% a year. However, the slowdown in the rise in wage costs during recent years has not been sufficient to allow an improvement in business profitability and hence a structural recovery in investment. Such a recovery has also been thwarted by the unfavourable trend of the world economy, one result of which has been that the improvement in competitiveness secured in recent years has been reflected to only a limited extent in the growth of export demand.

The weakness of domestic demand and the high level of revenue from natural gas have been major factors in the substantial balance-of-payments surpluses in recent years. It is anticipated that there will again be a large current account surplus in 1983, despite a fall in the export price of natural gas which follows that of heating oil.

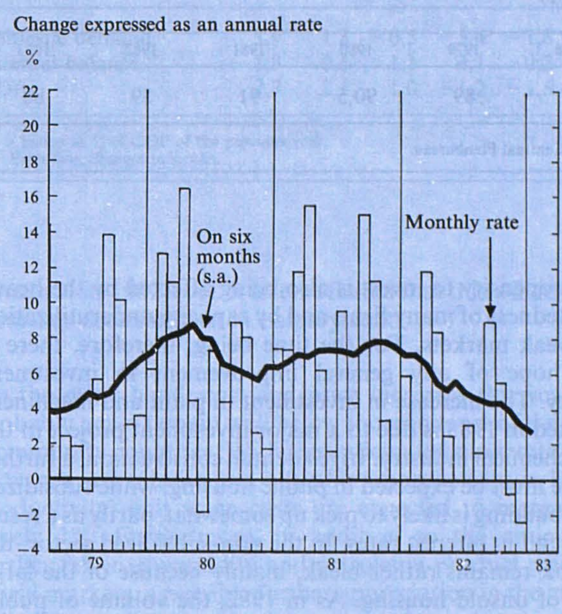
Although the strength of the guilder deriving from this trend has impaired the competitiveness of firms, it has also contributed to a further slowdown in domestic price and cost increases and played an important role in the sharp drop in interest rates in 1982.

The Netherlands: Industrial production (s.a.)



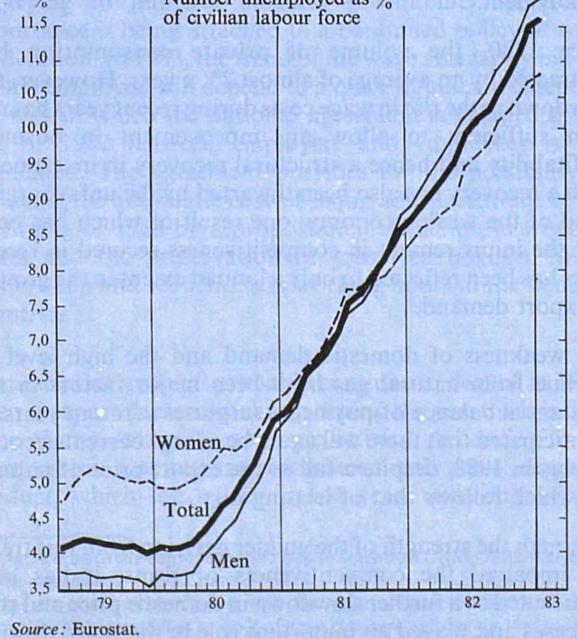
Source: CBS.

The Netherlands: Consumer prices



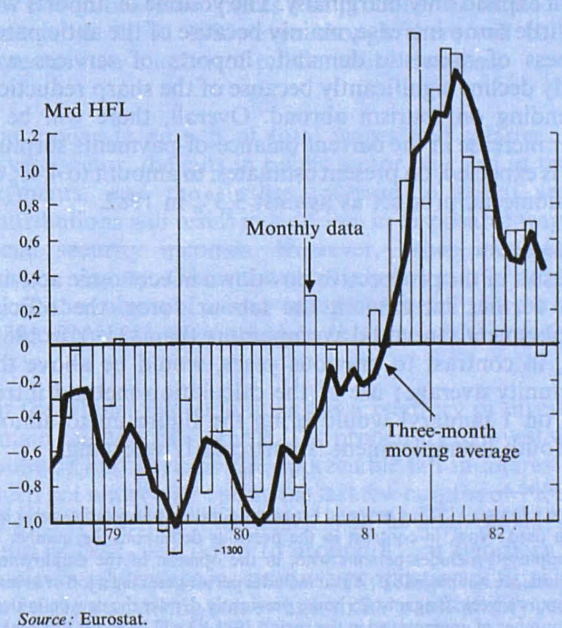
Source: Eurostat.

The Netherlands: Unemployment (s.a.)



Source: Eurostat.

The Netherlands: Trade balance (s.a.)



Source: Eurostat.

The Netherlands: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					
	1971-80	1981	1982[3]	1983[4]	1981	1982[3]		1983[4]		1981
					II	I	II	I	II	HFL '000 million at current prices
	% change over preceding period at annual rates — at constant 1977 prices									
Private consumption	3,9	−2,6	−1,8	−2,0	−3,3	−1,7	−0,2	−2,3	−3,1	212,6
Public consumption	2,7	1,5	0,5	1,6	0,9	0,2	0,7	1,7	2,2	62,9
Gross fixed capital formation	0,8	−10,8	−5,0	−0,8	−9,9	−3,7	−2,5	−0,8	0,9	66,4
Change in stocks[1]	0,9	−1,0	−0,4	−0,3	−1,1	0,2	−1,0	−0,8	0,2	−4,4
Domestic demand	2,8	−5,3	−1,3	−1,0	−4,3	1,0	−2,8	−0,9	0,6	337,5
Exports of goods and services	5,4	0,9	−0,8	1,9	1,4	0,4	−5,3	4,1	5,2	204,5
Imports of goods and services	4,1	−7,4	−0,2	−0,1	−4,8	5,8	−7,0	1,8	3,3	191,4
GDP at market prices	3,4	−1,2	−1,5	0,1	−1,1	−1,4	−2,1	0,4	1,8	350,5
	% change over preceding period at annual rates									
GDP at current prices	11,4	4,3	4,3	1,8	8,2	6,1	−3,1	3,2	3,8	
Industrial production	2,9	−1,8	−3,5	0,3	−0,9	−4,2	−5,6	1,9	3,3	
Unemployment rate[2]	3,4	7,5	10,5	13,3	8,5	10,3	11,3	13,1	14,1	
Compensation of employees	10,7	3,3	5,9	2,7	4,7	6,9	5,2	2,4	0,9	
M2	11,6	5,2	7,6	5,2	:	:	:	:	:	
GDP (implicit price index)	7,6	5,6	5,9	1,7	9,4	7,6	−0,9	2,8	2,0	
Private consumption (implicit price index)	7,7	6,5	5,5	3,0	7,3	6,1	2,7	2,7	3,8	
Exports, goods (implicit price index)	6,9	15,9	4,0	−1,7	16,1	0,6	−0,2	−1,6	−3,4	
Imports, goods (implicit price index)	7,9	16,7	1,5	−2,0	9,0	−4,0	5,7	−4,7	−3,9	
Terms of trade	−0,9	−0,7	2,5	0,3	6,5	4,8	−6,6	3,3	0,5	
	as % of gross domestic product									
Trade balance (fob/cif)	2,2	3,7	4,4	5,2	:	:	:	:	:	
Current balance	1,3	2,4	3,3	4,4	:	:	:	:	:	
Net borrowing of general government	−1,4	−4,6	−6,0	−6,2	:	:	:	:	:	

[1] As % of GDP.
[2] Unemployment as % of total labour force.
[3] Estimates.
[4] Forecasts.

Source: Eurostat and Commission services.

Given the large current account surplus and the very moderate rise in costs and prices, the economy of the Netherlands would appear to have some room for manœuvre for stimulating economic growth.

From the monetary point of view, most of this room for manoeuvre has already been used, as can be seen from the relatively rapid growth of the money supply and the appreciable fall in interest rates. Any sharper increase in the growth of wages and salaries would affect the profitability of the enterprise sector and competitiveness and would in particular pose the question of an appropriate exchange rate policy.

Consequently, it is ultimately the room for manoeuvre in budgetary policy which is the key factor. It must be borne in mind here that, during recent years, the general government borrowing requirement has increased at an accelerating rate, partly as a result of insufficient growth in revenue (due to the low level of economic growth, the rather low rate of inflation and the declining revenue from natural gas), and partly as a result of the sharp increase in expenditure, notably in the area of transfer and interest payments. While the increase in the general government deficit has not yet posed unduly serious financing problems, it is essential that it should be checked if the growth of expenditure is not to become increasingly uncontrollable and if an increasingly heavy interest burden is not to restrict unduly the room for manoeuvre available in budgetary and general economic policy. In the years ahead, very severe spending curbs will continue to be necessary, notably in the area of transfer payments, which have increased steadily. The public authorities must where possible rid themselves of tasks which are not their own specific responsibility and ensure that more of the costs of public services are passed on to users. In re-examining budgetary priorities, however, particular attention will have to be paid to reducing the burden on firms, as is indeed the government's intention.

The employment outlook in the years ahead is very gloomy. Redundancies will continue in industry, while budgetary stringency will result in a further reduction in employment in the public sector and in the subsidized non-market services sectors. At the same time, the growth of the labour force in the Netherlands is among the highest in the industrialized world. In these circumstances, the problems of redistributing work and reducing working hours will take on increasing importance. The above-mentioned agreement concluded between the national employers' and employees' organizations is of particular significance in this respect. However, care will have to be taken to ensure that the measures introduced in this area do not have the effect of increasing costs and thus jeopardizing the necessary improvement in business profitability. Efforts will also have to be made to increase the mobility of labour, notably through greater differentiation of incomes as between the working and non-working sections of the population and as between the various sectors and jobs.

United Kingdom

Trends and prospects

Economic activity increased somewhat in 1982, largely because of a significant recovery in private consumption, particularly in the second half of the year. This recovery in demand was accompanied by a fall in the level of stocks. Manufacturing production remained sluggish. Unemployment continued to increase, but at a slower rate than in 1981.

Inflationary pressures eased rapidly with the rate of consumer price inflation falling markedly in the third and fourth quarters. There were also large gains in labour productivity in manufacturing.

Export volumes held up well in 1982, despite the lack of UK export competitiveness, and sluggish world trade, so contributing to a substantial current account surplus of about UKL 4 500 million (1 ½% of GDP).

Economic policy for 1982-83 was established within the framework of the medium-term financial strategy (MTFS) published in March 1982, which included a target range for monetary growth of 8-12 % for the 1982-83 financial year. This range was set at a higher level than that indicated in earlier statements, a move partly reflecting apparent structural changes in the monetary aggregates and the velocity of circulation. These changes had led to the difficulties encountered, in previous years, in ensuring that the money supply as broadly defined, sterling M3, remained within the target ranges specified for it. Moreover, the authorities had taken the view that it was no longer appropriate to base the conduct of monetary policy largely on the control of a single aggregate.

Consequently for 1982-83 the 8-12% target range was applied to a range of monetary measures, both narrow and broad, and was officially considered to be consistent with a further easing of inflationary pressures, falls in interest rates, and an adequate recovery in economic activity. Indeed the falls in interest rates that occurred in 1982 were relatively marked.

Consumer prices and productivity

(% change at an annual rate)

	1981 I	1981 II	1981 III	1981 IV	1982 I	1982 II	1982 III	1982 IV [2]
Consumer prices	9,0	15,1	9,6	9,3	6,4	11,6	4,5	5,1
Productivity [1]	7,4	12,5	17,0	4,5	4,1	4,1	4,9	3,2

[1] Output per person employed in manufacturing industry.
[2] Estimates.

(weekly average %)

	1981 December	1982 March	1982 June	1982 September	1982 December
UK inter-bank sterling deposit rate	15,10	13,62	13,03	10,99	10,75

At the same time favourable developments in public sector revenues and expenditure provided scope in 1982-83 for a reduction in taxation. The major part of the available room for manœuvre was used to reduce the burden of taxation upon the company sector, particularly through a reduction in the national insurance surcharge. The changes in taxation led to an expected public sector borrowing requirement (PSBR) of UKL 9 500 000 million (3 ½% of GDP) for 1982-83 (compared to 4¼% in the previous financial year), a level considered to be appropriate to the target range for monetary growth.

However, the development of public sector borrowing made possible a number of discretionary changes to monetary and fiscal policy in the course of the year. Thus, in July 1982, hire purchase controls on the purchase of consumer durables were abolished, and in the event this gave a considerable stimulus to private consumption. In addition, the authorities announced, in November, in their 1982 Autumn Statement on economic policy, a modest reduction in the burden of taxation on the company sector for the financial year 1982-83. Despite these measures the PSBR is still expected to be only UKL 9 000 million for the financial year as a whole, somewhat below the original target level.

Although the discretionary policy changes which took place in the course of 1982 were of importance, of particular significance for the future development of the economy was the market change in the value of sterling towards the end of 1982 and early in 1983. Pressure on sterling began in November and by the end of January the effective exchange rate had fallen by over 12 %.

This movement was the result of a number of factors. In particular, financial markets had clearly become concerned about:

(i) a possible fall in the price of oil, which would have a significant impact on the UK's external position;

(ii) the underlying deterioration in the external accounts, due in part to the weakness of the growth of manufactured exports, a response to the substantial loss of export competitiveness in the period to 1981. In addition, the substantial outwards movements of private sector capital, a feature of the external position since the abolition of exchange controls in late 1979, have continued;

(iii) the possibility of an election in 1983 and the uncertainties for economic policy such a situation implies.

The fall in the value of sterling was accompanied by some upward pressure on interest rates.

The main framework for monetary and fiscal policy for the financial year 1983-84 has already been given in the MTFS published in March 1982, and the November 1982 Autumn Statement. Thus the target growth range for the monetary aggregates is 7-11% and the PSBR officially foreseen is UKL 8 000 million (2¾% of GDP).

Monetary developments in 1982-83 remain consistent with the 7-11% target. On the other hand, lower inflation in late 1982 than expected and underspending on capital projects point to a level of public expenditure in 1983-84 somewhat below that foreseen earlier. The government's expenditure plans for 1983-84, published on 1 February, by allowing for an expenditure shortfall, now foresee an increase in the planning total by 5,8% to UKL 119 600 million, compared to UKL 120 100 million in the Autumn Statement and this development, together with a more favourable outlook for revenues, suggests that, on the basis of present policies, the PSBR, even in the case of indexation of personal tax allowances and specific duties, could be about UKL 6 500 million, below the level of UKL 8 000 million given in the Autumn Statement.

On the assumption that the sterling exchange rate remains at its present level, that the recent deceleration in the growth of average earnings is maintained in the year ahead, that the growth of the monetary aggregates remains within the target range specified, and that the stance of fiscal policy in 1983-84 remains unchanged, except the indexation of personal tax allowances and specific duties, the outlook for the economy in 1983 is for a modest increase in the rate of growth of GDP, accompanied by a significant change in the structure of demand, to which the fall in sterling will make a major contribution. In particular the relatively rapid expansion of private consumption, observed in the second half of 1982, is foreseen to slow down significantly, and in the second half of 1983 a slight fall in the volume of consumption expenditure can be expected, as the growth of earnings falls and real personal disposable incomes are squeezed. Investment should expand modestly and there should be some stock accumulation as the year progresses.

Export volumes

(% change)

	1979	1980	1981	1982	1983
Exports of crude oil	68,0	−0,8	37,7	13,2	6,7
Exports of other goods	1,0	3,3	−4,3	−1,6	1,7
Total	3,4	1,8	−0,5	0,4	2,5

On the external side the outlook is for a significant improvement in the rate of growth of export volumes. This reflects both a further increase in North Sea crude oil exports, although at a more modest pace than in 1981 and 1982, and an increase in the volume of exports other than crude oil (mostly manufactures), following two years of relatively marked decline. This change partly reflects the recent improvements in UK export price competitiveness (see box).

Taking account of an adverse movement in the terms of trade foreseen for goods as a whole, the current account of the balance of payments is expected to move into deficit in the second half of the year.

Although the growth of average earnings should slow down further, import prices (in sterling terms) in 1983 are expected to show a marked increase (approaching 10% for the year as a whole), and these developments point to a modest increase in the underlying rate of inflation from the middle of the year onwards.

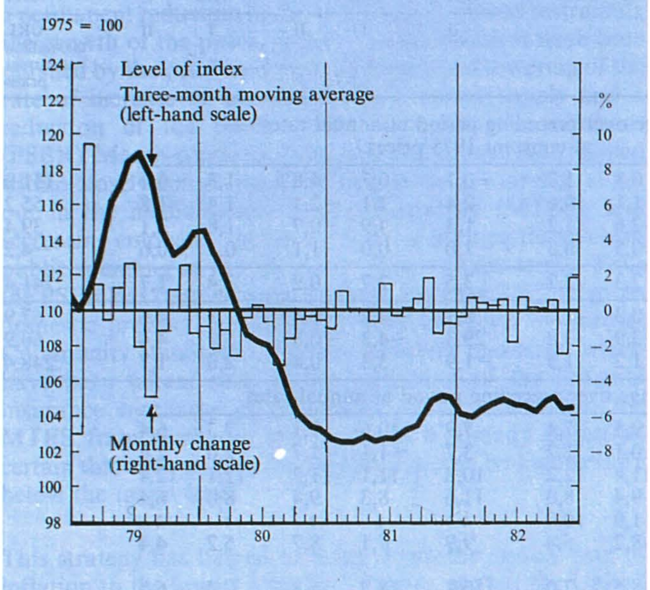
Unemployment (including school-leavers)

('000)

	1981				1982			
Total number of unemployed [1]	2 235	2 433	2 629	2 750	2 787	2 839	2 973	3 062
of which: [2]								
— under 25	39,3	35,1	40,1	40,8	39,1	36,3	39,5	:
— unemployed for more than one year	19,2	19,8	21,5	26,8	30,7	32,7	32,6	:

1 Seasonally adjusted.
2 Based on data unadjusted for seasonal variations.

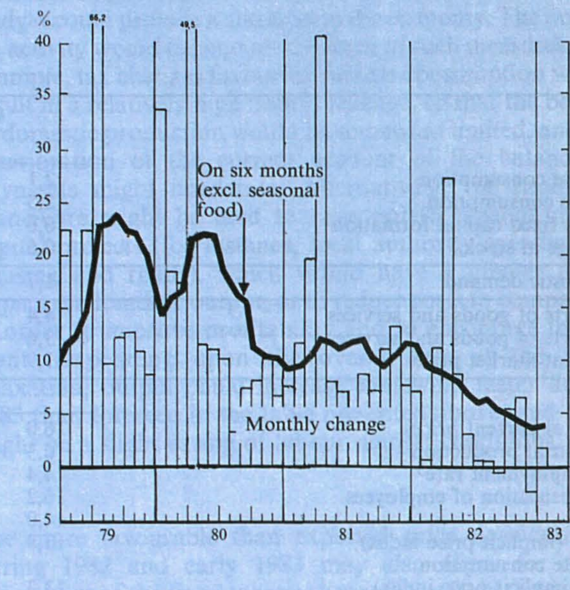
United Kingdom: Industrial production (all industries other than construction) (s.a.)



Source: CSO.

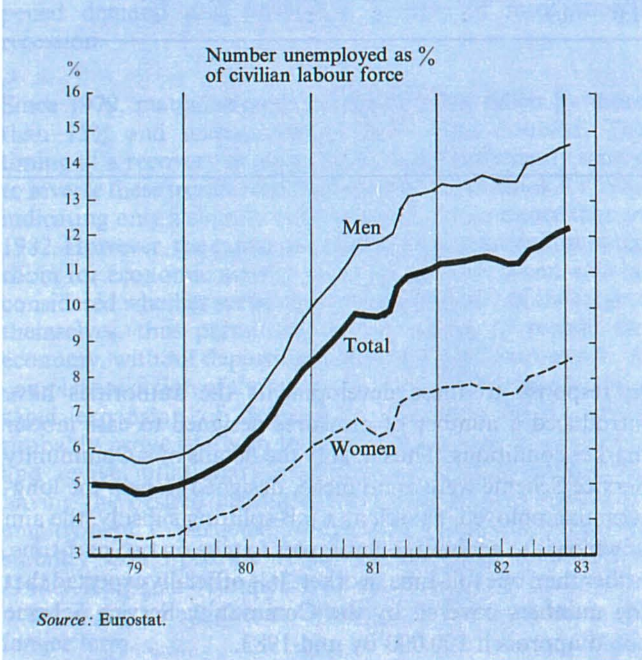
United Kingdom: Consumer prices

Change expressed as an annual rate



Source: Eurostat.

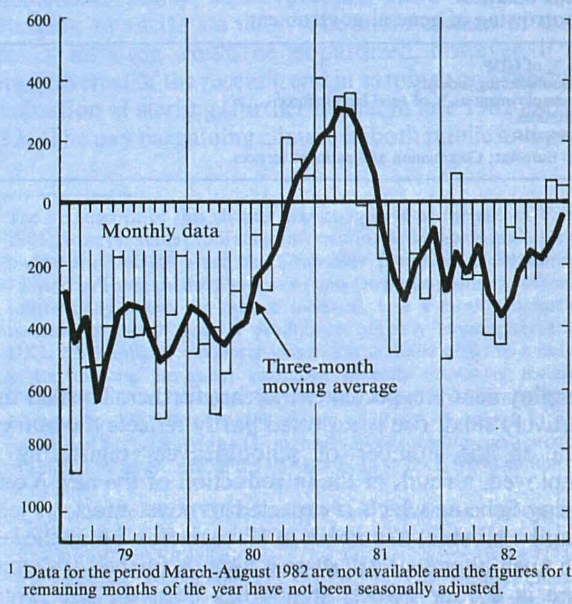
United Kingdom: Unemployment (s.a.)



Source: Eurostat.

United Kingdom: Trade balance fob/cif (s.a.) [1]

Mio UKL



[1] Data for the period March-August 1982 are not available and the figures for the remaining months of the year have not been seasonally adjusted.

Source: Eurostat.

United Kingdom: Supply and uses of goods and services together with main economic indicators, 1971-83

	Annual data				Half-yearly data (s.a.)					
	1971-80	1981	1982[4]	1983[5]	1981	1982[4]		1983[5]		1981
					II	I	II	I	II	UKL '000 million at current prices
	% change over preceding period at annual rates — at constant 1975 prices									
Private consumption	2,1	0,3	0,8	1,7	−0,1	−0,7	4,8	1,3	−0,7	151,0
Public consumption	2,5	0,3	1,1	0,6	2,4	2,1	−2,1	1,4	1,8	55,2
Gross fixed capital formation	0,6	−8,2	2,6	1,2	1,3	4,9	−0,7	1,8	2,1	39,4
Change in stocks[1]	0,5	−1,7	−0,5	0,3	−1,0	0,0	−1,1	−0,1	0,6	−4,2
Domestic demand	1,7	−1,5	2,3	2,2	3,5	2,7	0,2	3,4	1,7	241,4
Exports of goods and services	4,4	−1,9	0,3	1,7	8,7	−3,2	−0,4	1,3	4,6	67,9
Imports of goods and services	3,6	−0,2	3,9	3,8	29,3	−4,3	−0,8	5,9	4,4	60,9
GDP at market prices	1,9	−2,0	1,2	1,5	−1,9	3,3	0,4	2,0	1,7	248,4
	% change over preceding period at annual rates									
GDP at current prices	16,0	9,9	9,5	7,4	7,9	10,6	9,1	7,3	6,4	
Industrial production[2]	−0,3	−6,3	−0,1	1,2	3,7	−1,1	−1,7	2,0	2,6	
Unemployment rate[3]	4,4	9,7	11,4	12,2	10,2	11,1	11,7	12,1	12,4	
Compensation of employees	16,2	11,4	9,4	8,0	11,6	8,3	9,4	8,0	6,4	
M3	14,0	14,6	11,0	10,0	:	:	:	:	:	
GDP (implicit price index)	13,9	12,1	8,2	5,8	9,9	7,1	8,7	5,2	4,4	
Private consumption (implicit price index)	13,3	10,9	8,5	7,0	10,8	8,2	6,8	7,4	6,5	
Exports, goods (implicit price index)	13,9	8,4	7,4	6,4	13,7	4,0	8,7	6,1	4,6	
Imports, goods (implicit price index)	14,5	4,1	5,4	9,5	15,5	2,7	2,6	12,7	10,1	
Terms of trade	−0,5	4,1	1,4	−2,9	−1,6	1,3	1,8	−4,6	−3,7	
	as % of gross domestic product									
Trade balance (fob/cif)	−3,5	−0,3	−0,9	−2,2	−1,3	−1,2	−0,9	−2,0	−2,5	
Current balance	−0,7	2,4	1,5	0,3	1,3	1,2	1,9	0,8	−0,1	
Net borrowing of general government	−3,2	−2,1	−1,0	−0,9	:	:	:	:	:	

[1] As % of GDP.
[2] Manufacturing industry.
[3] Unemployment as % of total labour force.
[4] Estimates.
[5] Forecasts.
Source: Eurostat; Commission and national services.

Unemployment is expected to increase further. The fact that a relatively small rise is expected partly reflects the marked decline in the number of school-leavers registering as unemployed, a result of the introduction of the new Youth Training Scheme which is expected to cover most 16-year-olds and a substantial number of 17-year-olds. None the less, youth unemployment will remain high. A further disturbing feature in labour market trends has been the substantial increase in the numbers of longer-term unemployed (see table).

In response to these developments the authorities have introduced a number of measures designed to ease labour market conditions. Thus in July the details of a Community Service Scheme were announced, designed to help the long-term unemployed, as well as a job-splitting subsidy, the aim of which is to encourage employees to take on two part-time, rather than one full-time, worker. It is officially expected that the numbers covered by the Community Service Scheme could approach 100 000 by mid-1983.

Problems of economic policy

Since 1979 the principal goal of economic policy has been to improve prospects for growth and employment by achieving a permanent reduction in the rate of inflation and restraining the growth of the public sector. These objectives have been pursued by the combined means of a gradual lowering of the rate of increase of broadly defined money supply and a reduction of the public sector borrowing requirement (PSBR). Macro-economic policy measures have been framed within closely controlled fiscal and monetary targets, as set out in the medium-term financial strategy (MTFS), and increasing emphasis has been placed on limiting the levels of public spending in money rather than volume terms. Thus the PSBR has been brought down to less than 3½% of gross domestic product in 1982-83, a very low level by current Community standards. Any discretionary measures, which have been taken, such as the reduction of the national insurance surcharge in November 1982, were within the MTFS framework; in this instance it already appeared certain that the out-turn for the PSBR would be significantly below the target level.

This strategy has helped to bring down the annual rate of inflation to the lowest level for 13 years, so that the United Kingdom has now switched from being one of the Community countries with a faster than average rate of price increase to being one with a relatively low rate. It may also have created other underlying structural conditions more conducive to long-term growth, such as improvements in productivity well above earlier established trends, but the restrictive stance of fiscal and monetary policy has dampened demand and output at a time of international recession.

Since 1979, manufacturing production has fallen by more than 15% and unemployment more than doubled. The timing of a recovery of economic activity sufficiently strong to reverse these trends remains in doubt, the outlook for 1983 indicating only a slightly better growth performance than in 1982. However, the existing financial targets may allow some room for economic activity to be stimulated. It can also be considered whether scope exists for adjustment of the targets themselves, thus permitting further action to sustain the economy, without departing from the overall framework. A complete rejection of the current strategy, to be replaced by a rapid expansion of demand in the short term, would probably prove costly in terms of the balance of payments and revive inflationary expectations, without necessarily having the desired lasting effects on domestic output and employment. In particular, the recent relative wage and price stability should provide a basis for an improvement in the United Kingdom's competitive position which is necessary in order to promote higher investment and faster growth in the longer term.

It seems likely that there is scope within existing financial targets to allow for some fiscal relaxation.[1] As noted above, monetary developments have been in line with expectations, and the 1983-84 outlook for the PSBR is below the illustrative figure, so that measures taken in the forthcoming budget could provide a stimulus to the economy. The impact on activity would depend on the form of such measures. For example, tax changes favouring private consumption would result in a relatively high import leakage, so that the benefit to domestic production would be somewhat limited, and the deterioration of the current account of the balance of payments might accelerate. Alternatively, the room for manœuvre might be used to raise public expenditure on capital projects (for instance, local authority spending on housing and roads), which would have a greater direct impact on domestic output, or to reduce costs to companies, in order to improve profitability and to encourage investment. Depending upon the overall mix of the fiscal relaxation, output could increase somewhat faster during 1983 than foreseen in the table presented above, and there might be a slight easing of labour market conditions.

The more favourable than expected price developments during 1982 and early 1983 may also allow for some adjustment of the fiscal targets themselves within the overall financial framework. If inflation is lower than had been expected and assuming the velocity of circulation of money does not decline substantially, the (7-11%) objective for growth of money supply in 1983-84 could permit higher real expansion than the authorities had previously foreseen. If the prospects for expansion, and the demand for money, remain weak, fiscal policy could become more active without damaging financial stability. The maintenance of current rates of inflation would be jeopardized, however, if there were a reversal of the recent trend in earnings or a substantial devaluation of sterling (further to that in late 1982 and early 1983). The pay bargaining climate in both public and private

[1] The manuscript of this chapter was completed at the end of February 1983. However at the proof stage information had become available on the budget for 1983-84 which the Chancellor presented to Parliament on 15 March. The main fiscal measures were: increased personal allowances, substantially above the rate of inflation, and a modest reduction in taxation of North Sea oil production (directly reducing revenue by UKL 2 300 million); revalorization of excise duties offset by a reduction in the national insurance surcharge (directly increasing revenue by UKL 380 million). General government expenditure is expected to increase by 5,8% between 1982-83 and 1983-84 compared to a GDP increase of 7,6%, implying a fall in the level of expenditure as a proportion of GDP. The target level of the PSBR was set at UKL 8 000 million (2¾% of GDP).
A restatement of the MTFS set down a monetary growth target range of 7-11% for 1983-84 (applicable to a range of aggregates) falling to 5-9% in 1985-86, and a PSBR falling from UKL 8 000 million in 1983-84 (2¾% of GDP) to UKL 7 000 million (2%) in 1985-86. The measures announced clearly suggest that, in the official view, and in the absence of policy changes, the PSBR in 1983-84 would have been substantially less than the figure of UKL 8 000 million.

sectors is currently characterized by more moderation, partly reflecting lower inflationary expectations, but it is necessary that this continues under pressure resulting from higher import prices, or if conditions in the labour market change. If inflation remains under control and some further scope for encouraging demand is confirmed, and in view of the reversal of the adverse trend in competitiveness (see box), the outlook for domestic output should gradually improve. A critical factor in a possible recovery would be the level of interest rates, which are currently high in real terms. A sharp fall in their level might put further downward pressure on the external value of sterling and put the monetary growth targets in difficulty, but continued high real interest rates are likely to discourage the borrowing necessary to finance stock-building and investment.

The short and medium-term economic outlook will be significantly influenced by trends in the oil market. Their impact on the United Kingdom, as a major oil producer (in 1982 oil accounted for nearly a fifth of visible exports and about 6% of general government revenue), is considerably greater than on other Community countries. A marked fall in the oil price would have a wide range of direct and indirect effects on the economy. Export earnings in dollar terms would be reduced and, if this were not accompanied by a corresponding depreciation of sterling against the dollar, export revenue in sterling would also be lower, potentially putting a strain on the external account. Furthermore, a lower oil price would reduce tax revenue linked to its production, which would, in the existing financial framework, place a constraint on fiscal policy and limit the room for manoeuvre considered above. But a lower sterling price for oil would also reduce domestic costs and inflationary pressure, and some benefit to demand and output should thus be obtained.

A substantially lower dollar price for oil might also provoke downward pressure on the sterling exchange rate. Depreciation of sterling, further to that which has already occurred in late 1982 and early 1983, would however lead to increased inflationary pressure from import prices, while limiting the impact of the dollar price cut on tax revenue. In the short term at least, a lower exchange rate might also cause a deterioration in the current balance, until the markets reacted to the relative price changes. In these circumstances, particularly if there were any likelihood of a resurgence of inflation, the authorities might be expected to pursue a more active interest rate policy. The less direct effects of a fall in the oil price, through the likely benefit to growth in the industrialized economies and world trade in general, and the dangers of certain oil-producing countries falling into severe financial crises, are more difficult to assess, but might also have a substantial impact on the UK economy and on its management.

Even under the most optimistic assumptions with respect to growth of output in the medium term, the slow adjustment of the labour market and the underlying demographic conditions are such that unemployment can be expected to fall only slightly from its present level, unless further measures to tackle it directly can be implemented. The Youth Training Scheme will certainly help to reduce the number of unemployed school-leavers, but it is too early to assess whether it will create a pool of skilled labour to be drawn upon if and when the recovery occurs and thus alleviate the major problem of unemployment of the young. Further scope for dealing with the overall level may exist in the fields of work-sharing and early retirement schemes. Experience suggests that part-time jobs are popular with employees but that the costs to employers are not cut proportionately, so that appropriate institutional changes may be necessary. Until now, the application of work-sharing has mostly been concentrated in white-collar employment, and consideration should be given to its extension over a wider range of jobs. The UK activity rates for the over-60 population are still markedly higher than the Community average, but the costs of increased possibilities for early retirement, and the absence of provisions for this in pension schemes, are such that some official assistance might be necessary. Finally, it is hoped that a recovery of output would lead to significant new employment opportunities in small and new companies. Policy measures to reduce administrative restrictions and improve tax incentives for new companies, particularly in areas of high unemployment, are encouraging in this respect.

It is often argued that an underlying cause of the recent poor output performance is the insufficient rate of investment in the United Kingdom. Indeed over the past 10 years, the share of gross fixed investment in gross domestic product has tended to decline, with consequent implications for the capital stock and hence productive potential. However, this has been largely because of the sharp fall in investment by general government and in private sector housing. There is evidence to suggest that investment in manufacturing industry has remained at a relatively satisfactory level although in the United Kingdom it tends to generate less additional output than elsewhere. Possible reasons suggested for this have been attitudes of management and labour, and discontinuity of industrial policies. The choice of appropriate industrial and regional support measures, without diverting resources from their most efficient allocation, remains a problem area in economic policy.

An essential condition for future growth of investment is a further improvement of the international competitive position and, linked to this, a more favourable outlook for profitability. As can be seen in the attached box, the United Kingdom has suffered a considerable deterioration in competitiveness since the mid-1970s. The recent improvements in terms of labour productivity and inflation, together with the exchange rate adjustment since late 1982, have corrected this only to a limited extent, but allow for some optimism for future developments in this respect.

Price competitiveness and trade in manufactured goods

One of the more notable features of the United Kingdom economy in recent years has been the substantial changes of export and import price competitiveness that have occurred since the mid-1970s (see Graph 1). The loss of competitiveness was particularly marked between 1977 and early 1981, when the Commission services estimate that the UK's export prices, relative to the OECD area, increased by some 46%. The competitive position improved significantly in the course of 1981 and again in the latter part of 1982 and in early 1983, by which time it was close to that recorded in the opening months of 1980.

Reasons for the movements in competitiveness

The loss of competitiveness in the period to early 1981 was due to both internal and external factors. Of considerable importance, particularly more recently, was the behaviour of the effective exchange rate which appreciated by some 20% between the first quarters of 1979 and 1981. Three factors account for this appreciation: (i) tight fiscal and monetary policies with high interest rates and restrained demand; (ii) rising North Sea oil production; (iii) the second oil price crisis.

Since the mid-1970s there has been a significant change in the approach to economic policy in the United Kingdom, with greater emphasis being placed upon limiting the level of public sector borrowing, and on achieving a desired rate of growth of the monetary aggregates. This approach has been both strengthened and formalized in recent years, with the setting of fiscal and monetary policy targets within the framework of a medium-term financial strategy (MTFS), which in its most recent version aims for a reduction in the rate of growth of the monetary aggregates from 8-12% in the financial year 1982-83 to 6-10% in 1984-85. This change of emphasis clearly had a favourable impact on sentiment in financial markets. In addition, there has been a marked change in the structure of the UK economy as crude oil production has expanded; indeed in 1982 oil production is estimated to have been some 30% greater than inland consumption. This structural change has clearly benefited both the external position and the public sector accounts, and placed upward pressure on the sterling exchange rate. These pressures were particularly strong at the time of the second oil price crisis.

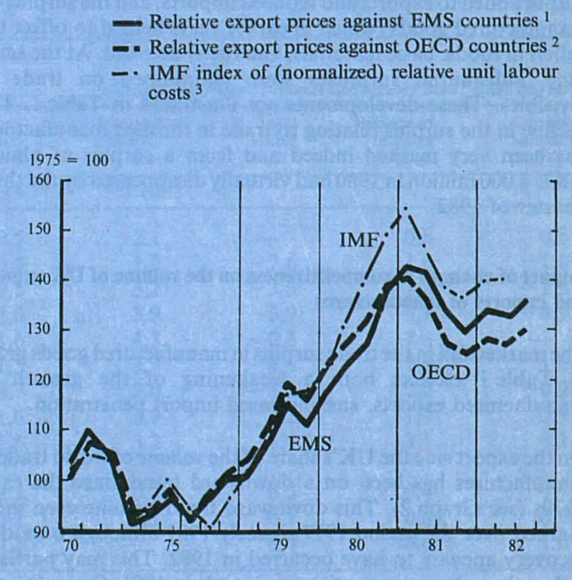
In addition to the appreciation of sterling, competitiveness was also adversely affected by a rapid rate of increase of average earnings (15% in 1979, over 20% in 1980) giving a rise in unit labour costs, significantly in excess of the increases experienced in the UK's main competitor countries. As noted above, the combined effect of sterling appreciation, and the surge in domestic costs, led to a loss of export price competitiveness by early 1981 compared to the position in the mid-1970s of well above 40%.

The improvements in competitiveness observed in 1981, 1982 and early 1983 reflect three factors: the fall in the value of sterling; the marked slowdown in the growth of average earnings, particularly in manufacturing industry, associated with the strength of the recessionary forces in 1980, 1981 and 1982, and the policy stance of the UK authorities; and also the substantial productivity gains made by UK manufacturing industry from late 1980 onwards. None the less, even taking account of the extra gains in competitiveness made by early 1983, the index of relative export prices is still likely to be significantly above the level recorded in the period to 1979.

The changes in competitiveness have also been reflected on the import side, although the effects appear to be less dramatic. The official index of import competitiveness[1] increased by 18% between 1977 and the first quarter of 1981 (an adverse movement). An improvement of 3% occurred in the course of 1981 with further gains made at the end of 1982 and early in 1983.

[1] See 'Revised measures of UK trade competitiveness in manufactures', *CSO Economic Trends*, May 1980, HMSO.

GRAPH 1: Measures of United Kingdom export price competitiveness



Source: Commission services (lines 1 and 2); *CSO Economic Trends* (line 3).

Measuring competitiveness

Three measures of export price competitiveness feature in Graph 1; two are based upon relative export prices as prepared by the Commission departments, and one upon normalized relative unit labour costs, as calculated by the IMF.

The measures of competitiveness based upon export prices compare UK manufactured export prices (in US dollars) with a weighted average of export prices (also in US dollars) for two groups of competitor countries; those whose currencies are linked by the European Monetary System's exchange rate mechanism, and those of the OECD area. However, such measures have a number of limitations, the most important of which is that competitiveness is assessed in relation to the export prices of the UK's competitors, and the position within the competitor countries' domestic markets is not taken into account. To overcome this problem indexes are also constructed on the basis of unit labour costs in manufacturing industry which provide a comparison of total domestic production costs. As Graph 1 shows, an index prepared on this basis points to an even greater loss of competitiveness over the period concerned, suggesting that profit margins may have been reduced in order to maintain export market shares.

Changes in the structure of the balance of trade in goods and services

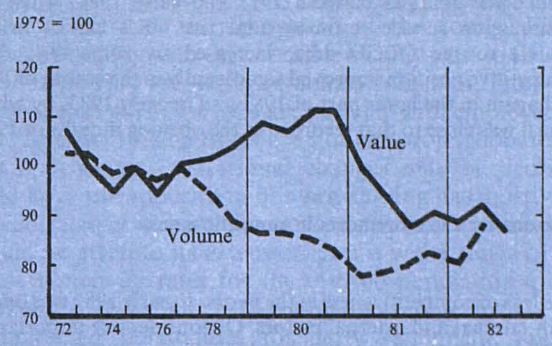
The loss of export and import price competitiveness, and the substantial change in the structure of UK production and trade due to the build-up of North Sea oil production, have had a significant impact upon the balance of trade. In particular, since 1980, the UK's trade in oil moved into surplus as North Sea oil output added to exports and reduced imports, and the surplus on manufactured goods (which in earlier years helped to offset the deficit in foods, basic materials, and fuels) declined. At the same time, substantial surpluses were maintained on trade in invisibles. These developments are illustrated in Table 1. The decline in the surplus relating to trade in finished manufactures has been very marked indeed and from a surplus of almost UKL 4 000 million in 1980 had virtually disappeared by the third quarter of 1982.

Impact of changes in competitiveness on the volume of UK exports and imports of manufactures

The marked fall in the trade surplus in manufactured goods given in Table 1 reflects both a weakening of the growth of manufactured exports, and increased import penetration.

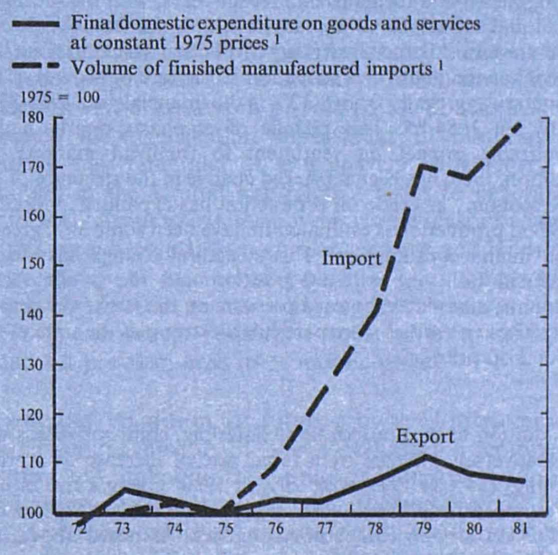
On the export side the UK's share of the *volume* of world trade in manufactures has been on a downward trend since the early 1970s (see Graph 2). This downward trend became even more marked over the period 1977 to early 1981 although a modest recovery appears to have occurred in 1982. This may partially reflect the gains in competitiveness made in 1981. For *values* the picture is somewhat different, with the UK's value share increasing marginally at least until 1980 and then declining. This

GRAPH 2: **Indicators of United Kingdom shares of world trade in exports of manufactures**



Source: National Institute Economic Review, November 1982 — NIESR.

GRAPH 3: **Recent trends in import penetration**



[1] Indexes with 1975 = 100.
Source: CSO Economic Trends (October 1982); *CSO Monthly Digest of Statistics* (October 1982).

suggests that over the earlier period when competitiveness was being lost, increases in the price of manufactured exports partly offset, at least initially, the adverse volume movements.

On the import side increased import penetration has been an important feature of the development of demand in the UK. In particular the growth in more recent years of the volume of imports of finished manufactures has been substantially greater than the growth of domestic demand (see Graph 3). However, this reflects both a deterioration in trade performance, and the increased integration of the UK domestic market into the world economy. A similar development can be observed for other countries as well.

The precise way in which changes in competitiveness affect the volume movements of manufactured imports and exports remains a matter of debate amongst economists and econometricians. It has frequently been argued that the performance of UK manufactured exports in recent years has been surprisingly good, despite the substantial loss of competitiveness, and that the loss of volume share of world trade has been less than expected. This points to substantial improvements in performance by UK exporters in response to the competitive pressures they have faced.

Recent studies of the impact of changes in competitiveness on export volumes, have focused upon the properties of the macro-economic models used by economic research institutes to forecast developments in the UK economy.[1] These differ widely and the longer-term competitiveness elasticities for exports of manufactures range from −0,27 in the case of the London Business School (LBS) model, to −0,69 as estimated for the model used by the National Institute of Economic and Social Research. The latter figure implies for example, that for each 1% loss of price competitiveness, manufactured export volumes will eventually decline by two thirds of 1%.

[1] See the discussion in 'Measures of competitiveness' in *Bank of England Quarterly Bulletin*, September 1982.

Estimates of the lags involved also vary substantially. Thus according to the macro-economic models used by the Bank of England and HM Treasury, changes in competitiveness are still affecting export volumes four years later, although the mean lag is estimated to be seven quarters. The LBS takes the view that the lags are much shorter, with the major impact of any change in competitiveness on export volumes occurring within the first year of the change. Clearly a judgment as to which of these views is correct is of particular importance in assessing the development of manufactured exports in the period ahead. On the basis of the Bank of England and Treasury view the adverse impact of the loss in competitiveness which occurred between 1979 and early 1981 will still have some influence on export volumes in 1983, although this effect will be offset by the improvements registered in 1981 and 1982.

Whereas much research supports the view that the effect of changes in competitiveness on export volumes is spread over several years, the general consensus is that changes in competitiveness have a fairly rapid impact on finished manufactured import volumes, with the full effects probably being felt within one year.

Table: A commodity analysis of the United Kingdom trade balance

(exports less imports; balance-of-payments basis; UKL '000 million)

	Food, beverages and tobacco	Basis materials	Fuels	Semi-manufactures	Finished manufactures	Total visible trade [1]	Balance of invisible earnings	Current account position
SITC R2	0+1	2+4	3	5+6	7+8			
1970	−1,3	−0,9	−0,5	0,5	2,1	—	0,8	0,8
1973	−2,0	−1,3	−0,9	0,3	1,2	−2,6	1,6	−1,0
1975	−2,7	−1,4	−3,1	0,5	3,2	−3,3	1,8	−1,5
1976	−3,0	−2,2	−4,0	1,0	3,9	−3,9	3,1	−0,9
1977	−3,3	−2,5	−2,8	1,6	4,3	−2,3	2,3	—
1978	−2,8	−2,2	−2,1	1,3	3,7	−1,5	2,6	1,0
1979	−3,1	−2,3	−1,1	0,7	2,0	−3,4	2,6	−0,9
1980	−2,4	−1,9	−0,2	1,6	3,9	1,2	1,7	2,9
1981	−2,4	−2,0	+2,7	1,5	3,2	3,0	3,1	6,1
1982 I	−0,7	−0,6	0,5	0,3	0,7	0,3	0,4	0,7
II	−0,7	−0,5	0,7	0,2	0,3	0,1	0,8	0,9
III	−0,7	−0,4	1,2	0,2	—	0,4	0,6	1,0

[1] Including 'miscellaneous' category.

Source: Monthly Review of External Trade Statistics, Department of Industry and Trade.

Regional analysis of trade in manufactured goods

One important feature of Graph 1 is the greater loss of export price competitiveness with regard to the countries participating in the EMS exchange rate mechanism, particularly in the period to early 1981, than with the total of industrialized countries included within the OECD grouping. This suggests, *prima facie,* that recent movements in the balance of trade in manufactured goods with Community countries, could be more adverse than for the world as a whole. Indeed whilst, for the first nine months of 1982, the United Kingdom registered a total trade surplus in manufactured goods (on a balance-of-payments basis) of UKL 1 500 million, this was associated with a deficit (estimated on the same basis) with the European Community of UKL 2 500 million.

However, an analysis of the trade balance alone does not give an adequate picture of trade in manufactures between the United Kingdom and the rest of the Community. It is useful to consider the various components of trade as well as developments over the longer term.

Recent analysis suggests that from many points of view the UK's trade performance in manufactures with the Community since the UK joined has been relatively satisfactory.[1] Thus between 1973 and 1980 UK trade in manufactured goods with other Community countries, as a share of total OECD trade, rose from 2,6% to 3,5%. This reflected a relatively substantial increase in the export share for non-durable consumer products (from 2,2% to 3,5%) combined with a more modest increase for investment goods (including motor vehicles) from 2,5% to 3,1%.

[1] See *European Economy* No 14, 'The Annual Economic Review 1982-83', Chapter 10.

On the import side developments were similar for non-durable goods with the UK market share increasing from 2,4% to 3,7%. With regard to investment and other durable goods and intermediate products, the UK's share of intra-EC imports rose somewhat faster than its share of exports, reflecting a trading weakness in particular sectors such as engineering and motor vehicles.

Concluding points

The following points emerge from this brief analysis:

(i) On the basis of most measures the United Kingdom lost competitiveness significantly between 1977 and 1980, but the position will have improved somewhat in 1981, 1982 and early 1983, both because of an easing of inflationary pressures, and a fall in the value of sterling.

(ii) The major part of the loss of competitiveness is likely to have worked through into export volumes for manufactures and indeed, in the period ahead, export volumes should benefit somewhat from the recent improvements in competitiveness.

(iii) The loss of competitiveness has been accompanied by a fall in the balance of trade in manufactured goods, offset by improvements elsewhere, particularly in trade in oil.

Budgetary systems and procedures for the central government budget in the Community Member States[1]

1 Mr Charles Depoortere of the Directorate-General for Economic and Financial Affairs is the principal author of this article.

Contents

1. Foreword 91

2. Some basic notions 91

3. Main features of the national budgetary systems 92

4. Comparative tables 94

5. Some concluding remarks 123

1. Foreword

In its communication of 1 July 1982 to the Council, on budget discipline and economic convergence, [1] the Commission once again stressed the importance of strict budgetary procedures and rigorous principles of financial management; it was convinced that the legal and administrative framework for financial policy determines its implementation and application in a number of ways.

There is no shortage of treatises on financial or budget law, describing the framework for financial policy in great detail for each country. But the first to realize how useful a comparative study of these institutional factors could be for the emerging European economic policy was the *Ragioneria Generale dello Stato,* a department at the Italian Ministry for the Treasury, which published a preliminary work in 1959 and an enlarged, updated version in 1969. [2] On the basis of this reference work and with the help of national budget departments, Commission services have produced and constantly updated succinct comparative tables to explain the main elements of budgetary systems and procedures; the points included were chosen because of their importance for controlling operations, and for the timing of the various stages in the preparation of decisions, and the execution of procedures. A set of 16 comparative tables is given below, incorporating the latest updating (1981). For the benefit of readers who are unfamiliar with the actual practice of budget management, the tables are preceded by a brief reminder of some basic notions and a review of the main features of budgetary systems in each country; some remarks will also be found on matters not covered by the tables but having a direct bearing on the points compared.

It should be stressed that the information relates only to budgetary law governing the central government budget; the rule applicable in each country to local authorities, public or semi-public agencies with specific responsibilities (e.g. social security funds) and public undertakings are usually considerably different.

2. Some basic notions

A budget fulfils two purposes: it is an *estimate* of the expenditure to be carried out by a public authority over a forthcoming period and of the financial resources (revenue) required to finance this expenditure; it is an *authorization* to carry out the expenditure and raise the revenue.

The executive authority draws up the estimate, i.e. the budget; authorization is granted by the legislative authority. On the revenue side, this authorization mainly covers the application of tax laws; the estimated amounts for proceeds are not binding. On the expenditure side, it is usual to grant authorization for a maximum amount known as an appropriation (for expenditure).

Estimates of revenue and appropriations refer to one of the successive stages in the cycle of revenue and expenditure:

(i) obligations: these are created on the expenditure side when the public authority undertakes a commitment or signs a contract with a third party; the appropriations to cover such obligations are usually known as commitment appropriations or long-term planning authorizations. On the revenue side, obligations are automatically generated by the occurrence of a taxable transaction (latent fiscal debt);

(ii) rights acquired or transactions: on the expenditure side, these are the result of third parties carrying out contractual obligations where the public authority has recognized, through discharge (discharge appropriations), the correctness, accuracy and legality of the claim. Rights acquired on the revenue side result from taxation or charge that transforms the latent debt into actual debt;

(iii) order to pay or demand for payment: on the expenditure side, this is the order to pay issued by the authority responsible for the expenditure (ordering appropriations). On the revenue side, it corresponds roughly to the sending of the tax demand ;[3]

(iv) payment of expenditure (payments) and actual collection of revenue (receipts).

Discharge appropriations, orders to pay and payments usually also cover the preceding stages as well, except in the case of split appropriations where specific authorizations are given for a specific stage of the cycle (e.g. a commitment appropriation and an order or a payment for the same item but for a different amount or a different period).

Appropriations are usually granted for one year. The strict application of the annual rule creates a system of 'annual budgets' where unused appropriations are annulled at the end of the 12th month. In fact the effects of appropriations may extend over a longer period, both with the system of the 'budget year', which leaves more time for one or more of the

[1] COM(82)422 final; see *European Economy* No 14, pp. 175-178.

[2] Ministero del Tesoro, Ragioneria Generale dello Stato, *Bilanci Statali in Europa (Struttura e disciplina giuridico – constituzionale: Paesi della CEE, Regno Unito e Svizzera),* Roma 1969, XXI + 435 pp.

[3] Numerous revenue items do not go through stages (ii) and (iii), either because they are payable when the debt arises (e.g. tax stamps) or because the taxpayer or a third party determines the amount of the tax (e.g. withholding tax), which is subsequently verified by the authorities.

later stages of the budget cycles or accounting transactions, and with the system of annual budgets where left-over appropriations are not annulled but carried over or transferred to the following year; it is also possible to adopt some mixture of budget year and carryover.

The scope of application of the budget differs fairly widely from one country to another; in general, however, the principles of completeness (all transactions are included) and of non-contraction (gross accounting with no offsetting between revenue and expenditure) are respected. The specification or allocation of expenditure and revenue also varies considerably, as some countries are prepared to accept broader authorizations than others.

3. Main features of the national budgetary systems

(a) *Belgium*

The central government budget consists of the ways and means budget (revenue budget with estimates of amounts expected to be collected during the year) and the departmental expenditure budgets, except for a few specific categories of expenditure (debt, pensions, budgetary provisions). General government expenditure is divided into four headings (current expenditure, capital expenditure, repayment of debt, operations out of earmarked funds); the first two are the core of the budget and the centre of attention. It is not always easy to detect changes in scope from the allocation of resources, since the removal of items from the budget and advance financing are not always clearly indicated. All expenditure must be authorized in advance, but under certain strictly defined conditions the Cabinet may decide on cash advances with retrospective authorization by Parliament. The Belgian budget has no reserves. Authorizations carry spending limits and cover both commitment and payment (undifferentiated appropriations) or one of the two (differentiated appropriations); differentiated appropriations can be carried forward automatically with no limits applied, while undifferentiated appropriations can be carried over to a limited extent only and must relate to expenditure committed in the budget year. The budget is deemed to have been tabled when the general budget statement and the ways and means budget have been tabled. The other bills on expenditure are generally submitted to Parliament later, so that the approval of all the budgets for one year can extend over a fairly long period running well into the budget year concerned; the entire set of bills, however, corresponds to the view given in the general budget statement.

(b) *Denmark*

The formal unity of the central government budget is respected; it is presented in three volumes (text; accounts and appropriations requested [Anmaerkninger I]; comments); subdivisions as a rule relate to revenue and expenditure by ministry, except for tax receipts and certain specific types of expenditure, which are grouped together. Changes in scope are usually clearly indicated. Appropriations in the strict sense of authorizations that carry limits apply only to salaries, purchases and investment and are determined in real terms (in principle prices and salaries at January t-1). Prices and wages increases are usually met from the budgetary reserve, which is also used for new expenditure arising during the year. For expenditure governed by 'organic' laws (over 50% of the total), the appropriations voted are merely estimates (open-ended appropriations). Appropriations cover either payment or commitment (purchases, investment); only the latter can be carried forward indefinitely by annual renewal. The Standing Parliamentary Finance Committee may sanction overspending, by means of a retrospective amending budget. The budget is usually voted before the start of the budget year and is part of a multiannual strategy. Estimates of revenue cover both resources that will actually be collected during the year and rights yet to be established.

(c) *Federal Republic of Germany*

The Federal Government budget consists of the revenue budget (Allgemeine Finanzverwaltung, forecasting revenue to be collected during the year) and expenditure budgets broken down by department or specific task (e.g. debt or pensions). As well as summarizing the budget, the overall plan also summarizes methods of financing and the plan for recourse to borrowing (Kreditfinanzierungsplan). The scope of the budget is kept under close surveillance. Spending appropriations involve ceilings and cover either payments in the budget year or commitments which will give rise to payment in subsequent years. The carrying-forward of appropriations for payment is subject to limits as regards their nature (investment, expenditure covered by specific receipts, expenditure relating to multiannual measures) and as regard duration (two years). There are no appropriations in the nature of a reserve; in the event of an overriding and unforeseeable necessity, additional appropriations may be authorized by the Minister for Finance. Budgets are frequently not voted before the start of the budget year. Borrowing is normally restricted to the funding of capital expenditure. The budget is part of a multiannual strategy. The *Länder* also apply budgetary systems that broadly match that of the Federal Government.

(d) *Greece*

The budget is made up of a series of drafts comprising revenue to be recorded during the year and expenditure by ministry; expenditure is divided into current and capital expenditure and includes a fairly large reserve fund. Appropriations, which always involve ceilings, relate to payments: unauthorized commitments are permitted; payment appropriations may not be carried forward. Supplementary appropriations or appropriations for unforeseen expenditure may be authorized by decree of the Minister for Finance. A vote on supplementary appropriations, covering over-spending not covered by the budget reserve or by amending budgets (taken at the same time as that on appropriations for the following year) is current practice under the law closing the account; the Minister for Finance in practice also authorizes over-spending from cash advances by the Bank of Greece. The system of draft budgets by ministry frequently means that votes on budgets spill over into the budget year concerned. As regards the scope of the budget, a tendency for items (e.g. trading accounts) to be re-included in the budget is emerging.

(e) *France*

The Finance Act, which includes an article on the overall balancing of the budget, covers the general central government budget, the annexed budgets and the special Treasury accounts, notably the special allocation accounts and the loan accounts. Changes in the scope of the budget by contraction or by removing items therefrom are possible and are clearly indicated. Estimates of revenue refer to resources to be collected during the year. Appropriations usually involve ceilings, but there is provision for indicative authorizations for certain types of expenditure (notably public debt); provisional appropriations also exist and can be overspent by recourse to a reserve fund included in the budget. Appropriations usually cover commitment and payment. For capital expenditure, long-term 'programme authorizations' are given separately, and allow commitment; such authorizations can be carried forward indefinitely. Appropriations for payments relating to capital operations can be carried forward by decree of the Minister for Finance; appropriations for payment relating to other expenditure cannot be carried forward unless they relate to chapters in the list in the Finance Act. This Act implies the voting of the whole budget, but also makes the distinction between 'supply services' (i.e. existing expenditure), which are voted as a block, and 'new measures', which are voted chapter by chapter. The Finance Act must be adopted within strict time-limits. In case of need, appropriations that carry ceilings can be overspent by advances authorized by decree.

(f) *Ireland*

The expenditure budget (covering all expenditure) and the revenue budget are submitted separately to Parliament, the first before the start of the budget year and the second normally in February. [1] A distinction is made in budgetary practice between expenditure to be authorized by Parliament and automatic expenditure arising from existing laws on the country's institutions. The Appropriation Bill, which is normally voted on in the December preceding the budget year, covers expenditure to be authorized both for appropriations relating to the forthcoming year and for supplementary appropriations for the year drawing to a close. The appropriations are for payment (pure management system) without carry-over. In the case of central fund expenditure (e.g. interest on national debt), the amounts shown in the budget are open-ended. Transfers of appropriations between subheadings are permitted. Automatic expenditure under extra-budgetary legislation does not require an annual vote but is subject to nominal ceilings which, once reached, must be readjusted by law. Although commitment appropriations do not exist under the system, programmes in their stead are established by agreement between the minister administering the programme in question and the Minister for Finance. The revenue budget refers to actual amounts to be collected during the year.

(g) *Italy*

The central government budget comprises a section relating to the approval of the summary of expenditure and revenue and a section reserved for the tables of appropriations and estimates by chapter (revenue; expenditure by ministry). The Budget Law also lays down the maximum amount of loans which may be issued, although temporary recourse to the central bank is possible. The budget provides for commitment authorizations and payment authorizations for all expenditure. Expenditure incurred but not paid is automatically carried forward by being entered in the special residuals account (*residui passivi*); the maintenance of residuals is limited to a period which varies according to the object of the expenditure, subject to special provisions. Where necessary, provisional twelfths may be authorized for a maximum of four months. For certain expenditure (salaries, debts), appropriations are open-ended; other overshooting compulsory expenditure may be financed from the reserve fund. The reserve also serves to meet new expenditure decided on during the year. The budget forms part of a multiannual strategy. Like estimates of expenditure, estimates of revenue refer either to rights recorded (budget on an accruals basis) or to amounts actually collected (budget on a cash basis).

[1] In 1983 this budget too was, for the first time, tabled before the beginning of the budget year.

(h) *Luxembourg*

Formal unity of the budget exists, although there is no vote on the budget as a whole. It is subdivided into ordinary and extraordinary revenue and expenditure and, within these, into departmental sections and special funds (e.g. investment). In principle revenue refers to rights recorded (accruals), but since 1980 large amounts (especially the proceeds of taxation) have been included in the form of expected collection. The scope of the budget is clearly circumscribed. Appropriations cover commitments and the later phases of the payment cycle, except for the funds, where the appropriations relate to payment authorizations. Appropriations not committed at the end of the budget year are cancelled and carry-overs, which are very rare, are confined to committed appropriations and are restricted to one year. In addition to appropriations which are open-ended (indicated in the budget text), the Luxembourg system relies on appropriations without distinction as to budget year and on 'residuals from previous budget years' in order to avoid carry-overs. However, open-ended appropriations may not be exceeded without the prior authorization of the Minister for Finance. Appropriations subject to limits may be exceeded without prior parliamentary authorization by means of a decree issued by the Cabinet. The system of supplementary budgets is not used.

(i) *The Netherlands*

The central government's budget comprises ministerial budgets (covering revenue and expenditure) and budget funds, which are tabled together, although there is no formal vote on the overall package. Revenue and appropriations, which always involve ceilings, relate to payments; expenditure commitments are authorized by the wording of the articles. Appropriations may not normally be carried forward, except where specially provided for in the Budget Law and by means of royal decree; authorized carry-overs are renewable. Appropriations may be exceeded only with Parliament's prior authorization. The adoption of budgets frequently spills over into the budget year concerned. The scope of the budget is clearly defined and the budget forms part of a multiannual strategy.

(j) *United Kingdom*

The central government's budget is made up mainly of the Consolidated Fund and the National Loans Fund, the first of which receives current revenue (tax and other, estimated as the actual amount to be collected) and covers the bulk of expenditure. Part of the expenditure from the Consolidated Fund, governed by permanent laws, and expenditure from the National Loans Fund do not require annual parliamentary authorization. Other expenditure from the Consolidated Fund is authorized annually (supply procedure). Details of the overall budget situation are given to Parliament twice a year (Financial Statement and Budget Report; Autumn Statement) without there being a vote on the whole. The appropriations voted relate to payments and always involve ceilings; however, there are two budget reserves to absorb overruns and new expenditure: the contingency reserve and the contingencies fund (expenditure from the latter being permitted only on the basis of advances repayable to this fund after voting of supplementary appropriations). Appropriations are not carried forward. Voting on appropriations normally takes place in July, i.e. after the beginning of the financial year; expenditure in the first few months is based on provisional appropriations (votes on account). In special cases, 'excess votes' permit appropriations to be exceeded subject to retroactive parliamentary approval. The budget forms part of a framework of multiannual forecasts.

4. Comparative tables

(a) *The budgetary system* (Tables 1 to 10)

This group of tables covers the main elements of present budgetary systems, especially the scope of authorizations for expenditure or assessments of revenue, and the way in which the Member States apply the principle of 'annuality'.

The tables show:	*Table*
A. Budgetary act(s)	
1. Scope of the estimate and authorization of expenditure	
(a) Scope of authorization	1
(b) Period covered	2
(c) Distinction, if any, between actual payments and commitments to pay (long-term planning authorizations)	3
2. Scope of revenue forecast	4
B. Effect on end of financial year (lapse of appropriations)	5
C. Carry-forward of appropriations	
1. Appropiations which can be carried forward	6
2. Procedures for carrying forward	7
3. Treatment of appropriations carried forward	8
4. Maximum period of carry-forward	9
D. Annual accounts (act closing the account)	10

A few remarks may be made about the comparisons in the tables.

While most countries base their revenue budgets on the amounts they expect to collect, there are differences between countries in the approach to expenditure appropriations, not solely because systems choose a different stage in the cycle, but also because commitment appropriations exist alongside other types of appropriations. There are several types of appropriations because only commitment authorizations enable the course of expenditure to be properly controlled if there are no 'organic' rules independent of the budget. The nature of budgetary authorizations is crucial in controlling expenditure, and authorizations other than commitment authorizations (e.g. appropriations for payment) have the disadvantage of being ambiguous in cases where autonomous 'organic' laws or regulations govern the course of expenditure and create pools of obligations resulting either from such laws or from previous contracts or commitments.

As far as autonomous legislation or contractual expenditure is concerned, such as those relating to debt servicing, some countries (Ireland and the United Kingdom) have gone all the way and exclude the relevant expenditure from the annual vote on budget appropriations. Other countries make provision, in certain cases, for indicative appropriations (France), or open-ended appropriations (Denmark,Luxembourg). None the less, in the majority of cases, double authorization remains: that implicitly given by the 'organic' law, and the annual budgetary authorization; obviously unless there is a change in the former, the latter in practice takes on the nature of estimates. This situation is often the cause of expenditure going off course and makes for great short-term rigidity in controlling budgets.

The same is true of pools of obligations created by previous commitments which had been carried over, in so far as any acceleration in implementing such obligations must be honoured by the budget. The situation for carry-overs is varied and complex. Disbursement or payment ceilings may be introduced, but they are usually without much effect; moreover, such limits cannot provide a lasting or long-term solution to the problem, which is fundamentally one of controlling commitments and timetables for implementation of expenditure. Control may be reinforced by multiannual financial forecasts, like those drawn up in the Federal Republic of Germany, Denmark, Italy, the Netherlands and the United Kingdom, updated each year in the first three countries and twice a year in the last two. The forecasts, which are normally indicative, have the great advantage of showing public expenditure for several years ahead assuming no change in legislation (though the 'reserves' of the type used in the United Kingdom also cover new expenditure). The only drawback to these forecasts, from the point of view of 'controlling' expenditure, is that the amounts entered in the programmes might be regarded as an established right and might subsequently hamper any efforts to re-deploy or cut expenditure. Long-term planning authorizations (or sometimes programme laws) and their accompanying timetables to some extent fulfil the role of multiannual forecasts in France.

Table 1

Scope of authorization

Belgium	(i) Undifferentiated appropriations and commitments to pay: commitment of expenditure. (ii) Payment appropriations: authorization of expenditure. (iii) Expenditure out of allocated receipts: order to pay.
Denmark	For transfers, estimated payments during the year. For purchase of goods and services, authorization to enter commitments during the fiscal year.
FR of Germany	Actual expenditure (payments) and commitments to expenditure.
Greece	Actual expenditure (order to pay and payment during the financial year).
France	Actual expenditure (order to pay); carrying-out of expenditure (order to pay).
Ireland	Actual expenditure during financial year (payment).
Italy	Commitment to expenditure (budget on an appropriations basis) and payment (cash budget).
Luxembourg	Commitment to expenditure — contractual liability (creation of debts due from the State) with the exception of special funds (order to pay).
The Netherlands	Carrying-out of expenditure (order to pay).
United Kingdom	Actual expenditure (payment) by central government on supply services.

Table 2

Period covered

Belgium	1 January - 31 December. Order to pay in the budget may extend to 28 February in the following year. Expenditure necessary to the continued functioning of public services may be entered into from 1 November in the preceding year up to a limit of one third of the appropriations for the corresponding expenditure (year n-1); deliveries may not be made nor services rendered before the start of the budgetary year.
Denmark	1 January - 31 December.
FR of Germany	1 January - 31 December. In principle, no supplementary period.
Greece	1 January - 31 December. Two-month supplementary period for expenditure contracted for up to 31 December.
France	1 January - 31 December. Additional period to 31 January for certain transactions contracted for before 31 December. Regulatory transactions — until last day of February. Anticipatory expenditure — from 1 November; in essence, expenditure on Armed Forces.
Ireland	1 January - 31 December.
Italy	1 January - 31 December.
Luxembourg	1 January - 31 December. Supplementary period for expenditure contracted for 1 January - 31 March of following year. Supplementary period for ordering and discharging expenditure — April of following year. Supplementary period for payment of expenditure — May of following year.
The Netherlands	1 January - 31 December.
United Kingdom	1 April - 31 March.

Table 3

Distinction, if any, between actual payment and commitment to pay

Belgium	The current expenditure budgets and capital expenditure budgets may include undifferentiated and differentiated appropriations (commitment appropriations and/or payment appropriations). Differentiated appropriations apply only in the case of expenditure on work or supplies where completion or delivery will take longer than 12 months. (i) Undifferentiated appropriations cover both commitments and payments. (ii) Commitment appropriations fix the amounts which can be underwritten during the financial year. (iii) Payment appropriations fix the amount which may be paid during the financial year to discharge the liabilities of the current as well as the previous year.
Denmark	See Table 1.
FR of Germany	Actual payments made during the financial year; commitments may extend to payment in future years.
Greece	Appropriations cover payments only.
France	For capital expenditure, distinction between: (i) commitment appropriations (long-term planning authorizations); (ii) payment appropriations, opened in the Finance Act for each year on the basis of forecast payments and taking account of any carry-forward (see Table 6).
Ireland	Only actual payments during the financial year are dealt with.
Italy	The Budget Act includes both actual payments and commitments to pay.
Luxembourg	The Budget Act makes no distinction between appropriations for commitment and payment.
The Netherlands	For all expenditure, distinction between: (i) commitment appropriations; (ii) payment appropriations, opened each year in the Budget Act on the basis of foreseeable disbursements and taking account of carry-overs.
United Kingdom	Only actual payments during financial year (cheques issued during year) are dealt with.

Table 4

Scope of revenue forecast

Belgium	Actual receipts during the budgetary year.
Denmark	Revenue estimates: for direct taxes — cash revenue, for other taxes — booked revenues.
FR of Germany	Revenue expected in financial year.
Greece	Revenue collected during the financial year, including a one-month supplementary period for receipts ascertained before 31 December.
France	Revenue collected during the financial year.
Ireland	Actual receipts during the financial year.
Italy	Revenue ascertained during the financial year (budget on an appropriations basis) and revenue collected during the financial year (cash budget).
Luxembourg	As a rule, rights to revenue acquired by the State from 1 January to 31 December, with additional period for collection: 1 January - 30 April of following year. In fact, major revenue items (especially tax revenue) are estimated and recorded as the proceeds collected from 1 January to 31 December.
The Netherlands	Revenue collected during the financial year.
United Kingdom	Receipts are considered separately from expenditure (Finance Bill) and refer to actual receipts by the public sector in the financial year to come and the effect of proposed changes in a full year (revenue collected).

Table 5

Effect on end of financial year (lapse of appropriations)

Belgium	If not carried forward, unused appropriations are cancelled.
Denmark	As a main rule, unused appropriations lapse at the end of the financial year; for exceptions see below (Table 6).
FR of Germany	Unless carried forward, unused appropriations lapse at the end of the year.
Greece	Unused appropriations cannot be carried forward.
France	If not carried forward, unused appropriations are cancelled.
Ireland	Unused appropriations lapse at the end of the year.
Italy	In general, expenditure not committed for is cancelled. Expenditure contracted for but not paid is transferred to the 'residual' account. In all cases, it is necessary to draw a distinction between the two kinds of commitment appropriation: (i) those intended to meet liabilities to third parties, and (ii) those which in the absence of such liabilities are maintained on the basis of specific acts. These facts are usually concerned with capital expenditure. However, special provisions have extended this possible course of action to certain current expenditure.
Luxembourg	Appropriations not charged to expenditure by 31 December are cancelled.
The Netherlands	If not carried forward, unused appropriations are cancelled.
United Kingdom	Unused appropriations lapse, except where a body has been given a 'grant in aid'.

Table 6

Appropriations which can be carried forward

Belgium	(i) Undifferentiated appropriations: the balances may be carried forward but solely in order to support the orders to pay with a view to discharging the commitments entered into during the financial year. (ii) Differentiated appropriations: the balances of commitment appropriations and payment appropriations may be carried forward with no restriction as to their use.
Denmark	Only appropriations for specified, well-defined purposes — mainly investment expenditure — may be carried forward, subject to the approval of the Ministry of Finance, and later inclusion in the supplementary appropriation bill.
FR of Germany	Only appropriations for investments and those 'tied' to resources allocated or expressly provided for in the Budget Act may be carried forward.
Greece	Appropriations cannot be carried forward.
France	Operating expenditure: a list of appropriations which may be carried forward appears in the Finance Act; for other headings, with the exception of staff expenditure, carry-forward is possible if the expenditure is contracted for within a limit of 10% of the allocation to the chapter in question. Capital expenditure: long-term planning authorization and payment appropriations may be carried forward without restriction.
Ireland	Appropriations cannot be carried foward; if necessary, they must be voted again in the following year.
Italy	No carry-forward in the true sense. Appropriations committed but not paid are included in the 'residual' account. Appropriations of the nature of capital expenditure and certain current expenditure are preserved in the budget by special acts for that purpose.
Luxembourg	No limitations, on condition that the appropriations are charged with expenditure contracted for and in the course of execution at the end of the financial year. In fact, the system of carry-forward has fallen into disuse and is usually replaced by 'remainders from previous years' or appropriations not allocated to a specific year.
The Netherlands	Restricted list in the Finance Bill.
United Kingdom	None.

Table 7

Procedures for carrying forward

Belgium	In practice, almost automatic. In theory, the King fixes the amount still needed to achieve the purpose for which the appropriation was allocated. The surplus is cancelled.
Denmark	See Table 6.
FR of Germany	The carry-forward of appropriations is the responsibility of the competent Federal Minister. Their use requires the agreement of the Federal Finance Minister. This agreement can only be given if other expenditure of an equal amount is not undertaken in the current year or if special appropriations have been made to cover additional expenditure.
Greece	None.
France	Operating and payment appropriations for capital expenditure are carried forward on a decree of the Minister for the Budget. Planning authorizations are carried forward automatically.
Ireland	Not applicable.
Italy	As a general rule, automatic.
Luxembourg	Verification of the balance of transactions by the Chamber of Accounts — prior authorization of the Minister for Finance. Inclusion in the next budget following the end of the financial year.
The Netherlands	In principle, exceptional procedure requiring both decree and assent of the Finance Minister.
United Kingdom	Not applicable.

Table 8

Treatment of appropriations carried forward

Belgium	(i) Undifferentiated appropriations carried forward to the following year are included in the corresponding appropriation in that year's budget; they are dealt with in a special way: they may only be used for expenditure arising out of obligations created during the year to which the original budget applied. (ii) Differentiated appropriations are added to the corresponding allocation in the following year's budget.
Denmark	See Table 6.
FR of Germany	They are included under the same heading.
Greece	Not applicable.
France	Included in appropriations of the next budget — not dealt with separately.
Ireland	Not applicable.
Italy	Inclusion in the 'residual' account, which is dealt with separately from the budget on an appropriations basis and the cash budget.
Luxembourg	Payment of expenditure contracted after the final closure of the financial year, but orders to pay relating to the appropriations carried forward regularized — included in a special section: 'carry-forward from previous year'.
The Netherlands	Appropriations carried forward are dealt with separately. They appear in the cash position when payments are made.
United Kingdom	Not applicable.

Table 9

Maximum period of carry-forward

Belgium	(i) Undifferentiated appropriations — one year. (ii) Differentiated appropriations — no limit.
Denmark	None, but subject to annual approval.
FR of Germany	In principle, two years.
Greece	Not applicable.
France	Renewable each year.
Ireland	Not applicable.
Italy	In general, two years for the 'residual' account as relating to current expenditure (three years for expenditure relating to works, supplies and services). The capital expenditure items together with certain current expenditure which do not represent commitments to third parties may be carried forward for five years.
Luxembourg	One year.
The Netherlands	Renewable each year without limitation.
United Kingdom	Not applicable.

Table 10

Annual accounts (Act closing the account)

Belgium	The budget account is presented in tables having the same subdivisions as the budget. For receipts as well as expenditure, it covers all transactions charged in the budgetary year, including those involving a carry-forward. Details are given of appropriations carried forward to the following year as well as those which are cancelled.
Denmark	Covers the income and expenditure for the year.
FR of Germany	Covers the whole of revenue and expenditure, including State property and national debt.
Greece	Covers the out-turn for the year, in income and expenditure, and contains approval of spending in excess of appropriations, if any.
France	Covers the outcome of the financial year, i.e. the execution of the Finance Act on the basis of payments.
Ireland	The accounts of the Exchequer receipts and expenditure cover the whole of the receipts and payments for the financial year. An appropriation account is prepared at the end of the year showing the actual and estimated expenditure.
Italy	Covers the total activities of the financial year, i.e. both the budget and the 'residual' account.
Luxembourg	Rights acquired by the State and its creditors during the year for which the budget applies (financial year method), taking into account the remainder (revenue and expenditure) as well as any carry-forward — special fund — expenditure ordered to be made.
The Netherlands	Covers the outcome of the financial year.
United Kingdom	Expenditure is dealt with in the appropriation accounts. The Treasury submits annual accounts for the Consolidated Fund and the National Loans Fund. Receipts are covered by accounts published by the individual collecting departments.

(b) *Flexibility of the annual authorization of expenditure as to the total of expenditure* (Tables 11 to 13)

The second group of tables deals with techniques for adjusting expenditure in the course of the year. In most of the countries, estimates for revenue may also be adjusted using supplementary budget measures or amending budgets.

In some countries, flexible authorizations (open-ended appropriations: see Table 11) are granted. Other possibilities, summarized in Tables 12 and 13, are:

(i) procedures for increasing initial estimates (Table 12 (a) and 12 (b));

(ii) procedures for limiting the amount or changing the rate of expenditure (Table 13).

In most countries, provisional appropriations may be made if the budget is not approved by the beginning of the calendar or financial year; this is automatic in the Federal Republic of Germany in the case of compulsory expenditure and in the Netherlands for a quarter or a half of the proposed appropriations. In fact, the normal procedures make provisional appropriations exceptional in Denmark, Germany, France, Greece, Ireland, Italy and Luxembourg. In Belgium, the Netherlands and the United Kingdom, frequent use is made of provisional twelfths: in Belgium and the Netherlands, owing to the need to vote on each departmental budget or chapter separately; in the United Kingdom, because the provisional appropriations are, as it were, the first phase of the procedure for approving the budget. Generally speaking, provisional appropriations cover only expenditure which has already been approved previously.

Where recourse to provisional appropriations is exceptional, it is usually motivated by a government crisis which delays the normal procedures. Under these circumstances, provisional appropriations are made automatically in Germany and the Netherlands; in the other countries, a law or special vote is required.

All the Member States monitor the budget's implementation fairly regularly. In some cases (Germany, France, Italy, the Netherlands and the United Kingdom), amending budgets are tabled when the need arises; in Italy at least one supplementary budget must be introduced; in Belgium and Ireland, it is customary for an amending budget to be introduced only when the budget proposals for the following year are submitted; in Denmark, supplementary authorizations are submitted to Parliament's Standing Finance Committee, but are not the subject of a supplementary budget until after the end of the budget year; in Luxembourg, authorization for expenditure which may be required is given by special laws; in Greece, where amending budgets are in principle required if the reserve fund is insufficient, this principle is no longer applied and overruns are regularized under the law closing the account.

No Member State, however, makes any direct reference in its budgetary legislation to any rule that operations as a whole, or at any rate current account operations, must be in equilibrium; indeed, such rules would severely restrict freedom to adjust expenditure budgets without an offsetting on the revenue side. In Germany, there is an indirect rule restricting disequilibrium, deriving from the limits imposed on borrowing to fund capital spending (barring exceptional circumstances due to the economic situation) and the authorization of borrowing limits by Parliament. In a number of countries, there is or was a tradition that there should be overall equilibrium (e.g. France) or current account equilibrium (Belgium, Greece, Luxembourg), though such traditions have during recent years been overtaken by events. At present, use is most often made of targets for the overall net deficit, [1] although in several countries (Belgium, Greece, Ireland and Italy in particular) this means significant disequilibria on current operations, and deficits are often aggravated by overruns during the year.

The need to make use of amending budgets is partly dependent on the flexibility of the budgets in terms of the scope for spending without prior parliamentary authorization, and in terms of the provision of reserve funds within the budget. Overruns that are not subject to prior authorization may occur either, as in France and Luxembourg, on the basis of indicative or open-ended appropriations, or, as in the case of Denmark, Ireland and the United Kingdom, through expenditure governed by 'organic' laws. In some countries, overspending subject to subsequent approval by parliament is possible, as in the case of Belgium (*avances de trésorerie*), France (*décrets d'avances*), Greece and the United Kingdom (calls on the contingencies fund, to be repaid subsequently), and in Luxembourg, where such advances are regularized by offsetting against appropriations carried over from previous years, or appropriations not allocated to a specific year in the following budget.

Reserve funds are used regularly and on a large scale in Denmark, Greece, Italy and the United Kingdom. They are used to a lesser extent in France (provisional appropriations) and in Luxembourg (reserve for amendments in the draft budget). In Denmark, use of the reserve fund, which is constantly adjusted to requirements, is bound up with the specific nature of the budget (see above). In Greece, the reserve fund is rarely sufficient to cover spending in excess of appropriations for actions expressly provided for in the budget and unforeseen items. In Italy, compulsory expenditure may be increased through use of the reserve funds. In the United Kingdom, the contingency fund is intended to absorb overruns or extra spending resulting from new measures; the size of this fund is such that amending budgets have to be used only in exceptional circumstances; this practice has the advantage of determining the probable maximum level of expenditure with greater certainty from the outset, but requires great budgetary discipline within government to avoid the rash use of the reserve.

[1] Or 'net borrowing requirement', i.e. the balance on expenditure and revenue, including financial operations: loans, advances and equity purchases.

Table 11

Existence of open-ended appropriations

(a) Capable of being met from reserves

(b) Others

Belgium	None.
Denmark	A distinction is made between: (i) expenditure governed by budget ceilings, mainly purchase of goods and services (including salaries) for current and investment purposes, and (ii) expenditure governed by legislation outside the budget, especially transfers to households and local authorities. Legislation expenditure covers approximately 55% of the budget, while expenditure controlled by budget ceilings covers a good 30%. As regards A, the appropriations are fixed in real terms, but generally subject to adjustment for price and wage increases. As regards B, expenditure is open-ended both in real terms and as regards changes in prices and wages. The expenditure included in the budget thus represents estimates. (a) Price and wage increases can be covered by drawing on the reserve for this purpose, which is currently being revised. (b) None.
FR of Germany	None.
Greece	Increases in appropriations listed in the budget, and extraordinary and emergency expenditure not provided for in the budget, are charged to a reserve.
France	(a) Provisional appropriations (list given in the Finance Act) may be included by recourse to a general appropriation for contingent expenditure. (b) Indicative appropriations: (i) by nature (public debt and pensions, costs of judiciary and civil restitution, repayment and redemptions), (ii) for certain budgetary chapters determined by the Finance Law.
Ireland	(a) None. (b) Specific expenditure provided for by statute not subject to vote by the Dáil, i.e. charges on the central fund (e.g. service of public debt, judicial salaries, etc.).
Italy	(a) Obligatory expenditure which the administration is bound to by virtue of the existing juridical system or judicial decisions, and regulatory expenditure (concerned with determination of the *assiette* or base and recovery of revenue) — list given in the budget — may all be increased by recourse to reserve funds. (b) Fixed expenditure (salaries, pensions, debt interest).
Luxembourg	(a) Appropriations for salaries, wages and pensions if an appropriation common to all departments is provided for in the budget of the Ministry of Public Works. (b) Appropriations for salaries, wages and pensions if no common budget is provided. Appropriations under the heading 'unlimited'.
The Netherlands	None.
United Kingdom	None.

Table 12(a)

Procedures for increasing initial estimate

(a) Increase not requiring authorization

(b) Increases by way of statutory powers not requiring parliamentary approval

Belgium	(a)	None.
	(b)	In principle, none. Under special clauses of the budgetary law, certain global provisions are included in a budget in order to be broken down subsequently between different articles of one or more budgets (e.g. provision for adjusting salary appropriations to the index, provision for social planning expenditure as yet undetermined when the budget is put together).
Denmark	(a)	No specific authorization is needed for (b) (see Table 11), but increases are subsequently registered on the supplementary appropriation bill.
	(b)	None.
FR of Germany	(a)	None.
	(b)	Extraordinary and unplanned expenditure requires the agreement of the Federal Finance Minister. This agreement will only be given in the case of overriding and unforeseen necessity (§ 112 of the fundamental law).
Greece	(a)	None.
	(b)	Supplementary appropriations, or appropriations for extraordinary expenditure not provided for in the budget, by order of the Minister for Finance.
France	(a)	Expenditure falling within indicative appropriations.
	(b)	Decree of Minister for the Budget to 'top up' the provisional appropriations within the limit. Decree increasing limited appropriations by recourse to a general appropriation for unforeseen expenditure. Fund in aid: creation of supplementary appropriations offset by specifically allocated resources (decree of Minister for the Budget).
Ireland	(a)	None.
	(b)	Funds may be transferred between the subheadings of a specific vote. This requires approval of the Ministry of Finance. No other adjustment permitted.
Italy	(a)	None.
	(b)	By presidential decree — expenditure within § 1 of Article 41 of the Law of accountability (staff, interest, etc.). By decree of the Treasury Minister — expenditure within § 2 of Article 41 of the Law of accountability (repayments, deposits, etc.). By decree of the Treasury Minister — expenditure which had already been contracted, but had been cancelled in the meantime, may be contracted again.
Luxembourg	(a)	None.
	(b)	All unlimited appropriations may only be exceeded with the prior authority of the Minister for Finance.
The Netherlands	(a)	None.
	(b)	None.
United Kingdom	(a)	None.
	(b)	Funds available from contingencies fund. This is a temporary operation and requires a supplementary estimate (see Table 13 (a)). The advance will be repaid out of the supplementary appropriation.

Table 12(b)

(c) Increases requiring parliamentary approval
(d) Amendment of authorization act prior to ratification
(e) Act closing the account

Belgium	(c)	In cases of urgency arising out of exceptional and unforeseen circumstances, the Council of Ministers can authorize either increased or new appropriations. This expenditure will be periodically made the subject of regularization acts.
	(d)	All other amendments of initial appropriations or entry of new appropriations involves a vote on supplementary appropriations.
	(e)	Supplementary appropriations provided for in the accounts law.
Denmark	(c)	New and altered activities during the fiscal year as regards category A require supplementary appropriations authorized by the Standing Parliamentary Finance Committee. These will then be incorporated in the supplementary appropriation bill which is placed before the Folketing after the end of the fiscal year.
	(d)	During the period from mid-August, when the draft budget is presented to the Folketing, until mid-December, when the budget is approved, amendments may be submitted to the Standing Parliamentary Finance Committee.
	(e)	None.
FR of Germany	(c)	Supplementary expenditure in time of recession — at the discretion of the government with parliamentary approval (economic policy programme under the law to promote stability and growth of the economy).
	(d)	By amending act in so far as the above measures do not apply.
	(e)	None.
Greece	(c)	None.
	(d)	Recourse to new laws necessary when the reserve fund is exhausted.
	(e)	Approval of changes in appropriations which have taken place during the year by the act closing the account.
France	(c)	Advances by government decree (in urgent cases only): (i) for provisional appropriation for additional expenditure exhausted (ratified in following Finance Act); (ii) for limited appropriations: in cases of urgency and provided the Treasury balance is not affected (compensatory cancellation of appropriations or increase in revenue) and with ratification in the following Finance Act; or if 'overriding national interest' is concerned, the Treasury balance constraint is not adhered to but a draft Finance Act ratifying these appropriations is placed before Parliament immediately or at the opening of the next session.
	(d)	All other increases in the original estimates require previous parliamentary authority (rectifying Finance Act).
	(e)	The act closing the account (see Table 10) recapitulates the various transactions which have taken place during the year, including any increases in indicative appropriations.
Ireland	(c)	Excesses on votes require parliamentary approval by way of supplementary estimates.
	(d)	The Appropriation Bill, taken towards the end of the financial year, covers both the original and supplementary estimates.
	(e)	None.
Italy	(c)	By presidential decree, unforeseen expenditure may be met out of reserve funds.
	(d)	All other increases in the original estimates require previous parliamentary authorization.
	(e)	An act is obligatory if adjustments are prior to 30 June; it is optional if they take place between 30 June and 30 October.

Table 12(b) *(continued)*

(c) Increases requiring parliamentary approval
(d) Amendment of authorization act prior to ratification
(e) Act closing the account

Luxembourg	(c) None. However, in case of lack or insufficiency of appropriations, and only in extreme urgency, provisional orders to pay may be issued following the advice of the Chamber of Accounts, the authorization of the Finance Minister, and a decree moved by the Cabinet. These orders are regularized in the remainders from previous years or appropriations not allocated to a specific year in the following budget. (d) In all other cases, the budget appropriations may not be increased or new appropriations set up without special acts (special appropriations). (e) None.
The Netherlands	(c) Supplementary budget. (d) Supplementary budget. (e) None.
United Kingdom	(c) All needs exceeding the approved appropriations for a particular purpose must be approved by way of supplementary estimates. Supplementary estimates are normally submitted in July, December and February. (d) Revised estimates may be submitted after 1 April but before Parliament votes on the original estimate in — at the latest — early August. (e) None.

Table 13

Procedures for controlling the limit or changing the rate of expenditure
(a) Reduction of expenditure
(b) Changing the rate of expenditure
(c) Fund for counter-cyclical action

Belgium	(a) Since the appropriation authorizes expenditure, but does not make it obligatory, each minister (or the Cabinet, where general measures are concerned), may decide to block particular appropriations. (b) (i) Current expenditure The use of appropriations has sometimes been limited by ministerial circular (pursuant to Cabinet decisions), e.g. at the end of the year to prevent balances from being used up as a matter of routine; also during the year, if the need to hold down certain types of expenditure is foreseen (prospect of a supplementary budget to reduce expenditure or need to compensate for extra expenditure which proves to be unavoidable); or in the event of a government crisis to prevent outgoing ministers from exhausting appropriations prematurely; except for the limits imposed at the end of the year, the special measures are generally incorporated into the supplementary amending budget. (ii) Capital expenditure Changing the rate of expenditure is part of current practice for capital expenditure. Irrespective of the appropriations, this expenditure is the subject of annual (commitment) programmes, released by (three or four-month) instalments in line with the economic and financial situation. Part of the annual investment programmes can sometimes be frozen from the start of the year. At other times, however, provision is made for an 'economic contingency instalment' (over and above the annual programme), which is released in special circumstances. (c) None.
Denmark	In conformity with the law, the government may limit expenditure under category A and regulate the rhythm of such expenditure.
FR of Germany	(a) The budget may be 'frozen' by the Minister for Finance if the state of revenue and expenditure warrants it. Government authorization to the Minister for Finance to restrain expenditure for cyclical purposes. (b) None. (c) No Fund, but counter-cyclical action is possible via the law to promote stability and growth of the economy (e.g. economic contingency reserve with the Bundesbank; supplementary appropriations).
Greece	(a) The Minister for Finance each quarter fixes the percentage of appropriations to which effect is to be given: when necessary he may decide not to allocate appropriations in full. He may also lower the payment limits which he fixes each month. (b) Acting on a reasoned proposal by the ministers concerned, the Minister for Finance may speed up or slow down the rate of expenditure under the powers indicated under (a). (c) None.
France	(a) Appropriations may be cancelled during the year, either by a rectifying Finance Act or by a decree of the Minister for Finance with the agreement of the government. (b) None. (c) The original Finance Act may, if required, have an appropriations reserve which may only be used after a government decision following consultation with the Finance Committee.
Ireland	(a) The government can control the rate of expenditure freely, to take account of the overall economic situation. However, because of the inflexible nature of much of government expenditure (e.g. pay, debt service and social welfare outlay) the scope for effecting reductions is limited. (b) The timing of certain items of expenditure may be slowed down but, as with (a), the room for manoeuvre is not considerable. (c) None.

Table 13 *(continued)*

Procedures for controlling the limit or changing the rate of expenditure
(a) Reduction of expenditure
(b) Changing the rate of expenditure
(c) Fund for counter-cyclical action

Italy	(a)	Since the appropriation authorizes expenditure, but does not make it obligatory, each minister or the Cabinet, where general measures are concerned, may decide to block particular appropriations.
	(b)	None.
	(c)	None.
Luxembourg	(a)	Budget appropriations voted by the Chamber of Deputies represent maximum amounts. On proposal from the Minister for Finance the Cabinet may decide not to use appropriations in whole or in part.
	(b)	Similarly, on proposal from the Minister for Finance the Cabinet may decide to regulate certain categories of expenditure, especially investment, during the financial year.
	(c)	None.
The Netherlands	(a)	The budget estimates of expenditure represent maxima. The Cabinet may therefore, on the proposal of the Minister for Finance, not use the whole of the budget appropriations.
	(b)	The Cabinet can decide to slow down the rate of certain expenditure. The expenditure may be accelerated during the year, or carried forward to the following budget, or cancelled.
	(c)	None.
United Kingdom	(a)	The government can reduce the rate of expenditure to take account of the overall economic situation.
	(b)	The government may adjust the timing of expenditure within the financial year.
	(c)	None.

(c) *The budgetary timetable and voting procedures*

Budgetary timetables appear in Tables 14/0 to 14/9. On the whole, the different countries' timetables have grown more closely similar over the years (except that of the United Kingdom), in particular for the preparatory stages of the budget.

Parliamentary voting procedures, on the other hand (see Tables 15(a) and 15(b)) are strongly marked by the parliamentary traditions of the invidual Member States. One specific aspect, that of amendments (see Table 16), is vital to budgetary control. Parliaments in France, Ireland and the United Kingdom do not have the right to amend budgets so as to increase expenditure; in Italy, this right is limited. In the other countries, parliaments do have this right, though in practice it is used only to a limited extent. In Germany the amendments must be accepted by the government. The initiative of whether or not to fund the amendments is more often than not left to the government, except in Luxembourg where a special reserve designed for the purpose is incorporated in the draft budget.

In addition to such amendments, new laws entailing expenditure may be introduced during the year; in most cases it is left to the government to decide how they should be financed; appropriations allowing the expenditure to be carried out are granted either by law (Luxembourg), or through amending budgets, or are drawn from the reserves (Italy, United Kingdom). In so far as expenditure covers only part of the current year, and sometimes a very short part, the full budgetary effect of the changes is not always clearly apparent except in countries where multiannual forecasts are updated regularly, or at least periodically, and show them up clearly.

Table 14

Budgetary timetable

Belgium	Year t-1	
	I-II	Fixing of the working assumptions by the Ministry of the Budget for the budget of the following year. Request by the Minister for the Budget to the other ministers for their proposals.
	III-IV	Preparation of expenditure proposals by departments and examination by the Inspector of Finance. Preparation by the Minister for Finance of the estimates of receipts.
	V	Examination of the expenditure proposals by the Budget Administration and by committees of responsible departments.
	VII	Preparation of the final estimates with respect to receipts. Final decisions in the Budget Committee. Perhaps a second review and final decision on any disputes by the government.
	VIII	Preparation of general presentation of the budget (summary of the government's economic, financial and budgetary policies).
	IX	Tabling of the draft budget in Parliament (before the end of September). Except for the ways and means and debt, estimates of which are always submitted straight away to the Chamber of Representatives, the estimates are submitted immediately to one or other of the Chambers by rotation.
	X	Opening of the budgetary debate (second Tuesday of October). Examination by parliamentary committee, and then by Parliament as a whole, of the budgets of the different ministerial departments.
	XI-XII	No time-limit on the parliamentary procedure, but in principle the ways and means budget (= receipts) is passed before 31 December. A Finance Act authorizes tax collection in default of this. A Provisional Authorization Act permits expenditure on budgets which have not been passed.

Table 14(a)

Denmark	Year t-2	The procedure in January-February in t-1 outlined below (decisions on expenditure policy for the following four years) is in principle predetermined by decisions in years t-2, t-3 and t-4.
	Year t-1	
	I-II	The government makes decisions on the expenditure policy for the four following years in fixed prices. The decision is formalized in budget 'ceilings' for appropriation items subject to direct expenditure control (January-February). The Department of the Budget sends ministries a circular giving budget ceilings and personnel maxima (end of February).
	IV-VI	Estimates are prepared by the government for total expenditure in current prices and for revenues. This includes (besides the 'ceilings') preliminary estimates concerning the various transfer payments according to laws and estimates for the reserve covering price and wage increases and the reserves for new appropriations and laws (April-May). Individual ministries submit their budget proposals to the Department of the Budget (beginning of May).
	VII-IX	The government decides on the draft budget to be submitted to the Folketing. The draft budget is submitted to the Folketing, which refers it to the Standing Parliamentary Finance Committee for preparation of a report for the Folketing (middle of August).
	X	The proposed budget is re-presented to the Folketing without changes compared to the August submission. First reading of the budget (beginning of October). The Folketing decides on the levy rate for State tax.
	XI	Second reading of the budget (beginning of November).
	XII	Third and final reading of the budget. Once the royal assent is obtained, the approved budget is published in the official law bulletin (end of December).

Table 14(b)

FR of Germany	Year t-2	Instruction from Minister for Finance to prepare estimates and on the contributions to the budget programme.
	Year t-1	
	I-II	Preparation of estimates and submission of the departmental estimates to the Federal Minister for Finance.
	III	Budget discussions. Preparation of draft budget by the Minister for Finance.
	V	First option of the Cabinet on the general outline of the budget.
	VI	Discussion between the Minister for Finance and departments.
	VII	Adoption of the draft Finance Bill and the budget by the government.
	IX	Submission of draft Finance Bill and budget to both Houses; opening of budget debate in the Bundestag by the Minister for Finance. First reading in the Bundestag.
	X	Bundesrat first reading (six-week time-limit).
	XI-XII	Second and third reading by the Bundestag; second round in the Bundesrat. (No formal time-limit within parliamentary procedure; the budget bill should be adopted and published before the relevant budget year.)

Table 14(c)

Greece	Year t-1	
	V-VI	Instruction from Minister for Finance to ministerial departments to prepare expenditure estimates.
	VI-VII	Preparation of expenditure estimates by ministerial departments. Preliminary revenue estimate by Ministry of Finance.
	VIII	Departmental expenditure estimates forwarded to the central government general accounts department.
	IX-X	Examination of departmental expenditure estimates and exchange of views between the Ministry of Finance and other ministries on their proposals. Contentious issues are decided in Cabinet.
	XI	Finalization of draft budget. Introductory statement drafted by the Ministry of Finance and draft budget presented to Parliament by the Minister.
	XII	Examination of the draft budget by a special parliamentary committee. Drafting of reports. Discussion and vote by Parliament.

Table 14(d)

France	Year t-1		
	I-II	Preparatory work within the Department for the Budget. Minister briefed (end of January). Prime Minister provides guidance on the preparation of the budget (letter of guidance).	
	III-IV	Examination of the proposals of the ministerial departments in bilateral meetings held at the Department for the Budget. Discussion of each department's budget on an 'unchanged policies' basis. Taking stock of additional demands. Report sent to the government.	
	V	Restricted Cabinet meeting. Transmission to each department of a 'letter of limit', indicating the amount of the budget on 'unchanged policies' and the envisaged new measures.	
	VI	Interdepartmental meetings to discuss technical aspects of the new measures.	
	VII	Revision to working assumptions on the economy. Final decision on expenditure.	
	VIII	Final estimate of receipts and approval of contingency plans for fiscal measures.	
	IX	Approval by the whole Cabinet of the draft budget (Finance Bill).	
	X	Tabling of draft budget in Parliament (no later than the first Tuesday of October).	
	XI-XII	Examination and vote on the Finance Bill by both Houses of Parliament (no later than 70 days after the tabling of the Bill).	

Table 14(e)

Ireland	Year t-2	Forecast estimates of expenditure prepared by departments.
	Year t-1	
	IV-VI	Receipt of detailed estimates of both expenditure and revenue; preliminary consideration by the Department of Finance.
	VII-IX	Consideration of expenditure proposals (capital and non-capital) and revenue and resource estimates by the Minister for Finance; review of overall situation in the light of the latest macro-economic projections.
	X-XII	Discussion by the government of broad outlines of the budget and consideration of allocations to departments. Examination by the government of details of expenditure proposals. Government approval of expenditure estimates to be presented to Parliament.
	Year t	
	I-II	Government consideration of budget concessions and tax changes. Presentation of budget.
	III-IV	First stages of Finance Bill giving statutory effect to changes in the budget and other tax reforms.
	V-VI	Enactment of Finance Bill.

Table 14(f)

Italy	Year t-1		
		IV	The Treasury requests the other ministerial departments to draw up the expenditure proposals.
		V	Departmental expenditure proposals sent to the Treasury.
		VI	Consultations between the Treasury and the other departments.
		VII	The Minister for the Treasury sends the Minister for the Budget the working assumptions for the budget. The Ministry for the Budget is sent the activity forecasts of the other ministerial departments. The Minister for the Treasury sends the broad outlines of the draft annual and multiannual budgets to the Interdepartmental Committee for Economic Planning, the Regions and the Interregional Committee.
		VIII	The Interregional Committee's opinion on the draft annual and multiannual budgets.
		IX	The Interdepartmental Committee for Economic Planning approves the economic forecast report and the broad outlines of the annual and multiannual budgets. Draft economic report, Finance Bill and annual and multiannual budget proposals presented to Parliament (before the end of September).
		X	The Ministers for the Budget and for the Treasury open the parliamentary debate (first working day of October).
		XI-XII	There is no time-limit to the parliamentary procedure.

Table 14(g)

Luxembourg	Year t-1	
	I	Preparatory work within the Ministry of Finance.
	II	Political and technical instructions sent out by the Minister for Finance to the departments for the purpose of drawing up budgetary proposals (mid-February).
	III	Preparation of the budgetary proposals by the departments. Sent to the Ministry of Finance (before the end of March).
	V	Preparatory examination of the budgetary proposals by the Ministry of Finance (Inspection générale des Finances). Joint examination by the departmental delegates.
	VII	Final decision on the draft budget by the Cabinet, perhaps after an interdepartmental meeting.
	VIII	Drafting of the Budget Statement.
	IX	The draft budget is sent to the Council of State and to the Professional Chambers (consultative bodies). The draft budget is tabled in the Chamber of Deputies (first week in September). Examination of the draft budget by the Council of State and the Professional Chambers and also by the Chamber of Deputies' Finance and Budget Committee.
	XI	Full parliamentary debate on the draft budget opened by the Minister for Finance. Presentation of the Finance and Budget Committee report. Tabling of government amendments (end of November).
	XII	Final vote by the Chamber of Deputies (end of December).

Table 14(h)

The Netherlands	Year t-2	Guidelines of a primarily technical nature, from the Minister for Finance concerning the drawing-up of the expenditure proposals of ministerial departments.
	Year t-1	
	I-II	Request of the Minister for Finance to take into account in their proposals the departments' previous agreement on the multiannual forecasts. Possibility of modifications to these forecasts being proposed to the Cabinet.
	III	Expenditure proposals drawn up by departments.
	IV	Departmental expenditure proposals sent to the Minister for Finance (before 1 May).
	V-VI	Expenditure proposals examined by the Ministry of Finance. Consultations between the Ministry of Finance and the departments on these proposals and the new multiannual forecasts. Consultations between the Minister for Finance and other ministers.
	VII	The Minister for Finance submits the disputed points to the Cabinet. The departments draw up the final proposals on the basis of the Cabinet decisions. The Cabinet discusses and approves the revenue forecast.
	VIII	The Minister for Finance sends a report to the Queen on the draft budget. The draft budget is sent to the Council of State for an opinion (to be rendered before the end of August). Final approval of the draft budget by the Cabinet.
	IX	The Cabinet discusses and approves the financial report (Miljeonennota), containing the new multiannual forecasts. New report to the Queen following the opinion of the Council of State. The draft budget and financial report are tabled in the second Chamber of Parliament.
	XI-XII	There is no time-limit to the parliamentary procedure.

Table 14(i)

United Kingdom	Year t-1		
		IV-VI	Departments submit public expenditure projections to the Treasury. These include most expenditure covered by supply estimates and other expenditure by central government, local authorities and capital expenditure by public corporations. Examination of the projections.
		VII-X	Public expenditure projections submitted to ministers for consideration. The Treasury asks departments to submit estimates of central government expenditure for the financial year starting the following April. Decisions taken on the total of public expenditure.
		XII	Discussion between the Treasury and departments on the estimates (starting in December, continuation into January).
	Year t		
		I-II	Taxation policy considered in the Treasury and in the departments responsible for tax collection. Short-term economic forecasts are prepared for these discussions.
		III	Publication of white paper on public expenditure, which comprises departmental expenditure estimates for the next three years. Defence estimates published. Civil estimates published.
		IV-VII	Budget proposals outlined to Parliament by the Chancellor of the Exchequer. Publication of the Financial Statement and Budget Report. First stages of the Finance Bill. Final stages of the Finance Bill and consideration of the Appropriation Bill. Both Bills enacted.

Table 15(a)

Voting procedure

(a) Preliminary vote on broad budget outlines and Exchequer balance

Belgium	Each Chamber in turn examines the general presentation and the ways and means budget. The voting of the ways and means budget implies adherence to the broad lines of economic, financial and budgetary policy set out in the Budget Statement.
Denmark	No preliminary vote. Before examination of the budget there is a general political debate at the first reading.
FR of Germany	Bundesrat: first passage of Bills. Bundestag: general debate at the first reading; the budget is then sent to the Budget Committee.
Greece	No preliminary vote. Parliament discusses the broad budget outlines and government policy in general, presented in the introductory statement.
France	Preliminary vote on total revenue and expenditure.
Ireland	The Dáil votes on a motion to give immediate statutory effect to any proposals which need them. No separate vote on the budget total. No preliminary vote on the financial balance.
Italy	Preliminary vote on total revenue and expenditure.
Luxembourg	None.
The Netherlands	No preliminary vote, but before examination of the budget section by section, there is a general political debate.
United Kingdom	There is no vote taken on the budget as a whole. However, when the Chancellor of the Exchequer has made his budget speech, resolutions are put to the House which have the effect of authorizing (pending the Finance Bill) any tax changes proposed in the budget. The debate on the budget is carried on; 'general' resolution of approval put to the House each year.

Table 15(b)

Voting procedure
(b) Order and scope of vote

Belgium	Each departmental budget forms a separate draft law. The draft budgets are examined in parliamentary committee in each Chamber (report stage) and are then discussed in full parliamentary session. Each article of the Budget Act is voted separately, and then the whole Act is voted.
Denmark	After the first reading (early October): detailed examination of the proposed budget, including income and expenditure and amendments proposed by the Standing Parliamentary Finance Committee. Interrupted by a second reading, in the beginning of November. Third reading (mid-December). Vote on amendments article by article. Vote on the budget as a whole.
FR of Germany	Before the second reading in full sitting, discussions on individual departmental budgets in the Budget Committee. Vote on third reading. Bundesrat: second passage: enactment and proclamation of the Finance Bill. Adoption of the budget by the Finance Bill.
Greece	The draft budget, submitted before the end of November, is examined by a special parliamentary committee, which draws up reports. The plenary session debate covers receipts in general, and expenditure broken down by ministry and category. Receipts and expenditure by ministry are approved separately in a single vote.
France	The evaluation of revenue is the subject of an overall vote for the general budget. General budget expenditure is voted: one specific vote for services and one vote per heading and within each heading, per ministry, for 'new measures'. Services: represent appropriations vital to the continued functioning of State services under the same conditions as in the previous year. New measures: correspond to the differences (plus or minus) by reference to the services.
Ireland	Tax changes may be voted on individually when the relevant financial resolutions are put on budget day, and they may also be voted on when the Finance Bill comes before the Dáil subsequently. Expenditure by department is debated in Dáil Éireann during the course of the year and estimates are usually taken by ministerial group. The estimates of expenditure are given formal statutory effect by the annual Appropriation Act. Under the Central Fund (Permanent Provisions) Act 1965, departments may spend up to four-fifths of the previous year's appropriation pending consideration of the estimate by the Dáil and the passing of the Appropriation Act.
Italy	Sequential vote: (i) the various estimates of expenditure (one for each ministry) and the estimates of resources: voting proceeds article by article, (ii) articles of the draft Bill, (iii) the whole of the draft Bill.
Luxembourg	Voted article by article. Vote on amendments proposed by the government or deputies, article by article. Vote on the budget as a whole. Second vote on the budget as a whole after three months, unless dispensed with by the Chamber of Deputies and the Council of State.
The Netherlands	Each departmental or special service budget (17 altogether) constitutes a separately voted draft law. Voting is by article and, where appropriate, by subparagraph, i.e. the smallest subdivision provided for.
United Kingdom	Supply services are authorized by the Appropriation Act. The authority covers the total as itemized in approximately 190 separate votes. Measures affecting taxes are authorized in the Finance Act.

Table 16

Power of Parliament to amend budget proposals

Belgium	Each of the Chambers has unrestricted rights of initiation and amendment.
Denmark	(See Table 15 (b)). Amendments to increase or decrease expenditure and/or income may be proposed by the government and equally by members/parties of the Folketing.
FR of Germany	The Bundesrat cannot amend government proposals; it can only propose modifications (Law on use of the right of veto). The Bundestag has complete freedom to amend, with the reservation that increases in expenditure or decreases in revenue shall be accepted by the government (Article 113 of the Basic Law).
Greece	No limit on Parliament's power to amend proposals.
France	Two texts are applicable: (i) Article 40 of the Constitution: 'Proposals and amendments put forward by Members of Parliament will not be entertained where their adoption would lead either to a reduction in public resources or an increase in or creation of a public liability.' (ii) Article 42 of the *loi organique* as concerns Finance Acts: 'Only the amendments which lead to the reduction of expenditure, to the creation or increase of revenue or to ensure control of public expenditure, will be entertained.' Expenditure: Increase in expenditure is judged by reference to the government's plans and not to existing liabilities (no amendment may reduce savings proposed by the government under the heading of 'new measures'). Any increase in expenditure is forbidden — compensatory amendments (increase in expenditure offset by reductions in other expenditure or by increase in revenue) are therefore not permissible. Revenue: 'No amendment shall reduce the total revenue deriving from existing legislation; it can, however, reduce the increase expected from new tax measures proposed by the government. Compensatory amendments (decrease in one item of revenue balanced by an increase of at least an equal amount in another) are permitted.'
Ireland	The Dáil may refuse to grant the supply of money for expenditure or reject a tax change. Only a member of the government, however, may put forward a proposal for any aid, grant or charge on the public revenue. Th Seanad cannot reject tax increase proposals in a Finance Bill or expenditure items in the annual Appropriation Bill.
Italy	The Finance Act cannot introduce either new taxes or expenditure by reference to the existing law but within the framework of the existing law, Parliament can increase or decrease appropriations proposed by the government. It can also reject the proposed economies.
Luxembourg	No limit on the power of the Chamber of Deputies. All amendments must be submitted to the Council of State (consultative body on legislation) for an opinion prior to any vote.
The Netherlands	The second Chamber can modify the draft budget in any way. The first Chamber can only accept or reject a section (draft Bill).
United Kingdom	Parliament has power only to reduce the estimates. Increases cannot be proposed except by the government.

5. Some concluding remarks

While the trend of revenue depends mainly, as a rule, on the expansion of the tax base, the control and limitation of expenditure is above all a question of willingness and of political determination. According to the circumstances, the existence of a good budgetary system does not necessarily prevent a lack of control of public expenditure, whereas a less well developed system can permit a satisfactory measure of control, if the authorities apply themselves to such a task.

This is all the more the case as in all Member States, the growth of expenditure is to a large extent determined by the automatic application of legislative and existing regulations that only a political decision can change.

None the less, certain practices or techniques may, to a greater or lesser extent, lead to overshooting in expenditure. They include in particular:

(i) the use of non-consolidated funds with the main part of the budget, and the absence of a consistent and comprehensive presentation of expenditure;

(ii) the possibility of bringing forward appropriations and commitments that do not have a precise timetable;

(iii) the absence of sufficiently detailed multiannual expenditure forecasts as well as indications of the medium-term effects of new parliamentary or government initiatives;

(iv) the use of open-ended or contingency appropriations or simple estimates if the risks of overshooting are not covered by a sufficiently large reserve in the budget;

(v) the possibility of resorting, without too much difficulty, to expenditure not requiring prior authorization that can be approved retrospectively by Parliament;

(vi) the excessive use of fundamental rules regulating expenditure, while decisions on specific appropriations are not genuine expenditure authorizations.

Moreover, the alternative to a better control of expenditure, namely the discipline which countries previously imposed via the constitution or general legislation limiting the deficit, has practically disappeared (except in the Federal Republic of Germany).

Over the past few years, however, some countries have introduced methods into their budgetary procedures so that when budgetary objectives require the amendment of existing laws, the necessary amendments can be rapidly voted *en bloc;* this both speeds up the implementation and improves the efficiency of budgetary measures.

Unit labour costs in manufacturing industry and in the whole economy

The Community's unit labour costs for manufacturing industry relative to those of 11 industrialized OECD countries (in common currency terms) fell in 1982 by 3,7% after a decline of 13,4% in 1981. The more favourable development in the Community's relative unit labour costs since 1980 is, however, explained totally by exchange rate movements *vis-à-vis* its principal trading partners. Thus in 1981 and 1982 the effective exchange rate of Community currencies declined by 15% and 5,5% respectively, the balance of 1,8% and 1,9% reflecting a worsening of the position in national currency terms, i.e. excluding the effect of exchange rate changes. Accordingly as far as labour costs per unit of output are concerned, despite nominal disinflation in all member countries, no progress has been made in reversing the steady erosion of Community competitiveness experienced through most of the 1970s and it has been only the marked fall in relative exchange rates which has enabled this trend to continue without a fall in the Community's share of world markets.

In the USA and Japan, on the other hand, relative unit labour costs in national currency terms fell steadily during the 1970s. This movement was particularly pronounced in the period 1970-77 in the USA and in the period 1976-82 in Japan when the manufacturing indices for both of these countries fell by 25% and 40% respectively, reflecting, in the latter case, the enormous productivity gains being recorded in the industrial sector here (7% p.a. on average in the 1970s compared to Community productivity increases of 4% in the same period).

For the Community's Member States individually, developments in 1982 have differed both as between countries and within the different sectors of the economy. In national currency terms relative unit labour costs in manufacturing have declined in all Community countries except Greece, Italy and France, where large deteriorations are shown in the estimated figures and in Ireland, where little change was recorded. The improvement of relative labour cost competitiveness was most pronounced in the Benelux countries followed by the Federal Republic of Germany, the United Kingdom and Denmark.

Regarding the components of unit labour cost developments, manufacturing value added in 1982 fell or stagnated in all Community countries except Ireland and Denmark. Nevertheless, because of labour shedding in the industrial sector, productivity gains were recorded (as in 1981) in all countries with the exception of the Federal Republic of Germany and Luxembourg where productivity declined marginally for the third year in succession. Greatest productivity gains were recorded in Denmark, the United Kingdom and Ireland, followed by the Netherlands and Belgium, while in France, where measures were taken during the year to reduce the working week, increase holidays and boost recruitment, and in Italy productivity gains were under half a percentage point. In the United States production per employee fell modestly after the increase of 3% recorded in 1981, while in Japan productivity gains continued to be made, although they were down to just over 1% in both years after the rapid increases (nearly 8% on average p.a.) registered in the period 1976-80. The rapid productivity growth in Belgium over the past few years was due principally to a substantial fall in employment rather than to large increases in output. Thus, in Belgium, the capacity which has been lost does little to improve the overall position of the rest of industry. A similar situation emerged in the United Kingdom in the post-1980 period and this factor should also be borne in mind when analysing recent UK productivity performance.

As far as the growth of compensation of employees in manufacturing is concerned, Community countries can be broken down into two rather distinct groups. In 1982 growth rates of between 4,4% and 6,9% were recorded in the Federal Republic of Germany, Belgium, the Netherlands and Luxembourg, while increases of over 10% were registered in the United Kingdom, Denmark, Ireland, France and Italy. (Comparable data on employees have not yet been obtained for Greece.) Forecasts for 1983 show a significant deceleration in most rates of increase, with a particularly large movement projected for the United Kingdom, bringing the rate of growth here more into line with the first group of countries. Outside the Community, a continuation of the decline in growth rate of compensation per head is forecast for the United States, which is now expected to be down to just over 6% in 1983, an increase of the same order of magnitude as that forecast for Japan.

As a result of these individual developments in productivity and wages, unit labour costs in manufacturing in 1982, in national currency terms, increased most rapidly in Greece (29%), Italy (17%) and France (14%). In Luxembourg and Ireland increases were 8% and 7% respectively while in the Federal Republic of Germany, the United Kingdom, Denmark and the Netherlands rises were between 5 and 4%, with the lowest increase being recorded in Belgium (1,3%). Forecasts for 1983 show a significant slowing-down in unit labour costs for all countries except Belgium, where a modest increase is projected, and the United Kingdom, where the growth rate will remain at around 4,5%. Outside the Community, unit labour costs rose by 7,9% in the United States in 1982 and will decline to 4% in 1983, while in Japan the growth rate will move down from 3,8% in 1982 to just over 2% in 1983.

The interaction of unit labour costs in individual countries with those of competitor countries along with movements in exchange rates produces the results commented on at the beginning of this chapter. In last year's publication a number of reasons were listed why the data on relative unit labour costs should be interpreted with caution and only used as one indicator of the movement in an individual country's

Table 1

Average hourly labour costs in manufacturing industry

(ECU)

	B	DK	D	F	IRL	I	L	NL	UK	USA	JAP
1981	11,60	10,00	10,30	9,30	5,90	7,30	10,50	10,60	6,90	—	—
	(10,47)	(—)	(9,97)	(7,93)	(—)	(7,70)	(—)	(9,38)	(6,37)	(9,95)	(6,50)

Note: Figures for Community countries relate to labour costs and include all expenditure borne by employers in connection with the employment of workers, i.e. direct pay, bonuses, paid annual leave, benefits in kind, social security charges paid by the employer, special levies, etc. (*Source:* Eurostat, 17 December 1982).
Data in brackets for certain Community countries, the United States and Japan covering earnings and fringe benefits are drawn from the Institut der Deutschen Wirtschaft, 6 May 1982.

competitiveness. Only one of these reserves can be lifted this year. This relates to the trade weighting matrix which is now based on a moving rather than a fixed 1974 structure of international trade. The weights for the latest year in the series are shown in Table A1.

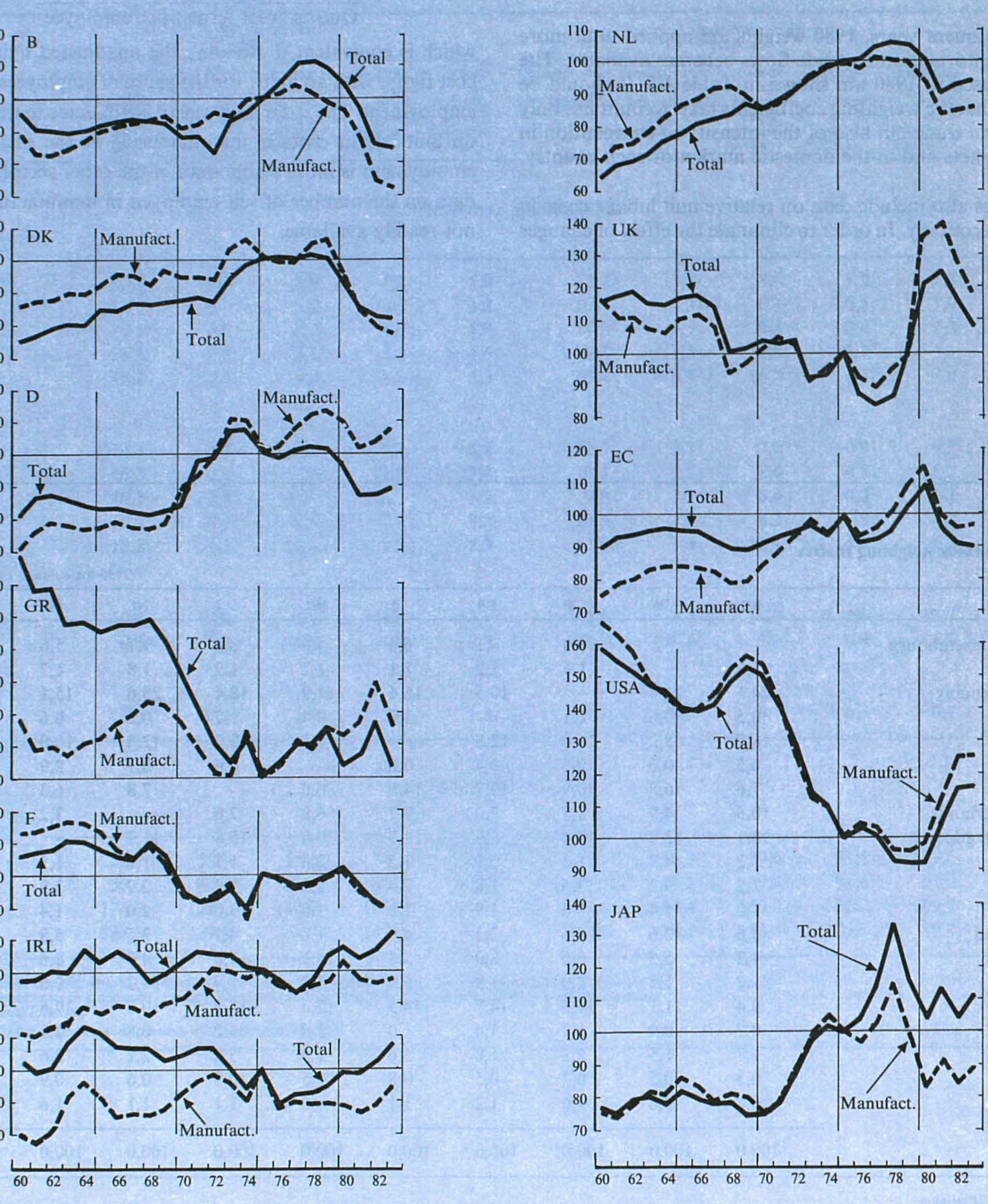
On the question of the absolute level of labour costs some fragmentary information is provided in Table 1 which shows 1981 data on absolute average hourly labour costs in ECU for Community countries except Greece, along with estimated data for the United States and Japan. Since the level of productivity may be very different from one country to another, figures on hourly wage costs cannot be considered to represent the level of unit wage costs. They do, however, give some interesting comparative data enabling certain qualifications to be made to the results given in the relative unit labour cost series. Accordingly, judging from the absolute levels of wages in the Federal Republic of Germany and the Netherlands on the one hand, and Belgium on the other, the Belgian economy may not be as competitive as is suggested by the relative cost series. In fact, absolute costs in the latter country are the highest among the countries studied. A similar, though opposite, conclusion could be drawn for the United Kingdom where average hourly labour costs are still considerably below those of most other Community countries. The deterioration in relative unit labour costs of the United Kingdom in recent years may not have had such a dramatic impact on developments as would have been expected from the relative costs series alone. Of interest too is the low absolute level of labour costs in Japan: the level here is, in fact, considerably below those in all Community countries except the United Kingdom and presumably Ireland.

The data on relative unit labour costs for the total economy are also presented in the country tables. Although some conceptual problems arise as far as the calculations are concerned (see Annex) as well as the appropriateness of comparing, on the basis of trade weights, relative prices of certain goods, included in output but not traded, the analysis produces some results which highlight cases where the exposed sectors of the economy have adjusted more rapidly to the various shocks received over the period than the sheltered sectors. Of particular note is the differences between the smaller and larger economies within the Community. Thus for most of the smaller member countries, adjustment in manufacturing relative unit labour costs has tended to be quicker and more pronounced than in those of the total economy (Belgium, the Netherlands, Ireland and, more recently, Denmark). In some of the larger Community countries the rate of increase in compensation of employees tended to be higher in manufacturing than in the total economy during the second half of the 1970s, the case of the Federal Republic of Germany in particular, while more recently industrial productivity growth has been below that recorded in the total economy (the United Kingdom and the Federal Republic of Germany). As a result, manufacturing competitivenesss for these two countries shows a less favourable position than that of the whole economy. In Italy a considerable divergence has emerged between the two measures, with a sharp deterioration in competitiveness of the total economy in recent years caused by lower productivity increases than in manufacturing. In the remaining Member States both measures have been quite close in recent years, a development which can also be noted, for a longer period, in the USA, while in Japan the large productivity gains in industry have meant that manufacturing competitiveness has outperformed that for the total economy.

Methodological changes in series

Data on remuneration of employees per head, productivity, unit labour costs and relative unit labour costs in manufacturing industry are given in this chapter on the basis of the methodology described in *European Economy* No 8, March 1981. Modifications and extensions to the weighting matrix used for the relative positions of countries were commented on in the Technical Annex to *European Economy* No 14, November 1982, point 2.2. These recent changes extend the

GRAPH 1: **Relative unit labour costs in manufacturing and in the whole economy (common currency terms, 1975 = 100)**



coverage of countries to Greece and Portugal and change the weighting system for individual countries from fixed weights, based on the 1974 pattern of trade to current-year weights for the years up to 1980.

For subsequent years, 1980 weights are applied until more detailed information on trade flows becomes available. The weights used in 1980 are shown in Table A1. It should be recalled that 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 tables also include data on relative unit labour costs in the total economy. In order to eliminate the effect of changes in the proportion of employees in total employment, unit labour costs in the total economy have been estimated as

$$\frac{\text{Compensation per employee}}{\text{Output (real terms) per employee}}$$

which is equivalent to dividing the unadjusted unit labour cost figure with an index for the share of employees in total employment. The latter adjustment is not made to the figures on unit labour costs in manufacturing as the structure of employment is more stable than in the other sectors and as data on the number of self-employed in manufacturing are not readily available.

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
Australia	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 at the head of the table.

Table 2

Labour cost indicators, EC 9

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	12,1	2,8	8,9	4,2	5,0	12,4	3,7	8,4	1,0	1,8	0,8
1972	11,0	5,5	5,2	3,9	5,2	10,9	4,3	6,3	0,5	1,9	1,3
1973	15,5	6,6	8,3	4,0	5,9	14,2	4,5	9,3	0,4	2,2	1,8
1974	16,3	2,8	13,2	−2,0	−4,6	16,5	1,5	14,8	−0,7	−3,3	−2,7
1975	18,1	−1,5	19,8	4,0	6,5	16,4	−0,1	16,4	4,5	7,0	2,4
1976	14,7	8,9	5,4	1,7	−6,8	12,5	5,1	7,0	−0,9	−9,2	−8,4
1977	10,5	2,8	7,6	1,9	2,8	10,3	2,2	8,0	0,8	1,7	0,9
1978	10,1	2,9	6,9	2,3	5,2	9,8	2,7	6,9	0,2	3,1	2,9
1979	10,9	4,3	6,4	2,2	8,2	10,9	2,4	8,3	1,9	7,9	5,9
1980	12,8	1,7	11,0	3,1	5,3	13,5	1,3	12,1	4,1	6,3	2,2
1981	10,4	2,2	8,1	1,8	−13,4	12,1	1,3	10,7	2,6	−12,7	−14,9
1982	9,5	1,4	8,1	1,9	−3,7	8,7	1,4	7,2	0,4	−5,1	−5,5
1983 [3]	7,6	0,5	7,0	2,4	1,3	7,2	1,1	6,1	0,5	−0,7	−1,1
	Index 1975 = 100										
1960	21,9	52,9	41,5	76,5	74,8	22,3	56,3	39,6	91,5	89,5	97,8
1970	50,6	85,4	59,,4	87,2	84,1	51,8	87,2	59,4	94,6	91,2	96,5
1980	174,7	122,2	143,0	111,7	114,9	171,6	114,4	150,0	106,2	109,2	102,9
1983 [3]	227,3	127,1	178,7	118,7	97,0	224,0	118,7	188,8	109,9	89,9	81,8

1 Unit labour costs in national currency by reference to the weighted average for 10 main competing countries.
2 Unit labour costs in a common currency by reference to the weighted average for 10 main competing countries.
3 Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 3

Labour cost indicators, Belgium

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	13,2	4,5	8,3	1,3	1,2	11,7	2,8	8,6	0,6	0,5	−0,1
1972	15,3	9,4	5,4	1,3	4,1	14,0	5,4	8,1	2,0	4,9	2,8
1973	12,9	9,4	3,2	−2,9	−1,5	13,0	4,8	7,8	−0,8	0,6	1,4
1974	20,5	2,5	17,6	4,8	6,2	18,2	3,0	14,8	1,2	2,5	1,4
1975	14,4	−0,7	15,3	−1,3	0,1	16,5	−0,6	17,2	3,2	4,7	1,4
1976	18,8	14,4	3,8	−1,1	1,3	16,1	6,4	9,1	2,0	4,4	2,4
1977	9,3	5,4	3,7	−3,1	2,5	8,9	0,9	7,9	0,3	6,1	5,7
1978	8,6	7,0	1,5	−4,9	−2,1	7,6	3,0	4,5	−2,4	0,4	2,9
1979	7,8	6,2	1,5	−4,2	−3,1	5,4	1,2	4,2	−3,1	−1,9	1,2
1980	9,6	1,6	8,0	−2,1	−2,6	8,8	3,1	5,5	−4,2	−4,7	−0,5
1981	6,2	3,7	2,4	−4,3	−9,4	7,3	0,3	7,0	−1,8	−7,1	−5,3
1982	5,4	4,0	1,3	−5,9	−14,6	6,1	1,6	4,4	−2,8	−11,8	9,2
1983 [3]	5,7	3,2	2,4	−3,1	−2,7	5,5	1,0	4,5	−1,1	−0,7	0,4
	Index 1975 = 100										
1960	21,4	47,3	45,2	95,4	88,5	23,9	56,9	42,0	102,8	95,3	92,7
1970	49,2	78,5	62,6	97,1	90,7	50,5	86,0	58,7	94,1	87,8	93,3
1980	166,6	139,2	119,7	85,6	96,0	156,0	115,3	135,3	92,7	104,0	112,2
1983 [3]	197,1	155,0	127,2	74,6	72,2	187,5	118,6	158,1	87,6	84,7	96,7

[1] Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
[2] Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
[3] Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 4

Labour cost indicators, Denmark

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	14,5	6,0	8,0	0,9	0,0	11,7	1,8	9,7	1,7	0,8	−0,9
1972	8,4	5,9	2,3	−1,9	−1,2	7,9	3,3	4,5	−1,9	−1,2	0,7
1973	14,9	4,1	10,3	4,5	10,8	13,1	2,6	10,3	2,1	8,2	6,1
1974	23,3	5,6	16,8	1,9	2,4	18,4	−0,4	18,9	3,9	4,4	0,5
1975	15,4	6,3	8,6	−8,8	−5,7	14,0	0,2	13,7	−1,6	1,7	3,4
1976	12,0	8,0	3,7	−3,1	−0,9	11,7	5,0	6,3	−1,9	0,4	2,3
1977	10,8	2,9	7,7	0,2	−0,3	9,7	1,2	8,5	0,2	−0,3	−0,5
1978	15,9	2,8	12,7	5,9	5,8	9,2	0,7	8,4	1,3	1,2	−0,1
1979	10,5	2,3	7,9	2,3	1,5	9,4	2,5	6,8	−0,5	1,2	−0,8
1980	8,5	2,2	6,1	−4,1	−11,7	9,9	−0,6	10,6	0,3	−7,6	−7,9
1981	9,3	5,5	3,6	−3,7	−10,3	10,2	2,0	8,0	−1,2	−7,9	−6,8
1982	11,2	6,6	4,3	−2,0	−6,1	11,0	2,5	8,3	1,0	−3,2	−4,2
1983 [3]	7,0	4,1	2,8	−2,3	−2,7	6,9	1,3	5,6	−0,3	−0,8	−0,5
	Index 1975 = 100										
1960	19,0	47,8	39,8	88,1	85,2	20,0	64,0	31,2	76,9	74,4	96,7
1970	49,3	76,2	64,7	104,0	94,6	54,3	92,9	58,5	96,1	87,4	90,9
1980	172,4	119,5	144,2	100,8	93,8	160,8	108,9	147,6	99,3	92,4	93,0
1983 [3]	224,3	140,0	160,2	92,9	76,8	210,3	115,4	182,3	98,8	81,7	82,6

[1] Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
[2] Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
[3] Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 5

Labour cost indicators, Federal Republic of Germany

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	10,6	2,1	8,4	1,9	4,9	12,6	3,0	9,3	1,5	4,5	3,0
1972	10,2	4,7	5,3	2,2	5,0	9,1	4,1	4,8	−1,5	1,2	2,8
1973	13,5	5,8	7,3	1,8	12,2	12,1	3,8	8,1	−0,8	9,4	10,2
1974	12,2	4,0	7,9	−6,0	−0,6	11,5	2,0	9,3	−5,4	0,0	5,7
1975	8,2	0,5	7,7	−10,8	−9,4	7,2	1,3	5,8	−9,0	−7,6	1,6
1976	10,3	8,8	1,5	−3,8	1,8	7,9	6,2	1,6	−6,9	−1,5	5,8
1977	7,5	2,7	4,6	−2,4	5,5	6,6	3,3	3,2	−5,4	2,4	8,2
1978	6,3	1,6	4,6	−1,7	4,2	5,6	2,5	3,0	−4,6	1,1	6,0
1979	7,1	4,3	2,6	−3,4	1,3	5,9	2,7	3,1	−4,9	−0,3	4,8
1980	6,5	−0,2	6,7	−3,5	−3,1	6,8	1,0	5,8	−4,5	−4,2	4,0
1981	3,7	−1,7	5,5	−2,3	−7,4	5,3	1,0	4,3	−5,6	−10,6	−5,2
1982	4,4	−0,6	5,0	−2,9	2,0	4,4	0,8	3,5	−4,8	0,1	5,1
1983 [3]	3,7	0,8	2,8	−3,4	3,7	3,7	1,6	2,0	−4,6	2,4	7,3
	Index 1975 = 100										
1960	26,5	54,4	48,7	105,4	70,6	26,7	56,5	47,2	120,2	80,5	67,0
1970	59,5	84,7	70,3	112,6	89,8	60,8	87,0	69,9	117,1	93,4	79,7
1980	143,7	118,2	121,6	86,1	109,7	137,3	116,7	117,7	76,3	97,3	127,5
1983 [3]	161,3	116,5	138,5	78,9	107,4	156,4	120,7	129,6	65,4	89,1	136,2

[1] Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
[2] Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
[3] Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 6

Labour cost indicators, Greece

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	:	:	2,2	−4,5	−6,5	9,2	8,1	1,0	−6,4	−8,3	−2,0
1972	:	:	3,0	−0,7	−6,9	12,4	8,4	3,7	−2,2	−8,3	−6,3
1973	:	:	13,3	6,9	−0,8	17,6	6,8	10,1	1,2	−6,0	−7,1
1974	:	:	28,5	12,7	13,4	18,7	−3,6	23,1	7,3	7,9	0,6
1975	:	:	15,7	−2,4	−12,1	19,7	5,4	13,6	−0,9	−10,8	−9,9
1976	:	:	13,7	8,4	3,2	23,9	5,1	17,9	9,5	4,2	−4,8
1977	:	:	18,6	10,7	8,1	22,3	4,4	17,1	8,3	5,8	−2,4
1978	:	:	12,9	6,3	−3,0	23,1	5,1	17,2	9,2	−0,4	−8,7
1979	:	:	18,5	11,8	5,8	21,9	2,1	19,4	10,7	4,7	−5,4
1980	:	:	25,0	13,8	−1,7	14,8	−0,1	14,9	4,1	−9,9	−13,5
1981	:	:	23,2	14,2	3,5	23,9	−0,8	24,9	13,8	3,1	−9,4
1982	:	:	28,8	19,3	10,8	27,7	0,4	27,2	17,8	9,4	−7,2
1983 [3]	:	:	18,2	11,5	−10,5	16,7	−0,2	17,1	10,1	−11,6	−19,7
	Index 1975 = 100										
1960	:	:	43,0	92,2	117,7	19,2	35,3	54,4	132,2	168,8	127,7
1970	:	:	56,4	89,7	116,1	48,8	78,7	62,0	131,6	101,6	129,4
1980	:	:	225,4	162,0	112,5	261,0	117,5	222,1	149,2	103,6	69,5
1983 [3]	:	:	422,6	246,1	115,4	482,0	116,8	413,0	220,3	103,3	46,9

[1] Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
[2] Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
[3] Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 7

Labour cost indicators, France

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	11,5	4,6	6,6	−0,7	−2,7	11,5	5,0	6,2	−2,0	−4,0	−2,1
1972	8,9	5,0	3,8	0,1	2,7	10,3	5,4	4,7	−1,8	0,8	2,6
1973	10,2	4,3	5,7	−0,3	3,8	12,8	4,1	8,4	−0,5	3,6	4,1
1974	11,3	2,4	8,6	−5,5	−11,6	17,6	2,5	14,7	−0,1	−6,5	−6,4
1975	26,8	1,1	25,5	6,1	16,6	18,6	1,2	17,2	2,0	12,2	9,9
1976	15,1	7,2	7,4	2,3	−1,2	14,7	4,3	10,1	2,2	−1,4	−3,5
1977	13,2	4,5	8,3	0,8	−3,5	12,6	2,3	10,1	1,6	−2,7	−4,3
1978	13,8	4,9	8,5	2,0	1,0	12,5	2,9	9,3	1,8	0,9	−1,0
1979	12,7	4,7	7,7	1,4	2,3	13,1	3,4	9,4	1,4	2,3	0,9
1980	14,2	1,6	12,4	1,9	2,3	14,8	1,3	13,3	2,8	3,2	0,4
1981	14,0	3,5	10,1	2,2	−6,7	14,5	1,0	13,4	3,5	−5,4	−8,6
1982	14,5	0,3	14,1	6,3	−2,4	12,1	1,6	10,7	2,6	−5,7	−8,1
1983 [3]	10,7	0,3	10,4	4,3	0,3	9,8	0,5	9,3	2,9	−1,1	−3,8
	Index 1975 = 100										
1960	22,4	46,0	48,7	107,9	112,7	21,0	51,9	40,6	100,7	105,3	104,5
1970	52,9	84,3	62,8	100,7	93,6	51,7	83,7	61,7	102,4	95,2	92,9
1980	190,9	125,1	152,5	108,6	100,7	188,8	114,8	164,4	110,2	102,2	92,7
1983 [3]	275,8	130,4	211,5	123,0	92,1	266,0	118,4	225,5	120,6	90,1	74,8

[1] Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
[2] Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
[3] Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 8

Labour cost indicators, Ireland

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	16,3	3,9	11,9	4,3	4,5	14,0	3,3	10,4	3,2	3,4	0,1
1972	17,7	5,7	11,3	7,2	5,1	16,9	7,0	9,2	1,5	−0,5	−1,9
1973	18,7	6,1	11,9	6,3	−0,7	19,8	4,0	15,2	6,6	−0,4	−6,5
1974	18,1	0,4	17,6	0,2	−2,3	18,6	3,1	15,0	−1,3	−3,8	−2,5
1975	23,1	−6,9	32,2	8,2	2,4	27,0	1,6	25,0	4,7	−0,9	−5,4
1976	23,2	8,7	13,3	5,7	−4,9	19,3	2,8	16,1	7,2	−3,6	−10,0
1977	14,4	4,3	9,7	2,1	−1,5	13,8	4,9	8,4	0,1	−3,4	−3,5
1978	17,3	8,1	8,5	0,8	1,5	14,8	3,3	11,1	3,0	3,8	0,7
1979	17,1	6,9	9,5	1,4	1,6	18,1	−0,7	18,9	8,5	8,8	0,2
1980	17,6	−4,5	23,2	9,0	6,8	19,5	1,2	18,0	5,0	2,9	−2,0
1981	16,0	4,9	10,6	2,7	−5,8	18,5	3,1	15,0	4,9	−3,8	−8,3
1982	13,0	5,7	6,9	0,2	−1,1	14,6	2,8	11,5	4,1	2,7	−1,3
1983 [3]	11,6	4,9	6,4	1,1	1,5	14,1	3,3	10,5	4,4	4,8	0,4
	Index 1975 = 100										
1960	17,0	62,4	27,2	63,7	80,8	16,1	54,9	29,4	76,6	97,2	126,9
1970	42,4	91,8	46,2	77,5	91,6	41,6	83,0	50,1	86,6	102,4	118,2
1980	227,6	125,1	181,9	120,2	103,2	219,8	112,0	196,2	126,1	108,2	85,8
1983 [3]	333,0	145,5	228,8	125,0	97,5	340,5	122,5	277,9	143,7	112,1	78,0

[1] Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
[2] Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
[3] Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 9

Labour cost indicators, Italy

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	10,9	−1,0	11,9	5,4	4,5	13,1	1,7	11,2	3,4	2,6	−0,8
1972	11,1	4,9	5,9	2,7	2,2	11,1	4,4	6,4	0,3	−0,2	−0,5
1973	22,5	8,5	12,9	7,5	−2,7	19,6	6,2	12,6	3,9	−6,0	−9,5
1974	23,2	3,7	18,7	4,6	−5,8	22,1	2,6	19,0	4,1	−6,2	−9,9
1975	22,3	−9,4	34,9	15,7	11,2	21,0	−3,8	25,7	11,1	6,8	−3,8
1976	24,0	12,3	10,4	5,8	−12,5	20,9	5,0	15,1	7,6	−11,0	−17,3
1977	20,0	2,1	17,5	10,8	2,3	21,4	1,2	19,9	12,1	3,5	−7,7
1978	14,3	2,8	11,2	5,1	−1,3	16,2	2,0	13,9	6,8	0,3	−6,1
1979	16,4	6,2	9,6	3,7	0,4	17,9	3,9	13,5	5,9	2,5	−3,2
1980	20,8	6,3	13,7	3,5	−0,4	22,2	3,1	18,6	8,5	4,4	−3,7
1981	19,3	0,9	18,3	10,9	−2,6	22,0	−0,6	22,7	13,4	−0,4	−12,2
1982	17,7	0,0	17,2	9,7	2,2	18,8	0,1	18,8	11,3	3,8	−6,8
1983 [3]	14,9	−1,4	16,5	11,1	6,9	15,1	0,1	15,4	9,6	5,5	−3,8
	Index 1975 = 100										
1960	16,0	52,9	30,2	61,6	79,4	16,5	49,7	33,3	79,3	102,3	129,0
1970	44,0	94,3	46,6	71,0	91,8	45,1	89,8	50,2	80,2	103,7	129,3
1980	239,1	133,1	179,7	132,2	88,3	245,7	116,2	211,6	148,0	98,9	66,8
1983 [3]	385,8	132,3	290,3	178,7	94,1	409,9	115,7	355,8	204,8	107,7	52,6

[1] Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
[2] Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
[3] Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 10

Labour cost indicators, Luxembourg

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	6,6	−2,8	9,7	:	:	9,3	1,2	8,0	:	:	:
1972	8,4	3,6	4,7	:	:	8,8	3,5	5,1	:	:	:
1973	10,0	7,1	2,8	:	:	12,8	8,7	3,7	:	:	:
1974	23,1	2,6	20,0	:	:	21,3	1,1	20,0	:	:	:
1975	11,8	−17,0	34,8	:	:	11,3	−7,6	20,4	:	:	:
1976	10,3	7,4	2,7	:	:	13,2	2,5	10,4	:	:	:
1977	7,7	1,7	6,0	:	:	9,4	0,4	9,0	:	:	:
1978	4,5	8,8	−3,9	:	:	5,6	4,5	1,0	:	:	:
1979	6,0	6,2	−0,2	:	:	6,0	2,9	3,0	:	:	:
1980	5,7	−0,4	6,1	:	:	7,8	0,6	7,2	:	:	:
1981	8,0	−5,2	13,8	:	:	7,7	−2,0	9,9	:	:	:
1982	6,9	−0,9	7,9	:	:	6,7	−1,1	7,8	:	:	:
1983 [3]	6,9	1,3	5,6	:	:	7,3	0,1	7,2	:	:	:
	Index 1975 = 100										
1960	26,8	91,8	29,2	:	:	29,0	69,9	41,4	:	:	:
1970	57,1	109,0	52,4	:	:	55,2	93,9	58,7	:	:	:
1980	139,1	125,6	110,7	:	:	149,4	111,3	134,2	:	:	:
1983 [3]	171,1	119,6	143,6	:	:	184,2	108,0	170,5	:	:	:

1 Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
2 Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
3 Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 11

Labour cost indicators, The Netherlands

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	13,0	4,7	7,9	0,7	1,9	13,4	3,7	9,4	1,4	2,6	1,2
1972	12,9	5,9	6,6	2,6	4,5	12,9	4,3	8,2	2,0	3,8	1,8
1973	17,2	9,6	6,9	1,1	5,3	15,1	5,7	8,9	0,4	4,6	4,2
1974	15,6	3,6	11,5	−2,1	3,4	15,8	3,5	11,9	−2,2	3,2	5,5
1975	12,2	−3,2	16,0	−1,8	0,9	13,3	−0,4	13,7	−0,8	1,9	2,8
1976	12,1	12,1	0,0	−5,2	−2,4	10,9	5,5	5,1	−2,3	0,6	3,0
1977	8,1	3,5	4,6	−2,3	3,5	8,1	2,2	5,9	−2,0	3,9	6,0
1978	7,4	4,6	2,6	−3,5	−0,8	7,2	2,0	5,1	−1,8	1,0	2,8
1979	6,7	3,3	3,3	−2,4	−0,7	6,0	0,8	5,1	−2,2	−0,5	1,8
1980	7,4	3,1	4,1	−5,9	−5,7	5,5	0,4	5,0	−4,8	−4,6	0,1
1981	4,4	3,6	0,8	−6,4	−11,0	3,3	0,1	3,2	−5,7	−10,3	−5,0
1982	6,5	2,4	4,0	−3,1	2,2	5,9	0,6	5,3	−1,9	3,5	5,5
1983 [3]	3,4	3,2	0,2	−5,2	0,8	2,7	1,9	0,8	−5,0	1,0	6,3
	Index 1975 = 100										
1960	20,1	51,2	39,4	84,8	69,0	18,9	57,5	32,8	79,0	64,3	81,4
1970	51,6	82,0	62,9	99,5	85,5	51,7	84,9	60,9	99,3	85,3	85,9
1980	149,2	129,2	115,4	82,5	93,8	143,7	111,3	129,1	87,6	100,1	114,3
1983 [3]	171,5	141,5	121,2	70,5	86,0	161,4	114,1	141,5	77,0	93,9	121,9

[1] Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
[2] Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
[3] Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 12

Labour cost indicators, United Kingdom

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	12,4	2,4	9,8	3,6	3,7	11,4	4,2	6,9	−0,6	−0,5	0,1
1972	11,2	6,1	4,8	1,4	−2,1	13,0	2,3	10,5	4,4	0,7	−3,5
1973	14,0	8,5	5,1	−0,7	−10,9	13,1	5,0	7,6	−1,0	−11,2	−10,3
1974	23,3	−0,1	23,5	8,0	3,9	18,8	−1,4	20,5	5,1	1,1	−3,7
1975	30,3	−1,8	32,6	14,0	5,2	30,9	−0,2	31,2	16,3	7,3	−7,7
1976	18,7	5,4	12,6	7,6	−8,2	14,6	4,3	9,9	2,0	−12,9	−14,7
1977	10,0	1,1	8,8	1,8	−3,1	10,4	1,0	9,2	1,5	−3,4	−4,8
1978	13,2	1,4	11,7	5,9	6,3	13,8	3,6	9,9	2,9	3,3	0,4
1979	15,8	1,3	14,4	8,9	15,6	16,4	0,7	15,6	8,0	14,7	6,2
1980	18,1	−3,7	22,7	12,6	23,9	20,2	−0,4	20,6	10,8	21,9	10,1
1981	13,3	4,3	8,7	1,6	2,7	14,7	3,5	10,9	1,9	3,0	1,1
1982	10,6	5,8	4,5	−2,7	−7,6	9,4	3,8	5,4	−2,1	−7,0	−5,0
1983 [3]	6,0	1,3	4,6	−0,8	−7,7	8,0	2,3	5,5	−0,4	−7,4	−7,0
	Index 1975 = 100										
1960	22,2	63,9	34,6	70,7	106,7	22,8	70,2	32,5	76,7	115,7	150,9
1970	43,6	86,4	50,5	77,8	101,1	45,1	90,7	49,8	79,7	103,5	129,9
1980	202,4	105,4	192,0	142,2	135,4	201,4	109,5	183,9	127,5	121,4	95,3
1983 [3]	268,8	117,9	228,1	139,4	118,6	272,9	120,3	226,8	126,7	107,8	85,1

1 Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
2 Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
3 Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 13

Labour cost indicators, USA

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	6,5	5,7	0,7	−5,7	−8,2	6,9	3,1	3,7	−3,7	−6,2	−2,6
1972	6,9	6,3	0,5	−3,1	−9,4	7,5	3,3	4,0	−2,2	−8,6	−6,5
1973	7,5	5,8	1,5	−4,9	−12,6	7,2	1,5	5,6	−3,5	−11,3	−8,1
1974	8,7	−3,6	12,8	−3,3	−1,8	7,9	−2,9	11,1	−5,4	−3,9	1,6
1975	10,6	1,4	9,2	−8,1	−8,9	8,2	1,6	6,5	−8,0	−8,8	−0,9
1976	9,6	5,3	4,1	−1,1	4,5	8,4	2,3	5,9	−2,3	3,2	5,6
1977	9,1	2,7	6,2	−0,5	−0,8	7,5	1,8	5,6	−2,4	−2,7	−0,3
1978	8,3	1,2	6,9	1,8	−7,1	7,9	0,0	7,9	1,5	−7,3	−8,7
1979	9,5	0,9	8,5	3,0	−0,4	8,6	−0,8	9,6	2,1	−1,2	−3,3
1980	10,7	−1,2	12,1	2,7	2,5	9,3	−0,8	10,3	0,5	0,2	−0,3
1981	9,8	3,1	6,5	−0,8	13,1	9,5	1,3	8,1	−0,9	13,0	14,0
1982	7,6	−0,3	7,9	0,5	12,6	6,0	−0,6	6,6	−1,4	10,5	12,0
1983 [3]	6,2	2,0	4,1	−1,4	0,1	6,2	1,0	5,1	−0,8	0,7	1,5
	Index 1975 = 100										
1960	43,1	65,7	65,7	144,3	166,7	42,4	78,3	54,2	137,2	158,5	115,5
1970	68,0	86,0	79,1	129,6	153,9	69,6	93,7	74,2	126,4	150,1	118,8
1980	156,9	109,1	143,9	105,9	98,3	149,3	102,4	145,8	99,4	92,2	92,8
1983 [3]	196,6	114,4	172,2	104,1	125,2	183,9	104,1	176,6	96,4	115,9	120,2

1 Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
2 Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
3 Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Table 14

Labour cost indicators, Japan

	Labour costs in industry					Labour costs, total economy					p.m.
	Compensation per employee (national currency)	Productivity (output per employee)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Compensation per employee	Productivity (output per person in total employment)	Labour cost per unit of output (national currency)	Relative unit labour costs in national currency [1]	Relative unit labour costs in a common currency [2]	Effective exchange rate
	% change over preceding year										
1971	13,9	4,5	8,9	4,6	6,3	15,1	4,0	10,6	4,6	6,3	1,6
1972	15,1	10,9	3,8	1,4	12,7	14,4	8,5	5,4	−0,1	11,1	11,2
1973	21,7	9,5	11,1	6,3	12,3	20,9	6,1	13,9	6,0	11,9	5,6
1974	25,2	−2,3	28,1	12,3	4,8	25,9	−0,8	27,0	11,5	4,1	−6,6
1975	13,9	1,2	12,6	−2,5	−5,2	16,3	2,7	13,3	0,9	−1,9	−2,8
1976	10,0	12,9	−2,5	−7,7	−3,1	10,3	3,4	6,7	−0,7	4,2	4,9
1977	10,1	7,5	2,4	−4,5	5,9	10,1	3,9	6,0	−1,2	9,5	10,8
1978	2,1	4,0	−1,8	−7,9	12,0	7,0	3,7	3,2	−3,9	16,9	21,7
1979	3,9	6,0	−2,0	−8,7	−15,1	6,2	3,9	2,3	−6,0	−12,7	−7,1
1980	7,9	9,2	−1,2	−11,4	−15,0	6,4	3,3	3,0	−7,1	−10,9	−4,1
1981	4,6	1,2	3,4	−3,7	9,8	7,1	2,3	4,7	−4,1	9,4	14,0
1982	5,4	1,5	3,8	−3,8	−7,9	5,4	2,0	3,4	−4,1	−8,2	−4,3
1983 [3]	5,7	3,5	2,2	−3,1	5,9	6,2	2,5	3,6	−2,2	6,8	9,3
	Index 1975 = 100										
1960	12,7	28,8	44,1	83,6	75,6	12,2	31,8	38,4	84,8	76,7	90,4
1970	44,0	79,7	55,2	81,1	74,8	42,9	82,0	52,3	80,3	74,1	92,3
1980	138,8	146,1	95,0	65,7	82,9	146,8	119,4	122,9	82,3	103,9	126,1
1983 [3]	161,8	155,3	104,2	59,0	88,8	176,2	127,7	137,9	74,1	111,5	150,5

1 Unit labour costs in national currency by reference to the weighted average for 19 main competing countries.
2 Unit labour costs in a common currency by reference to the weighted average for 19 main competing countries.
3 Provisional forecasts.

Source: Eurostat, estimates and forecasts by Commission services.

Financial markets and institutions in Greece[1]

[1] This article has been written by Professor George D. Demopoulos, Economic Adviser to the Directorate-General for Economic and Financial Affairs. The views expressed are the responsibility of the author and do not necessarily represent those of the Commission.

Contents

1.1.	Introduction	149
2.1.	The Greek financial institutions and the existing institutional arrangements	149
2.2.	The state of development of the capital markets	152
2.3.	Factors accounting for the inadequate development of the capital market	154
2.4.	Prospects for reform	155

1.1. Introduction

At the centre of the Greek financial system is the Bank of Greece, the country's central bank. Around it there is a 'thin' complex of private and governmental financial institutions which include commercial banks, investment banks, government-owned specialized credit institutions and the Athens Stock Exchange.

There are also private and foreign insurance companies, and pension funds as well as investment companies. There are, however, no building societies, hire purchase and finance houses nor any other kind of organization, apart from the above, which could be characterized as a financial intermediary.

Non-banking institutions do not play an important role in financing investment mainly due to the underdeveloped nature of the capital market. Thus, the banking system is the most important institutionalized means of mobilizing and allocating private and public financial resources.

To appreciate the structural features, the development and the workings of the Greek capital market and its nexus with the financial institutions, it is necessary that the workings and the institutional arrangements of the Greek banking system first be discussed.

2.1. The Greek financial institutions and the existing institutional arrangements

The Greek banking system consists of:

(1) the Bank of Greece;

(2) 34 commercial banks, 14 of which are Greek and 20 foreign;

(3) three investment banks;

(4) five specialized credit institutions.

2.1.1. The Greek monetary authorities [1]

The Greek monetary authority consisted, until recently, essentially in the Currency Committee, a collective body under the chairmanship of the Minister for Coordination and including the Ministers for Finance, Industry, Commerce, and Agriculture, as well as the Governor of the Bank of Greece.

The Currency Committee shaped the conduct of the country's monetary and credit policies and had the overall supervision of and responsibility for the exercise of these policies. It assigned the day-to-day execution of monetary and credit policies to the Bank of Greece.

Since June 1982, the functions of the Currency Committee have been distributed as between the government and the Bank of Greece. The government, through its Council of Government and Economic Policy, continues broadly to shape the country's monetary and credit policies, but the Bank of Greece has the responsibility for the development and implementation of these policies. The new legislation gives the Bank of Greece the power to administer interest rates, change the reserve requirements, apply credit ceilings, etc., and generally to take any action required for the implementation of monetary policy. Essentially, more powers are given to the Bank than previously.

(a) *The Bank of Greece*

The Bank of Greece, established in 1928, has the exclusive right of issuing bank notes; it provides credit to the banking system and, to a much lesser extent, to private enterprises; it provides finance to the government and manages its payments and receipts; it also manages the country's foreign exchange reserves and administers exchange controls. It seeks thus to protect the internal and external value of the Greek drachma and plays a direct role in financial intermediation.

(b) *The Capital Market Committee*

The Capital Market Committee—a public body—is entrusted with specific power to stimulate, improve and strengthen the capital market.

The Committee operates under the auspices of the Ministry of Commerce with the participation of the Ministries of Economy and Finance, the Bank of Greece, the commercial and investment banks, the Athens Stock Exchange and the Athens and Thessaloniki Chambers of Commerce. At present, the Deputy Governor of the Hellenic Industrial Development Bank acts as Chairman of the Committee.

The Capital Market Committee formulates the country's capital market policy and has the overall supervision of and responsibility for the execution of this policy. It acts as adviser to the government and the Bank of Greece.

[1] See also, George D. Demopoulos, *Monetary Policy in the Open Economy of Greece*, Athens: Centre for Planning and Economic Research, 1981; George Kasmas, *Money and Monetary Policy in a Developing Economy: The Case of Greece 1956-1966*, Ph.D. Dissertation, University of Manchester, January 1972.

2.1.2. Private and State-owned financial institutions

(a) *Commercial banks*

Commercial banks constitute the main body of the country's credit system. They are highly concentrated in the sense that the greater part of commercial banking activity is accommodated by the two major banks, namely, the National Bank of Greece and the Commercial Bank of Greece. The former covers 60% of total commercial banking activities, while the latter (along with the Ionian and Popular Bank) covers approximately 20%. They both have an extensive network of branches all over the country. [1] This illustrates the oligopolistic structure of commercial banking which, however, is technically well developed.

Despite the extent of the branch network, the use of checking accounts is very limited in Greece, the greater part of the liability side of the balance sheet of the commercial banks being in the form of private savings and time disposits.

Commercial banks extend short-term credit to industry, domestic services, import and export trades, the tobacco trades and shipbuilding. Medium and long-term credit is extended to industry and other enterprises for investment in plant and equipment and also to public enterprises. A relative peculiarity of the Greek system is the practice whereby commercial banks participate in the equity capital of a number of private enterprises. Finally, the banks are required to invest a large part of their total private deposits in interest-bearing Treasury bills.

(b) *Investment banks*

There are three Greek investment banks: the Hellenic Industrial Development Bank, which is a State-owned institution; the Investment Bank, and the National Investment Bank for Industrial Development, which are private banks. These banks were founded with the purpose of boosting the development of the capital market in Greece.

The main functions of the investment banks are to extend medium and long-term credit to industry and other enterprises such as mining, tourism and shipping, to participate in the equity capital of private enterprises, to issue and underwrite new issues of shares and bonds and to provide technical and managerial assistance to their clients.

(c) *Specialized credit institutions*

Under this heading we classify the (mainly State-owned) institutions engaged in extending credit to specific sectors within the country's economy. They extend credit to sectors where there is lack of interest on the part of the private financial institutions, mobilizing and allocating public and private financial resources in the process.

The specialized credit institutions are:

1. the Agricultural Bank of Greece, with an exclusive network of branches spread all over the country. It functions as a bank in the sense that it accepts deposits (mostly in the form of savings). It is, however, mainly financed by the Bank of Greece. It extends short and long-term credit to agriculture; it distributes fertilizers and other supplies to farmers; it supervises farm cooperatives and provides technical and management assistance;

2. the Postal Savings Bank which functions as a bank in the sense that it accepts deposits (mostly in the form of savings) and extends long-term credit to local authorities, public enterprises and to public sector employees and pensioners for housing;

3. the National Mortgage Bank of Greece functions as a bank in the sense that it accepts all types of deposits including deposits in foreign exchange. It is, however, mainly financed by the Bank of Greece. It extends credit to the housing sector, tourist enterprises, public enterprises and to non-profit-making organizations. It is the major mortgage institution of the country;

4. the Mortgage Bank which also extends credit for housing;

5. the Consignations and Loans Fund which accepts consignment deposits as well as private savings deposits; it manages the funds of public entities; it extends credit to public entities, non-profit-making organizations and to public sector employees and pensioners for housing.

(d) *Insurance companies*

There are numerous insurance companies, both Greek and foreign, operating within the country. Branches or agents of foreign insurance companies are not required to publish accounts concerning their business in Greece. Hence, their activities cannot easily be estimated. It would appear, however, that their reserves for different types of risk constitute approximately 25% of all insurance reserves.

The Greek insurance companies can be divided into two categories: those which are directly controlled by commercial banks, i.e. the 'banking insurance companies', and others—all of which are small family companies.

The insurance companies in Greece, in contrast to those in economies with a developed capital market, do not occupy

[1] They have also recently increased their network of offices abroad.

an important position in the financial markets. They invest much of their assets in real property, with only minor purchases of fixed-interest securities. However, they do engage in some purchases of business stocks and shares, though their total credit to the private sector is still rather low. By contrast, the insurance companies hold a substantial percentage of their total assets in bank deposits. It is noteworthy, too, that insurance business claims (mainly unpaid premiums) represent a significant percentage of their total assets.

The main reason for the peculiar investment pattern of the insurance companies is, as suggested above, the underdeveloped nature of the capital market in Greece, where the number of securities transacted on the stock exchange is limited and investment in securities with satisfactory productivity and a high marketability is very difficult. This situation suggests, of course, that savings are not being efficiently channelled towards capital formation.

(e) *Pension funds*

Pension funds can affect the liquidity structure of an economy by switching operations in the vast amounts of reserves they hold as well as through their investments of newly accruing funds. They can also play a special role in the longer term of the capital market, due to the special nature of their liabilities, since they are in a position to hold long-term investments.

In Greece, pension funds do not exercise an independent investment policy, particularly as regards their holdings of financial assets. They are required by law to invest all their funds in the form of deposits with the Bank of Greece, where in turn they are mainly utilized for the financing of agriculture, trade and industry; the remainder is invested in government securities, shares and units of the Greek investment funds and in other shares quoted on the Athens Stock Exchange.

2.1.3. Official intervention in the primary and secondary securities markets

(a) *General*

Although the Greek monetary authorities do not use open market operations as an instrument of monetary policy, they have, in their efforts to achieve stabilization and economic development objectives, heavily relied on monetary policy as a means of demand management as well as of influencing the allocation of credit to various sectors of the economy. To these ends, the authorities have introduced a complex system of quantitative controls, such as compulsory differential reserve requirements on banks' liabilities and assets, selective credit controls, the fixing of interest rates paid on bank credit and deposits, and credit ceilings.

Official intervention with regard to the interest rate structure affects price developments in the secondary securities market but it leaves the exercise of credit policy unaffected.

Banks are required to invest a percentage of their total private deposits, whether denominated in drachmas or foreign exchange, in Treasury bills, government bonds and bonds of public enterprises, as secondary reserves (at present this is equal to 39,5% of their total deposits: 37% is invested in Treasury bills and 2,5% in government bonds and long-term obligations of public enterprises). In addition, banks are required to invest 15% of their total drachma deposits in long-term loans for productive investment or in bonds or preferential stock issued by industrial concerns. However, banks' investment in private sector securities is low (in the 1970s, preferential stock and bonds ranged from 3,5 to 5,2% of the commercial banking system's total assets, although banks are permitted to invest up to one-sixth of their total capital in such securities).

In fulfilment of their obligation to invest in financial assets, banks use the Athens Stock Exchange when buying stock. Moreover, the authorities, in their effort to stimulate activity in the capital market, have, in the past, encouraged commercial bank financing, at a special interest rate and within quota limits, of the holders of securities on collateral of bonds or shares.

Funds of the specialized credit institutions, such as the Postal Savings Bank and the Consignations and Loans Fund are also, to a very minor degree, invested in Treasury bills or are used to buy bonds and shares with the permission of the monetary authorities.

No price support policy is exercised in the corporate bond market; curbing of price fluctuations is a matter for the issuer. However, companies are forbidden to purchase or subscribe to their own shares.

(b) *The tax system and the capital markets* [1]

This is not the place for a detailed presentation of the tax system which regulates the activities of the capital markets. However, a few aspects of it can be summarized.

The coupon income of all publicly issued bonds is exempt from income tax as is the case for interest earned on all types of deposits with financial institutions.

[1] This section draws heavily on Anestis S. Constantinides, *Greek Securities Markets*, Bank of Greece, Economic Research Department, Athens, 1981.

Domestic corporations are taxed on that part of their profits which is not distributed. Distributed profits are exempt from tax at the corporate level and are taxed only as shareholders' income from dividends. Double taxation of profits is thus entirely avoided.

Undistributed profits are taxed at different rates depending on whether or not the company is quoted on the Athens Stock Exchange, with lower rates applying to quoted companies. Common rates apply to domestic and foreign corporations, limited liability companies and partnerships.

Domestic corporations are subject to tax on their worldwide income, whether derived from domestic or foreign sources.

Foreign entities (corporations, limited liability companies, general limited partnerships) are subject to tax on (i) their income earned from Greek sources, and (ii) their profits of foreign origin earned through a permanent establishment in Greece.

Dividends, fees, fringe benefits, etc., for Board members, managers and directors are subject to a withholding tax collected by the companies. Tax incentives apply to dividends derived from quoted (as opposed to unquoted) shares. A second differentiation is applied to dividends according to whether the shares concerned are bearer or registered documents with the latter being treated more favourably.

Recent capital market legislation (Law No 876/1979) grants additional generous tax incentives in order to attract investors to the stock exchange. Among these are the following:

(i) The tax rate on dividends for registered and bearer shares is further reduced so long as the company increases its capital in cash by 30% and more than DR 30 million. The tax rate decrease is valid for a period of three years from the date of share issue on the following two conditions: (1) that the new shares are not sold to existing shareholders of the company, and (2) that the company does not reduce its issued capital by buying back shares within five years after the issue of the new shares (the three-year period of tax reduction may be extended to six if the company increases its capital by 60% in cash and if such an increase amounts to not less than DR 60 million).

(ii) It is also provided by the new legislation that companies may capitalize their existing tax-free reserves and be taxed at a much lower rate, i.e. at 10%, provided that, at the time of capitalization, an amount equal to such capitalized sums is contributed by existing or new shareholders in order to increase companies' capital in cash.

Tax incentives are also given to households who are allowed to deduct from their net income varying sums, depending on the size of the family, corresponding to the purchase of companies' new shares quoted on the Athens Stock Exchange if the capital of such companies increases in cash. Moreover, dividends from quoted securities are exempt from income tax subject to a maximum of DR 100 000 in total and to DR 25 000 for each share holding.

No capital gains tax is levied on transactions in bonds or shares. Similarly, wealth held in these financial assets is not subject to estate duty, except for inheritance tax.

2.2. The state of development of the capital markets

2.2.1. Overview

The money market in Greece diverges sharply from the characteristics and working of such markets in advanced economies. The banking system is the only financial intermediary in this market—an interbank money market operates since 1981. With regard to the longer end of the capital market, since virtually the total capital flow of households, private enterprises, public entities and public corporations is accumulated in the banking system in the form of demand, savings and time deposits, little funds remain for investment in issues of share capital or bonds. The result is that the market in Greece for corporate stock, corporate bonds, government bonds and mortgage borrowing is not well developed. The country appears to lack financial institutions in sufficient variety to provide a flexible mechanism for raising capital. It also lacks any specialized agencies for the promotion of companies and the issuing, underwriting and distribution of securities. Thus, the banking system remains the main institution which both advances short-term finance, mainly to the government and the business sector, and also assists in the public placement of securities.

2.2.2. The primary securities market

(a) *The bond market*

Table 1 reveals that since 1973 there have been no new government bond issues, while the latest bond issue by the public non-financial enterprises—that of the Public Power Corporation—was in 1977 for an amount of DR 3 000 million. Private non-financial enterprises have not been issuing new bonds since 1976; in the period 1978-82 bonds were issued almost exclusively by financial institutions.

The reluctance of the government to raise funds through the capital market stems from the fact that the public sector

Table 1

Issues of securities

(million DR)

	1975	1976	1977	1978	1979	1980	1981	1982 [1]
I. *Bonds*								
(a) *Total gross*	*330*	*2 949*	*6 808*	*3 987*	*6 007*	*13 892*	*17 440*	*30 420*
– Central government	—	—	—	—	—	—	—	—
– Public non-financial enterprises	—	—	3 000	—	—	—	—	—
– Private non-financial enterprises	84	304	—	—	—	—	—	—
– Financial institutions	246	2 645	3 808	3 987	6 007	13 892	17 440	30 420
(b) *Total net*	*–806*	*1 882*	*4 447*	*77*	*442*	*4 739*	*8 495*	*15 686*
– Central government	–579	–610	–774	–826	–904	–962	–851	—
– Public non-financial enterprises	–455	–396	2 443	–662	–446	–888	–1 583	—
– Private non-financial enterprises	2	265	–108	–54	–138	–60	–99	—
– Financial institutions	226	2 623	2 886	1 619	1 930	6 649	11 028	15 686
II. *Shares*								
Total	*1 367*	*6 313*	*1 324*	*2 827*	*4 490*	*7 146*	*1 199*	*1 130*
– Private non-financial enterprises	530	688	520	400	197	130	1 034	1 130
– Financial institutions	837	5 625	804	2 427	4 293	7 016	165	—
III. *Total new issues (net)*	*561*	*8 195*	*5 771*	*2 904*	*4 932*	*11 885*	*9 694*	*16 816*

[1] Provisional
Source: Bank of Greece.

succeeds in satisfying its new capital requirements by borrowing from the banks (which, as mentioned above, accumulate the bulk of short-term savings) at lower interest rates than would be required on the new issues market. Given the inflationary experience of Greece, the latter would demand relatively attractive rates, which could contribute further to increasing the national debt.

With regard to non-government bond issues, certain financial institutions—namely investment and mortgage banks—have been given the privilege of issuing short-term bonds which are offered to the public at attractive terms, including saisfactory interest rates, high liquidity and a stable par value. Under these circumstances, new corporate bond issues could not withstand the competition of the investment banks inasmuch as the latter are financed through the commercial banking system at relatively low cost. This is one of the main reasons why there have been no new bond issues by private non-financial enterprises since 1976.

(b) *The share market*

Table 1 indicates that it is the bank share market that has grown in the years 1978-80 with regard to new issues, while the corporate share market in new issues has been constantly decreasing since 1978. It is worth noting that though long-term credit to the private manufacturing sector amounted to DR 30 000 million at the end of 1982, the amount of new issues of corporate shares did not exceed DR 1 200 million for the same year. This is not the place for a thorough analysis of the factors accounting for this poor performance. None the less, some of the main factors can be summarized as follows:

(i) The institutional setting of the Greek banking system makes borrowing from it not only easily accessible but also possible at a low interest cost. Thus, private companies and especially the manufacturing sector have traditionally heavily depended on the banking system for loanable funds.

(ii) The predominance of small family-oriented units and the absence of incorporated enterprises coupled with the fear of relinquishing the control of family-owned concerns to the public militates against public share issues.

(iii) The sluggishness of private investment demand in recent years has cut down the general demand for capital.

Thus, the inadequate supply of new shares is a factor accounting for the low stage of development of the capital market, while some difficulties in the evolution of the primary market lie also on the demand side.

2.2.3. The secondary securities market

Though the new issue market of securities is more important in terms of economic growth and development, the secondary market, where transactions in outstanding securities take place, is also of considerable importance.

In Greece there is only one organized market, the Athens Stock Exchange (ASE), where stockbrokers can engage in securities transactions.

The Athens Stock Exchange is a semi-governmental institution which is controlled by the State. The trading which takes place in the Exchange covers government and public enterprises' bonds, the majority of the market shares of the financial institutions as well as securities of private non-financial enterprises.

Only some 110 companies are listed in the Athens Stock Exchange, compared with a total of approximately 2 500 existing companies with the legal form of *sociétés anonymes*. Only 24 out of the 100 biggest Greek companies were quoted on the Stock Exchange in 1982.

Table 2

Stock exchange transactions 1982

	Number of bond issues quoted	Million DR	
		Nominal value	Turnover
BONDS			
Categories			
Pre-World-War-II loans			
– Government bonds	17	5 980	54
– Corporation bonds	1	158	:
Post-war loans			
– Government bonds	11	9 189	335
– Public Power Corporation bonds	9	8 699	632
– Corporation bonds	5	255	1
– Short-term bank bonds	153	57 415	506
SHARES			
– Banks	14[1]	39 053	1 359
– Industrial	75[1]	22 272	955
– Commercial and insurance	21[1]	11 801	185

[1] Number of companies.
Source: Bank of Greece.

Although a great number of the non-listed companies are not qualified for quotation on the stock exchange—they need to have DR 100 million paid-up share capital as a minimum—the main reason for non-quotation is that shares are held by families or family-controlled corporations.

Nevertheless, due to the favourable new tax incentives for quoted companies (see Section 2.1.3), the total number of companies whose shares are listed on the stock exchange increased from 76 in 1967 to 110 at the end of 1982.

Table 2 indicates the volume of activity in the stock market for the year 1982.

Prices and the volume of stock exchange transactions fluctuate more or less irregularly but have been following a declining trend since 1978. The absence of regular issues of government bonds since 1972 and also those of private non-financial enterprises in the primary market, as outlined above, has limited the active role of the stock market. Only bank bonds and the new shares of banking institutions seem to be actively traded in the stock exchange. Bonds account for less than one quarter of the total volume of transactions as opposed to three quarters for (mainly bank) shares.

2.3. Factors accounting for the inadequate development of the capital market

Though the authorities have encouraged through legislation the development of the capital market, with tax incentives for listed companies, stockholders, capitalizing reserves, high dividend payments, etc., as described above, it appears that these measures have not brought about the desired effect. The capital market still remains underdeveloped and plays a limited role in mobilizing savings.

In addition to the factors listed in Sections 2.1.3 and 2.2, the following account for the inadequate development of the capital market:

(i) Public debt management is not a factor encouraging bond market activity since the government prefers borrowing in the form of compulsory investment in Treasury bills by banks to financing by means of bond issues to the private sector. The public almost never buys government bonds except those rare issues carrying premium on maturity.

(ii) In the money market, the Treasury bills market is still underdeveloped. Treasury bills transactions take place only between banks and the central bank.

(iii) The needs of the private sector for short-term securities and financing are supplied almost exclusively by the banking system. The absence of a developed capital market has shifted the demand which might be satisfied by money market instruments to savings and time deposits.

The existing institutional arrangements positively contribute to the process of disintermediation of the Greek oligopolistic banking system. In the Greek capital market there do not exist those types of institutions which could accumulate the savings of the public and use them subsequently for investment in the capital market.

2.4. Prospects for reform

Since the continuous and rational chanelling of funds for investment purposes is a prerequisite for maximizing the objectives of economic development and for efficient stabilization policies, a restructuring of the Greek banking system and development of the capital market is desirable.

In 1981, the Bank of Greece studied the question of restructuring the Greek financial system and capital market. Other studies recently issued by the Centre for Planning and Economic Research, Athens, Greece, also dealt with the financial system in a very detailed way and proposed restructuring both the financial system and the capital market.

Some possibilities for reform in the capital market which emerge from the studies conducted so far, as well as from the considerations set out in this note, are summarized below.

(i) The development of the money market, with the participation of a variety of financial institutions, would provide a more effective and flexible mechanism for raising capital. The range of short-term financial instruments could be enriched so as to include, among others, certificates of deposit, options, commercial paper, industrial acceptances, etc., which could be traded on the stock exchange.

(ii) Specialized agencies for the promotion of companies and the issue, underwriting and distribution of securities might be developed.

(iii) An 'over-the-counter' market in bonds might be encouraged, so that companies which do not enter the stock exchange, for whatever reason, would be able to raise capital and trade their stocks.

(iv) Interest rate policy on bank deposits should take into consideration the real rate of return on public bonds, with the ultimate objective of moving smoothly towards a market-determined interest rate structure.

(v) Investment of the surplus funds of insurance companies, social security organizations, pension funds, etc., in securities might be encouraged. This presupposes an adequate supply of new issues of securities as well as market-determined share prices.

(vi) Price indices for all types of securities should be published daily.

(vii) Non-residents might be encouraged to invest in the Greek securities market. (Note that all profits of EEC residents and company shareholders can be remitted abroad freely since 1981.)

(viii) An intervention policy might be developed which would smooth out fluctuations in security prices and stabilize investment expectations on the stock exchange.

(ix) The government, public entities and public enterprises should resort to the stock exchange for their own financing by issuing new bonds on a regular basis.

(x) Big, dynamic and well developed private companies which meet the requirements to enter the stock exchange should resort to the organized capital market for their long-term financing rather than borrow through the banking system. Their new issues of securities should be available for public subscription.

(xi) Over-borrowing through the banking system should be discouraged and a new policy might be adopted concerning the ratio of companies' own to total capital, so as to increase the financial soundness of companies quoted on the stock exchange.

(xii) A periodical compulsory re-estimation of the value of fixed assets of all companies listed on the stock exchange should be required.

(xiii) A stable tax policy should be pursued so as to encourage not only the entry of new companies in the stock exchange but also the trading volume of shares of those quoted.

List of contents of European Economy Nos 1 to 14

1. November 1978	— *Annual Economic Report 1978-79* — *Annual Economic Review 1978-79*
2. March 1979	— *European Monetary System* Texts of the European Council of 4 and 5 December 1978
3. July 1979	— *Short-term economic trends and prospects* — *The European Monetary System* Commentary Documents
4. November 1979	— *Annual Economic Report 1979-80* — *Annual Economic Review 1979-80*
5. March 1980	— *Short-term economic trends and prospects* — *Adaptation of working time*
6. July 1980	— *Short-term economic trends and prospects* — *Borrowing and lending instruments looked at in the context of the Community's financial instruments*
7. November 1980	— *Annual Economic Report 1980-81* — *Annual Economic Review 1980-81*
8. March 1981	— *Economic trends and prospects* — *The Community's borrowing and lending operations— recent developments*
9. July 1981	— *Fifth medium-term economic policy programme* — *The main medium-term issues: an analysis*
10. November 1981	— *Annual Economic Report 1981-82* — *Annual Economic Review 1981-82*
11. March 1982	— *Economic trends and prospects* — *Unit labour costs in manufacturing industry and in the whole economy*
12. July 1982	— *Documents relating to the European Monetary System*
13. September 1982	— *The borrowing and lending activities of the Community in 1981*
14. November 1982	— *Annual Economic Report 1982-83* — *Annual Economic Review 1982-83*
Special issue 1979	— *Changes in industrial structure in the European economies since the oil crisis 1973-78* — *Europe — its capacity to change in question!*

ORDER FORM

European Economy ISSN 0379-0991

Price annual subscription (3 issues per year):
ECU 19.64 / BFR 800 / IRL 13.50 / UKL 11.60 / USD 22.80

European Economy + Supplements A, B and C

Price combined annual subscription:
ECU 42.97 / BFR 1 750 / IRL 29.40 / UKL 25.50 / USD 50.00

Number of copies: ....

Name and address:

Date: .... Signature: ....

ORDER FORM

Supplements to 'European Economy'.

Series A — **Recent economic trends**
Price annual subscription (11 issues per year):
ECU 9.82 / BFR 400 / IRL 6.75 / UKL 5.80 / USD 11.50

Series B — **Economic prospects – business survey results**
Price annual subscription (11 issues per year):
ECU 9.82 / BFR 400 / IRL 6.75 / UKL 5.80 / USD 11.50

Series C — **Economic prospects – consumer survey results**
Price annual subscription (3 issues per year):
ECU 3.69 / BFR 150 / IRL 2.50 / UKL 2.20 / USD 4.20

Price all three supplements:
ECU 23.32 / BFR 950 / IRL 16.00 / UKL 13.80 / USD 27

Number of copies: ....

Name and address:

Date: .... Signature: ....

ORDER FORM

European Economy ISSN 0379-0991

Price annual subscription (3 issues per year):
ECU 19.64 / BFR 800 / IRL 13.50 / UKL 11.60 / USD 22.80

European Economy + Supplements A, B and C

Price combined annual subscription:
ECU 42.97 / BFR 1 750 / IRL 29.40 / UKL 25.50 / USD 50.00

Number of copies: ....

Name and address:

Date: .... Signature: ....

ORDER FORM
for European Economy and Supplements

Office des
publications officielles
des Communautés européennes

L-2985 **Luxembourg**

Office des
publications officielles
des Communautés européennes

L-2985 **Luxembourg**

Office des
publications officielles
des Communautés européennes

L-2985 **Luxembourg**

Salg og abonnement · Verkauf und Abonnement · Πωλήσεις καί συνδρομές · Sales and subscriptions Vente et abonnements · Vendita e abbonamenti · Verkoop en abonnementen

BELGIQUE / BELGIË

Moniteur belge / Belgisch Staatsblad
Rue de Louvain 40-42 / Leuvensestraat 40-42
1000 Bruxelles / 1000 Brussel
Tél. 512 00 26
CCP/Postrekening 000-2005502-27

Sous-agents / Agentschappen:

Librairie européenne / Europese Boekhandel
Rue de la Loi 244 / Wetstraat 244
1040 Bruxelles / 1040 Brussel

CREDOC
Rue de la Montagne 34 / Bergstraat 34
Bte 11 / Bus 11
1000 Bruxelles / 1000 Brussel

DANMARK

Schultz Forlag
Møntergade 21
1116 København K
Tlf: (01) 12 11 95
Girokonto 200 11 95

Underagentur:

Europa Bøger
Gammel Torv 6
Postbox 137
1004 København K
Tlf. (01) 15 62 73
Telex 19280 EUROIN DK

BR DEUTSCHLAND

Verlag Bundesanzeiger
Breite Straße
Postfach 10 80 06
5000 Köln 1
Tel. (02 21) 20 29-0
Fernschreiber:
ANZEIGER BONN 8 882 595

GREECE

G.C. Eleftheroudakis SA
International Bookstore
4 Nikis Street
Athens (126)
Tel. 322 63 23
Telex 219410 ELEF

Sub-agent for northern Greece:

Molho's Bookstore
The Business Bookshop
10 Tsimiski Street
Thessaloniki
Tel. 275 271
Telex 412885 LIMO

FRANCE

Service de vente en France des publications des Communautés européennes

Journal officiel
26, rue Desaix
75732 Paris Cedex 15
Tél. (1) 578 61 39

IRELAND

Government Publications Sales Office
GPO Arcade
Dublin 1

or by post

Stationery Office
Dublin 4
Tel. 78 96 44

ITALIA

Licosa Spa
Via Lamarmora, 45
Casella postale 552
50 121 Firenze
Tel. 57 97 51
Telex 570466 LICOSA I
CCP 343 509

Subagente:

Libreria scientifica Lucio de Biasio - AEIOU
Via Meravigli, 16
20 123 Milano
Tel. 80 76 79

GRAND-DUCHÉ DE LUXEMBOURG

Office des publications officielles des Communautés européennes
5, rue du Commerce
L-2985 Luxembourg
Tél. 49 00 81
Télex PUBLOF - Lu 1322
CCP 19190-81
CC bancaire BIL 8-109/6003/300

NEDERLAND

Staatsdrukkerij- en uitgeverijbedrijf
Christoffel Plantijnstraat
Postbus 20014
2500 EA 's-Gravenhage
Tel. (070) 78 99 11

UNITED KINGDOM

HM Stationery Office
PO Box 569
London SE1 9NH
Tel. 01-928 6977 ext 365
National Giro Account 582-1002

Sub-agent:

Alan Armstrong & Associates
Sussex Place, Regent's Park
London NW1 4SA
Tel. 01-723 3902

ESPAÑA

Mundi-Prensa Libros, S.A.
Castelló 37
Madrid 1
Tel. (91) 275 46 55
Telex 49370-MPLI-E

PORTUGAL

Livraria Bertrand, s.a.r.l.
Rua João de Deus
Venda Nova
Amadora
Tél. 97 45 71
Télex 12709-LITRAN-P

SCHWEIZ / SUISSE / SVIZZERA

FOMA
5, avenue de Longemalle
Case postale 367
CH 1020 Renens - Lausanne
Tél. (021) 35 13 61
Télex 25416

Sous-agent:

Librairie Payot
6, rue Grenus
1211 Genève
Tél. 31 89 50
CCP 12-236

SVERIGE

Librairie C.E. Fritzes
Regeringsgatan 12
Box 16356
103 27 Stockholm
Tel. 08-23 89 00

UNITED STATES OF AMERICA

European Community Information Service
2100 M Street, NW
Suite 707
Washington, DC 20037
Tel. (202) 862 9500

CANADA

Renouf Publishing Co., Ltd
2182 St Catherine Street West
Montreal
Quebec H3H 1M7
Tel. (514) 937 3519

JAPAN

Kinokuniya Company Ltd.
17-7 Shinjuku 3-Chome
Shiniuku-ku
Tokyo 160-91
Tel. (03) 354 0131

Price (excluding VAT) in Luxembourg

	ECU	BFR	IRL	UKL	USD
'European Economy' (4 issues per year)	19.64	800	13.50	11.60	22.80
Supplements					
Series A — 'Recent economic trends' (11 issues per year)	9.82	400	6.75	5.80	11.50
Series B — 'Business survey results' (11 issues per year)	9.82	400	6.75	5.80	11.50
Series C — 'Consumer survey results' (3 issues per year)	3.69	150	2.50	2.20	4.20
All three supplements	23.32	950	16.00	13.80	27.00
Combined subscription — 'European Economy' and supplements	42.97	1 750	29.40	25.50	50.00

The annual subscription runs from 1 January to 31 December of each year.

Prices for single copies may be obtained from the sales offices.

These are surface mail rates; for air subscription rates please apply to the sales offices.

OFFICE FOR OFFICIAL PUBLICATIONS
OF THE EUROPEAN COMMUNITIES

L-2985 Luxembourg

CB-AR-83-015-EN-C